

SFC resolves compliance concerns with Cheong Lee Securities Limited

9 Jan 2014

The Securities and Futures Commission (SFC) has resolved its compliance concerns with Cheong Lee Securities Limited (Cheong Lee) (Note 1). Under the resolution, the SFC reprimands and fines Cheong Lee \$2 million for internal control failures relating to self-matching transactions in breach of the SFC's Code of Conduct (Note 2).

An SFC investigation into Cheong Lee's client securities trading activities revealed that Cheong Lee allowed its clients to adopt a master account and sub-accounts structure. During the period from December 2008 to November 2011, more than 1,500 transactions were identified to be traded between the sub-accounts operated by different traders for the same master account.

The SFC found that Cheong Lee failed to put in place effective internal control procedures to detect and prevent self-matching transactions between the sub-accounts which the SFC considers not to be in the best interest of market integrity.

In deciding the disciplinary sanction, the SFC took into account all relevant circumstances of the case, including:

- adequate and effective internal control systems are fundamental to the fitness and properness of a licensed corporation;
- Cheong Lee's failures lasted for more than three years;
- Cheong Lee has a clean disciplinary record; and
- Cheong Lee co-operated in resolving these disciplinary proceedings.

End

Notes:

1. Cheong Lee is licensed under the Securities and Futures Ordinance to carry on business in Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities) and Type 5 (advising on futures contracts) regulated activities.
2. Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission
3. A copy of the [Statement of Disciplinary Action](#) in relation to the matter is available on the SFC website.

Page last updated : 9 Jan 2014

STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (SFC) has taken the following disciplinary action against Cheong Lee Securities Limited (**Cheong Lee**) pursuant to section 194 of the Securities and Futures Ordinance (**SFO**):
 - (a) publicly reprimanded Cheong Lee, pursuant to section 194(1)(b)(iii) of the SFO; and
 - (b) imposed a financial penalty of HK\$2 million on Cheong Lee, pursuant to section 194(2)(b) of the SFO.
2. Cheong Lee failed to put in place effective system and control procedures to detect and prevent the execution on the exchange securities trades that were self-matching in the same account.
3. The failure constitutes a breach of General Principle 2 (Diligence) of the Code of Conduct for Persons Licensed by or Registered with the SFC.

Summary of facts

4. In December 2008, Cheong Lee was advised by the SFC that it should have adequate and effective internal control systems in place to prevent self-matching of orders from the same clients.
5. In July 2011, the SFC found that Chong Lee allowed its clients to adopt a master account and sub-accounts structure, under which the account holder maintained multiple sub-accounts and authorized traders to give trading instructions for each of the sub-accounts. The trading activities among the sub-accounts resulted in self-matching trades.
6. Chong Lee said it had taken steps to prevent and detect the self-matching trades, including reviewing the self-matching trades, monitoring the orders from the sub-accounts, warning the relevant clients, and launching a new Broker Supplied System (**BSS**).
7. These steps are clearly insufficient and ineffective not only because there were over 1,500 self-matching trades during the period from December 2008 to November 2011 but also:
 - (a) the reviews:
 - (i) on average failed to identify 30% of the self-matching trades; and
 - (ii) failed to satisfactorily explain why the self-matching trades occurred;

- (b) the monitoring only involved eye-ball checking the client orders which was prone to mistakes and omissions;
- (c) no action was taken despite repeated warnings were given to clients; and
- (d) the BSS which can identify self-matching trades were launched only in June 2012.

Breaches and reasons

8. As a licensed corporation, Cheong Lee is under a duty to act in the best interest of market integrity. Cheong Lee should therefore implement adequate system and controls to prevent and detect trading irregularities, including self-matching trades, which were executed at the same price and of the same quantity, for the same master account.
9. In the circumstances, the SFC considers that Cheong Lee has failed to exercise due skill, care and diligence to ensure the regulated activities it carried on as a business were in the best interest of market integrity. The self-matching trades are not in the interest of market integrity given they are of no economic value and will result in an inflation of market turnover.

Conclusion

10. Having considered all the circumstances, the SFC has decided that the sanction of public reprimand and fine of HK\$2 million is the most appropriate and commensurate with the view of the SFC on the gravity of the failures.