

SFC reprimands and fines iSTAR International Futures Co. Limited \$3 million over anti-money laundering-related internal control failures

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The Securities and Futures Commission (SFC) has reprimanded iSTAR International Futures Co. Limited, now known as Rifa Futures Limited (Rifa), and fined it \$3 million over failures to comply with anti-money laundering regulatory requirements when processing third party fund transfers (Note 1).

An SFC investigation found that between January and July 2014, Rifa took insufficient steps to mitigate the risk of money laundering when handling third party deposits and transfers by failing to:

- obtain proper written instructions from clients and verify the identity of third parties before effecting third party deposits on numerous occasions (Note 2);
- make sufficient enquiries concerning third party deposits and maintain proper records of the findings (Note 3);
- ensure that the approval process in respect of third party deposits was effective;
- provide adequate anti-money laundering training to its staff; and
- put in place an appropriate and effective compliance function.

The SFC considers that Rifa's conduct was in breach of its obligation to take all reasonable measures to ensure that proper safeguards exist to guard against the risks of money laundering and terrorist financing associated with third party fund transfers, including making appropriate enquiries to ensure third party fund transfers are consistent with the customers' known legitimate activities, maintaining records of such enquiries, and effective implementation of internal policies for the prevention of money laundering and terrorist financing and communication of such policies to staff members.

The SFC further found that Rifa breached the Securities and Futures (Client Money) Rules on one occasion by effecting a payment from a client's account to the account of one of its responsible officers (Note 4).

In deciding the disciplinary sanction, the SFC took into account that Rifa:

- has since taken action to remediate its internal control deficiencies;
- cooperated with the SFC in resolving the disciplinary proceedings;
- agreed to engage an independent reviewer to conduct a review of its internal controls; and
- has an otherwise clean disciplinary record.

End

Notes:

1. Rifa is licensed under the Securities and Futures Ordinance (SFO) to carry on business in Type 2 (dealing in futures contracts) regulated activities.
2. Under paragraph 2 of the guidance note on Suggested Control Techniques and Procedures for Enhancing a Firm's Ability to Comply with the Securities and Futures (Client Securities) Rules and the Securities and Futures (Client Money) Rules, which was published under section 399 of the SFO in April 2003, a licensed corporation is required to ask its clients to give written instructions in all their dealings with the firm (except for trade instructions), which should bear the client's signature which the firm should in turn match against that appearing in the client's account opening documents kept in the firm's records. Where the instructions provide for acts by a third party on a client's behalf, a licensed corporation should verify the identity of the designated third party.
3. Under paragraphs 5.10 and 5.11 of the second edition of the Guideline on Anti-Money Laundering and Counter-Terrorist Financing, a licensed corporation is required to examine and make enquiries regarding the background, purpose and circumstances of transactions which are complex, large or unusual; the findings and outcomes of such examinations and enquiries should be properly documented in writing and be available to assist the relevant authorities.
4. Section 5(3) of the Securities and Futures (Client Money) Rules provides that a licensed corporation may not pay any client money to any of its employees unless that employee is the client on whose behalf such client money is being held.

5. Licensed corporations are reminded to refer to the "Circular to Licensed Corporations and Associated Entities – Anti-Money Laundering/Counter Financing of Terrorism (AML/CFT) Compliance with AML/CFT Requirements" issued by the SFC on [26 January 2017](#) which sets out key areas of concern identified by the SFC in its review of certain licensed corporations' AML/CFT systems.

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

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STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has taken the following disciplinary action against Rifa Futures Limited, formerly known as iSTAR International Futures Co. Limited (**Rifa**):
 - (a) publicly reprimanded Rifa, pursuant to section 194(1)(iii) of the Securities and Futures Ordinance (**SFO**); and
 - (b) imposed on Rifa a financial penalty of a total of \$3 million, pursuant to section 194(2) of the SFO.
2. The disciplinary action addresses Rifa's internal control deficiencies during the period between 1 January and 31 July 2014 (**Relevant Period**). Specifically, Rifa failed to:
 - (a) effectively enforce its internal policies and ensure compliance with regulatory requirements on third party deposits and transfers, as evidenced by the following:
 - (i) Rifa effected a number of third party deposits:
 - before proper written directions had been obtained from clients;
 - without making any enquiries notwithstanding that the deposits were inconsistent with the clients' profiles and/or information in the relevant account opening documents;
 - (ii) Rifa effected an internal transfer from a client to a responsible officer;
 - (iii) Rifa failed to maintain proper records to show that inquiries were made concerning third party deposits;
 - (iv) Rifa did not have in place an effective approval process in respect of third party deposits; and
 - (v) Rifa failed to provide adequate anti-money laundering (**AML**) training to its staff to ensure they knew what was required to be done to fulfil their roles with respect to AML when they handled third party deposits; and
 - (b) have in place an appropriate and effective compliance function.

