

## SFC reprimands and fines Guotai Junan Securities (Hong Kong) Limited \$1.3 million

30 May 2016

The Securities and Futures Commission (SFC) has reprimanded and fined Guotai Junan Securities (Hong Kong) Limited (Guotai Junan) \$1.3 million for non-compliance with the regulatory requirements in relation to ascertaining client identity (Note 1).

In July 2014, the SFC requested Guotai Junan to provide details of the ultimate clients of certain transactions it effected for an intermediary client in Korea. Guotai Junan was unable to provide the requested information within two business days of the request pursuant to the Client Identity Rule Policy, due to the intermediary client's failure to comply with its obligation under its client agreement (Notes 2 & 3).

The intermediary client informed the SFC and Guotai Junan on 1 August 2014 that as a matter of Korean law, it could not provide the requested client identity information without its clients' written consent. It was not until January 2015 that Guotai Junan provided the requested information to the SFC.

Notwithstanding this, Guotai Junan continued to effect more than 8,000 transactions for the intermediary client between August 2014 and January 2015 despite having been reminded by the SFC of its obligation to refuse the business of those who are not prepared to provide ultimate client information to the regulators.

In the circumstances, the SFC found that at the time when Guotai Junan effected those transactions, it could no longer be satisfied on reasonable grounds that it would be able to make available the ultimate client information in relation to such transactions to the SFC on request, which is in contravention of the Client Identity Rule Policy (Note 4).

In deciding the sanctions, the SFC took into account all relevant circumstances, including, Guotai Junan:

- co-operated with the SFC in resolving the disciplinary proceedings; and
- has agreed to conduct an independent review of its systems and controls in respect of its compliance with the regulatory requirements on ascertaining client identity.

End

Notes:

1. Guotai Junan is licensed under the Securities and Futures Ordinance (SFO) to carry on Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities.
2. The Client Identity Rule Policy explains the client identity rule, paragraph 5.4 of the Code of Conduct for Persons Licensed by or Registered with the SFC, and the general approach the SFC will take in enforcing the client identity rule.
3. Under its client agreement with Guotai Junan, the intermediary client: (a) agreed to provide ultimate client information to the SFC, the Stock Exchange of Hong Kong and/or the Hong Kong Futures Exchange (the Regulators), within two business days of a request; and (b) confirmed that they and their clients have waived the benefit of any law which prohibited the provision of ultimate client information to the Regulators.
4. The Client Identity Rule Policy stipulates that a licensed person must refuse the business of those who are not prepared to provide client identity information to the Regulators upon request (paragraph 23). The Client Identity Rule also stipulates that if a licensed person has been put on notice that some intermediary in the chain of intermediaries involved in a transaction might not comply with its agreement in relation to that transaction so that the licensed person could no longer be satisfied on reasonable grounds that the information would be available to the Regulators on request and continued to deal with that intermediary, the SFC would consider taking disciplinary action against the licensed person (paragraph 27).

[A copy of the Statement of Disciplinary Action is available on the SFC website](#)

## STATEMENT OF DISCIPLINARY ACTION

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### The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded Guotai Junan Securities (Hong Kong) Limited (**Guotai Junan**) and fined it \$1,300,000 pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. The disciplinary action is taken for Guotai Junan's non-compliance with the regulatory requirements in relation to ascertaining client identity, in breach of General Principle 2 (Diligence) and paragraph 5.4 (Client identity) of the Code of Conduct<sup>1</sup>. Guotai Junan's conduct also fell short of the requirements explained in the Client Identity Rule Policy<sup>2</sup> (**CIR**).

### The Client Identity Rule

3. In conducting its business activities, Guotai Junan is required under General Principle 2 of the Code of Conduct to act with due skill, care and diligence, and in the best interests of its clients and market integrity.
4. With respect to information about client identity, paragraph 5.4 of the Code of Conduct provides that, before effecting a transaction for its client, a licensed corporation should be satisfied on reasonable grounds about the identity, address and contact details of the person / entity ultimately responsible for and benefit from the transaction, so that it can make available the information of the ultimate client to the SFC.
5. The CIR explains the client identity rule, paragraph 5.4 of the Code of Conduct, and the general approach the SFC will take in enforcing the client identity rule. Salient points in the CIR include:
  - (a) A licensed person should provide client identity information within two business days upon a request from the SFC and/or the exchanges (the **Regulators**).
  - (b) The SFC will not specify any particular way to comply with the client identity rule so long as a licensed person has systems in place to ensure that client information can be provided within two business days of the request. One method is by using an agreement whereby the licensed person's client would agree to provide the details of the ultimate beneficiary and of the person originating the instruction for a transaction directly to the Regulators on request.
  - (c) A licensed person *must* refuse the business of those who are not prepared to provide client identity information to the Regulators within two business days of a request.

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<sup>1</sup> Code of Conduct for Persons Licensed by or Registered with the SFC.