Summary of regulatory requirements

3. Under the Guideline on Anti-Money Laundering and Counter-Terrorist Financing (**AML Guidelines**)¹:
- (a) a licensed corporation is required to take all reasonable measures to ensure that proper safeguards exist to mitigate the risks of money laundering and/or terrorist financing (**ML/TF**) (paragraph 2.1);
 - (b) the senior management of a licensed corporation should appoint firstly, a director or senior manager as a Compliance Officer (**CO**); and secondly, a senior member of the financial institution's (**FI's**) staff as the Money Laundering Reporting Officer (**MLRO**) (paragraph 2.11);
 - (c) a licensed corporation should ensure that its CO and MLRO are (i) of a sufficient level of seniority and authority; (ii) fully conversant in the licensed corporation's statutory and regulatory requirements and the ML/TF risks arising from its business; and (iii) equipped with sufficient resources (paragraph 2.12);
 - (d) the CO should assume responsibility for AML/counter financing of terrorism (**CFT**) systems of FIs (paragraph 2.13);
 - (e) a licensed corporation should make relevant enquiries of complex, large or unusual transactions and document such findings (paragraphs 5.10 and 5.11);
 - (f) a licensed corporation should ensure that the MLRO is of sufficient status within the organisation, and has adequate resources to perform his functions. The MLRO should play an active role in the identification and reporting of suspicious transactions. Also, a licensed corporation should possess procedures to ensure that all staff are made aware of the identity of the MLRO (paragraphs 7.20, 7.21 and 7.23);
 - (g) a licensed corporation should keep sufficient transaction records in respect of a customer that may be obtained for the purposes of enhanced due diligence (**EDD**) or ongoing monitoring (paragraphs 8.2 and 8.3);
 - (h) a licensed corporation should maintain records sufficient to permit reconstruction of individual transactions and establish a financial profile of any customer (paragraph 8.5); and
 - (i) a licensed corporation should provide sufficient AML/CFT training to its staff to maintain their AML/CFT knowledge and competence (paragraphs 9.2, 9.3 and 9.5).

¹ The AML Guidelines were published by the SFC under section 399 of the SFO and came into effect on 1 April 2012. The second edition of the AML Guidelines was published in July 2012 and remained effective up to 30 March 2015, i.e. it was applicable during the entire Relevant Period. The second edition of the AML Guidelines was superseded by the third edition published in April 2015, which was not yet in force during the Relevant Period. In this Statement of Disciplinary Action, all references to the AML Guidelines are to the second edition.

4. Under the “Circular to Licensed Corporations and Associated Entities – Anti Money Laundering/Counter Financing of Terrorism – Suspicious Transactions Monitoring and Reporting” published by the SFC on 3 December 2013 (**AML/CFT Circular**), a licensed corporation should, amongst other things:
 - (a) take reasonable steps to identify funds from third party sources;
 - (b) pay special attention to monitor any frequent and/or large third party funds transfers involving customers;
 - (c) undertake EDD and ongoing monitoring to mitigate the ML/TF risks especially where money is paid by a non-resident third party;
 - (d) conduct appropriate enquiries to ensure third party funds transfers are consistent with the customers’ known legitimate activities; and
 - (e) ensure sufficient guidance is given to staff to enable them to recognize suspicious transactions.
5. Under section 5(3) of the Securities and Futures (Client Money) Rules (**Client Money Rules**), a licensed corporation may not pay any client money to any of its officers or employees unless that officer or employee is the client on whose behalf such client money is being held.
6. The foreword of the guidance note on Suggested Control Techniques and Procedures for Enhancing a Firm’s Ability to Comply with the Securities and Futures (Client Securities) Rules and the Securities and Futures (Client Money) Rules (**Guidance Note on Suggested Control Techniques**)² provides that in considering whether a licensed corporation is fit and proper, the SFC may take into account whether the firm has established effective internal control procedures and risk management systems to ensure its compliance with the Client Money Rules and will be guided by the suggested control techniques and procedures set out in the Guidance Note on Suggested Control Techniques.
7. Under paragraph 2 of the Guidance Note on Suggested Control Techniques, a licensed corporation is required to ask its clients to give written instructions, which should bear the client’s signature matching that appearing in the client’s account opening documents; where the instructions provide for acts by a third party on a client’s behalf, a licensed corporation should verify the identity of the designated third party.
8. Under the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC (**Internal Control Guidelines**), the management of a licensed corporation is required to:
 - (a) assume full responsibility for the firm’s operations (Part I, paragraph 1);

² The Guidance Note on Suggested Control Techniques was published under section 399 of the SFO to provide guidance on internal control techniques and procedures that are generally expected of a licensed corporation in complying with the Securities and Futures (Client Securities) Rules and the Client Money Rules.