<sup>2</sup> The CIR was issued by the SFC on 28 February 2003 under the SFO.

- (d) If a licensed person has been put on notice that some intermediary in the chain of intermediaries involved in a transaction might not comply with its agreement in relation to that transaction so that the licensed person could no longer be satisfied on reasonable grounds that the information would be available to the Regulators on request (e.g., if a licensed person became aware that an intermediary had breached its agreements in the past) and continued to deal with that intermediary, the SFC would consider taking disciplinary action against the licensed person.

### **Summary of facts**

6. On 7 July 2014, the SFC requested Guotai Junan to provide ultimate client information in respect of a number of transactions in the shares of a company (**Transactions**) listed on the Stock Exchange of Hong Kong (**SEHK**).
7. On 10 July 2014, Guotai Junan informed the SFC that the Transactions were executed by Guotai Junan for an intermediary client (**Client**).
8. The Client is a broker in Korea and has indicated in its account opening form (**Client Agreement**) that the beneficial owner of the account is its retail clients. Under the Client Agreement, the Client:
  - (a) agreed to provide ultimate client information to the Regulators within two business days of a request by the Regulators; and
  - (b) confirmed that they and their clients have waived the benefit of any law which prohibited the provision of ultimate client information to the Regulators.
9. On 11 July 2014, the SFC granted consent for Guotai Junan to disclose the SFC's request to the Client, so that it could request the Client to provide the ultimate client information to the SFC. On 14 July 2014, Guotai Junan sent a request to the Client for details of the ultimate client(s).
10. The SFC informed Guotai Junan on 21 July 2014 that it had not received the ultimate client information from the Client. The SFC requested Guotai Junan to explain whether it had an agreement in place with the Client regarding the provision of ultimate client information upon request from the Regulators, and what steps it would take if the SFC did not receive the information from the Client.
11. On 23 July 2014, Guotai Junan informed the SFC that there is a provision in the Client Agreement requiring the Client to provide ultimate client information to the SFC within two business days upon request, and suggested that the SFC sought the assistance of the regulator in Korea if it did not receive the information from the Client.
12. On the same day, the SFC reminded Guotai Junan of its obligation to refuse the business of those who are not prepared to provide the ultimate client information to the Regulators within two business days of a request. The SFC also asked Guotai Junan to confirm whether it had refused business from the Client. Guotai Junan did not respond to the SFC's question.

13. On 1 August 2014, the Client informed the SFC and Guotai Junan that as a matter of Korean law, it could not provide the requested client identity information without the clients' written consent. The Client maintained this position in its communications with the SFC and Guotai Junan in the subsequent months.
14. The requested client information was eventually only provided on 12 January 2015, more than six months after the SFC's request. Guotai Junan continued to effect transactions for the Client pending its provision of the requested client information. More than 8,000 transactions were effected for the Client between 1 August 2014 and 12 January 2015.

### **Reasons for action**

15. Although the Client had agreed in the Client Agreement to provide ultimate client information to the Regulators within two business days of a request, by 21 July 2014, Guotai Junan was made aware that the Client had breached that agreement vis-à-vis the SFC's request for ultimate client information with respect to the Transactions (see paragraph 10 above).
16. Further, although the Client had confirmed in the Client Agreement that they and their clients have waived the benefit of any law which prohibited the provision of ultimate client information to the Regulators, by 1 August 2014, Guotai Junan was made aware that the Client took the position that it was prohibited by Korean law from providing the requisite client information to the SFC without client consent (see paragraph 13 above).
17. Therefore, by 1 August 2014, Guotai Junan must have known that the Client might not comply with its obligation under the Client Agreement to make available its ultimate client identity information to the SFC. This means that with respect to transactions effected for the Client after 1 August 2014, Guotai Junan could not be satisfied on reasonable grounds at the time of those transactions that it would be able to provide client identity information of the Client's ultimate clients in due time (i.e. within two business days of a request by the Regulators).

### **Conclusion**

18. The SFC has decided to take the disciplinary action against Guotai Junan as described in paragraph 1 above, after taking into account all relevant considerations, including:
  - (a) Guotai Junan's failure could jeopardize the integrity of the market as it might hinder the SFC from ascertaining the identities of those responsible for and/or who benefit from securities transactions, which is important for the prevention and identification of potential market misconduct;
  - (b) Guotai Junan's conduct was deliberate in that it did not suspend the transactions for the Client, even though it was put on notice that the Client was not prepared to provide the requested client identity information to the SFC and/or to comply with its obligations under the Client Agreement;
  - (c) the number of transactions executed by Guotai Junan for the Client after 1 August 2014;

- (d) Guotai Junan's co-operation in resolving the SFC's concerns; and
- (e) Guotai Junan has agreed to engage an independent reviewer, to be approved by the SFC, to review its systems and processes in respect of its compliance with the regulatory requirements in relation to ascertaining client identity.