- (b) ensure that management and supervisory functions are performed by qualified and experienced individuals (Part I, paragraph 5);
 - (c) ensure that adequate and ongoing training is provided (Part III, paragraph 3); and
 - (d) establish and maintain an appropriate and effective compliance function and procedures and ensure that staff performing the compliance function possess the necessary skills, qualifications and experience (Part V, paragraphs 1, 2 and 4).
9. Under the Code of Conduct for Persons Licensed by or Registered with the SFC (**Code of Conduct**), a licensed corporation:
- (a) is required to act with due skill, care and diligence, in the best interests of its clients and the integrity of the market in conducting its business activities (GP 2);
 - (b) should have and employ effectively the resources and procedures which are needed for the proper performance of its business activities (GP 3);
 - (c) should comply with all regulatory requirements applicable to the conduct of its business activities so as to promote the best interests of clients and the integrity of the market (GP 7);
 - (d) should ensure that any person it employs or appoints to conduct business is fit and proper and otherwise qualified to act in the capacity so employed or appointed, including having relevant professional training or experience (paragraph 4.1);
 - (e) should ensure that it has adequate resources to supervise diligently and does supervise diligently persons employed or appointed by it to conduct business on its behalf (paragraph 4.2);
 - (f) should have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its operations, its clients and other licensed or registered persons from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or omissions (paragraph 4.3); and
 - (g) should comply with, and implement and maintain measures appropriate to ensuring compliance with the law, rules, regulations and codes administered or issued by the SFC and the requirements of any regulatory authority which apply to the licensed corporation (paragraph 12.1).
10. GP 9 of the Code of Conduct also provides that the senior management of a licensed corporation should bear primary responsibility for ensuring the maintenance of appropriate standards of conduct and adherence to proper procedures by the firm.

Summary of facts and breaches

Failure to enforce internal policies and/or comply with regulatory requirements on third party deposits and transfers

(a) Third party deposits effected in the absence of proper written instructions

11. During the Relevant Period, Rifa effected third party deposits before proper written directions had been obtained from clients in situations including the following:
 - neither the reason for deposit nor the relationship between the client and the third party was stated on the prescribed third party deposit notification form (18 transactions);
 - the prescribed third party deposit notification form had not been obtained at the time the deposit was accepted (4 transactions); and
 - identification document of the third party was unavailable (16 transactions).
12. In the above cases, the third party deposit was processed first and the client was allowed to provide the outstanding information later, which was contrary to Rifa's internal policies. Even when the missing information/document was not forthcoming, this was not diligently followed up.
13. Rifa's failure to obtain proper written directions for third party deposits in accordance with its internal policies was in breach of paragraphs 2.1 and 8.5 of the AML Guidelines, paragraph 2 of the Guidance Note on Suggested Control Techniques, Part I paragraphs 1 and 5 of the Internal Control Guidelines, and paragraphs 4.2 and 4.3 of the Code of Conduct.

(b) Third party deposits effected despite inconsistencies with client profile/information in account opening documents

14. Rifa processed and effected third party deposits despite inconsistencies with client profile/information in account opening documents. Firstly, client signature was clearly different from signatory specimen on account opening document. Secondly, discrepancies exist between declared net worth and deposit amounts. The situation was aggravated by the absence of documentary proof of clients' assets and records to show that EDD had been carried out in order to mitigate money laundering risks.
15. Rifa's failure in this regard was in breach of paragraphs 2.1, 5.10 and 5.11 of the AML Guidelines, the AML/CFT Circular, and paragraph 2 of the Guidance Note on Suggested Control Techniques.

(c) Internal transfer from client's account to employee's account

16. Rifa effected a payment of US\$200,000 from a client's account to the account of one of its responsible officers (**ROs**), who claimed that it was a repayment of a loan by him to the client. Such internal transfer was in breach of section 5(3) of the Client Money Rules.

(d) Failure to maintain proper records to show that inquiries were made concerning third party deposits

17. Rifa failed to record all client instructions concerning third party deposits. It did not take any steps to ensure that a recording line was used even though phone lines were equipped with a recording function and its staff were required by internal policy to record confirmation of third party deposits with clients. Hence only a few audio recordings exist in relation to clients' instructions regarding third party deposits. As such, it is unclear whether any inquiries were made at all in the majority of the cases where the requisite information/document was lacking.
18. Furthermore, neither the findings nor outcome of any AML checks, know-your-client (**KYC**) or EDD purportedly conducted have been documented. Consequently, there is no means of ascertaining the results of any enquiries made and whether KYC/EDD has in fact been performed.
19. Rifa's failure to maintain proper records was in breach of paragraphs 5.10, 5.11, 8.2, and 8.3 of the AML Guidelines.

(e) Failure to have in place an effective approval process in respect of third party deposits

20. The two ROs of Rifa both denied primary responsibility for approving third party deposits. Each of them assumed that the other person had scrutinized and approved the third party deposits when signing on the daily report thereby rendering their signatures as mere rubber stamps.
21. Further, one of the ROs made six deposits of substantial amounts into the accounts of various clients; received two substantial third party deposits in his trading account when he needed additional margin to trade but did not have sufficient funds; and accepted an internal transfer from a client of Rifa's for a purpose other than trading. The RO acted as the approver for these deposits. Although these transactions all gave the appearance of impropriety, no proper reason was provided.
22. In light of the deficient approval process, Rifa was unable to ensure compliance with the relevant internal policies and regulatory requirements when handling third party deposits.
23. Rifa's failure to have in place an effective approval process in respect of third party deposits was in breach of GP9 of the Code of Conduct.

(f) Failure to provide adequate AML training

24. Rifa did not provide regular AML training to its staff and even then, such training was not compulsory. Neither was there sufficient guidance on identifying suspicious transactions. Staff members were left in the dark as to the criteria for approval of third party deposits. As a result, the overall AML awareness among Rifa's staff members was low.
25. Rifa's failure to provide adequate AML training to its staff was in breach of paragraphs 9.2, 9.3 and 9.5 of the AML Guidelines, the AML/CFT Circular, Part III paragraph 3 of the Internal Control Guidelines and GP3 of the Code of Conduct.

Lack of compliance function

26. The above internal control deficiencies reflect the inadequacy of Rifa's compliance function during the Relevant Period.
27. In particular, between February and August 2014, Rifa appointed its then administration and human resources manager as a temporary CO and MLRO under the AML Guidelines as qualified staff could not successfully be recruited at that period. As she was neither qualified nor did she possess relevant expertise for the role, she admitted to having minimal involvement in compliance as well as AML-related matters. Some of Rifa's staff did not even know that she was the CO and MLRO at the material time.
28. Rifa did not have an appropriate and effective compliance function, thereby breaching paragraphs 2.11, 2.12, 2.13, 7.20, 7.21 and 7.23 of the AML Guidelines, Part I paragraph 5 and Part V paragraphs 1, 2 and 4 of the Internal Control Guidelines, and paragraph 4.1 of the Code of Conduct.
29. In light of the matters set out in paragraphs 11 to 28, the SFC further considers that Rifa has breached GP 2, GP 7 and paragraph 12.1 of the Code of Conduct.

Conclusion

30. Having considered all relevant circumstances, the SFC is of the opinion that Rifa has been guilty of misconduct, and its internal control failures set out above have called into question its fitness and propriety to remain a licensed corporation.
31. A breakdown of the fine in paragraph 1(b) is as follows:
 - (a) \$2 million for the failures of Rifa as summarised in paragraph 2(a) above; and
 - (b) \$1 million for the failures of Rifa as summarised in paragraph 2(b) above.
32. In deciding the disciplinary sanction set out in paragraph 1, the SFC has had regard to its Disciplinary Fining Guidelines and has taken into account all relevant circumstances, including:
 - (a) Rifa has taken steps to remediate the internal control deficiencies identified since these matters were brought to light;
 - (b) there was a change in the management of Rifa subsequent to the Relevant Period;
 - (c) Rifa co-operated with the SFC in resolving the disciplinary proceedings;
 - (d) Rifa agreed to engage an independent reviewer to conduct a review of its internal controls and systems in relation to AML/CFT and the handling of third party deposits; and
 - (e) Rifa has no disciplinary history with the SFC.