

## SFC reprimands and fines The Royal Bank of Scotland PLC \$6 million for internal control failings

22 Apr 2014

The Securities and Futures Commission (SFC) has issued a reprimand to The Royal Bank of Scotland Public Limited Company (RBS) and fined it \$6 million for internal control failures relating to the detection and prevention of unauthorized trading activities and the conduct of its Emerging Markets Rates business in Hong Kong (Notes 1 & 2).

The action follows an SFC investigation into the systems and controls around RBS's Emerging Markets Rates Desk in 2011 following the discovery of unauthorized trading activities by one of its traders, Ms Shirлина Tsang Pui Yu (Note 3).

On 15 October 2011 which was a Saturday, RBS contacted the SFC on an urgent basis to report its concerns about unauthorized trading activities by Tsang, who worked on its Emerging Markets Rates Desk in its Hong Kong branch.

At the time of the self-report, RBS had discovered anomalies in Tsang's trading but did not yet know their scale or the size of any losses. It was later found that Tsang's unauthorized trading and mis-marking activities, which had taken place over a three-year period, caused substantial losses to RBS totaling GBP24.4 million. Tsang concealed the losses by mis-marking her bond positions and booking, cancelling and amending fictitious bonds and futures trades in RBS's internal systems.

While Tsang's misconduct is the primary cause of the losses to RBS, the SFC considers RBS's risk management and controls over its Emerging Markets Rates Desk were deficient and failed to prevent misconduct like Tsang's. In particular, the SFC investigation found:

- inadequate and ineffective front office supervision;
- an absence of controls over the process for independent price verification to mitigate the risk of inaccurate marking by traders of their positions, which had allowed Tsang to collude with RBS's pricing sources to manipulate prices in her favour;
- weak reconciliation process which Tsang exploited to conceal her unauthorized trading (Note 4);
- RBS required traders to mark their positions to market value every day but when Tsang took leave in 2008, 2009 and 2010, her positions were not covered by anyone else resulting in her positions not being independently marked during these periods (Note 5);
- the computerised system used by RBS to store block leave information failed to "lock out" Tsang from her RBS computer account and prevent her from accessing RBS applications while on block leave;
- a lack of processes to monitor trades conducted outside RBS's office and/or outside normal business hours via remote access i.e., a remote connection to RBS's internal systems;
- the management information provided to the front office for supervision purposes was unclear and/or inadequate making it difficult for supervisors to detect and question anomalies; and
- there was no training provided to front office in relation to RBS's front office supervisory policy and to employees who were promoted to supervisory roles as to their responsibilities which created inconsistent standards of supervision in the front office.

RBS's systems and controls in relation to its Emerging Markets Rates business were seriously inadequate and revealed significant weaknesses in its procedures, management systems and internal controls.

"RBS acted quickly in alerting the SFC on a Saturday afternoon which in turn led to action being taken that prevented Tsang from leaving Hong Kong. This deserves substantial credit and is the reason why today's sanctions are not heavier ones," said Mr Mark Steward, the SFC's Executive Director of Enforcement. "The SFC expects firms to report misconduct concerns immediately, as in this case."

In deciding the disciplinary sanction, the SFC took into account all relevant circumstances, including RBS's full co-operation with the SFC's investigation, no loss to customers, RBS's clean disciplinary record and its implementation of new governance structures, including front office supervision and new controls over operations, information technology, remote access, business unit control, group internal audit, compliance, block leave and trading books.

End

Notes:

1. RBS is a registered institution under the Securities and Futures Ordinance to carry on Type 1 (dealing in securities), Type 4 (advising on securities) and Type 6 (advising on corporate finance) regulated activities.
2. RBS's Fixed Income, Currency and Commodities in Asia Pacific (FICC APAC) operated a number of businesses in Asia Pacific which includes the Emerging Markets business. The Emerging Markets business was the second largest business in its FICC APAC and had four distinct trading desks, one of which was Rates.
3. On 30 August 2013, Tsang was convicted of one count of fraud and sentenced to four years and two months' imprisonment. Please see the Reasons for Sentence (DCCC326/2013) which is available on the Judiciary's website ([www.judiciary.gov.hk](http://www.judiciary.gov.hk)).
4. RBS extracted the relevant trading data for the reconciliation process from its systems at different points in time which created timing gaps. This was manipulated by Tsang to bypass the process. Tsang's explanations concerning "breaks" identified in her books arising from the reconciliation process were accepted by RBS without adequate investigation or challenge.
5. RBS's block leave policy required employees to take at least 14 consecutive calendar days of leave each year in a block (including public holidays). When on block leave, employees were prohibited from, among other things, effecting transactions, altering official bank records, conducting or influencing business critical activities via telephone or emails or remote access. RBS also required traders to mark their positions to market value every day and, when a trader was on block leave, that trader's positions must be covered and re-marked by another trader daily.
6. A copy of the [Statement of Disciplinary Action](#) in relation to the matter is available on the SFC website.

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## 蘇格蘭皇家銀行有限公司因內部監控缺失遭證監會譴責及罰款600萬元

2014年4月22日

蘇格蘭皇家銀行有限公司（蘇格蘭皇家銀行）因在偵察和防止未經授權的交易活動及在香港進行其新興市場利率業務時犯了內部監控缺失，遭證券及期貨事務監察委員會（證監會）譴責及罰款600萬元（註1及2）。

證監會在蘇格蘭皇家銀行發現其交易員曾佩瑜（女）進行未經授權的交易活動後，於2011年就其新興市場利率部門的系統及監控進行調查，並決定採取上述行動（註3）。

2011年10月15日星期六，蘇格蘭皇家銀行緊急聯絡證監會，就注意到曾進行未經授權的交易活動一事作出舉報。曾在蘇格蘭皇家銀行香港分行的新興市場利率部門工作。

蘇格蘭皇家銀行主動作出舉報時，發現曾的交易中有異常情況，但未知情況有多嚴重或是否有任何損失和損失的程度。其後發現，曾進行的未經授權交易及虛報價值的行為已持續三年，令蘇格蘭皇家銀行招致合共2,440萬英鎊的重大損失。曾在蘇格蘭皇家銀行的內部系統內就其債券持倉虛報價值、就虛構的債券及期貨買賣入帳，並取消及更改有關買賣，藉以隱瞞上述損失。

雖然曾的失當行為是導致蘇格蘭皇家銀行蒙受損失的主因，但證監會認為蘇格蘭皇家銀行新興市場利率部門的風險管理及監控有所不足，及未能阻止類似曾所犯的失當行為發生。具體而言，證監會的調查發現：

- 蘇格蘭皇家銀行對前線辦公室的監督不足且並不奏效；
- 對獨立價格核實程序缺乏監控，以致難以減低交易員不準確地就其持倉計值的風險，令曾可串謀蘇格蘭皇家銀行的定價來源以對自己有利的方式操控價格；
- 曾利用鬆懈的對帳程序隱瞞其未經授權的交易（註4）；
- 蘇格蘭皇家銀行規定交易員每日就其持倉按市價計值，但在2008年、2009年及2010年曾放假的期間，並沒有其他人代管其持倉，導致其持倉在這些期間沒有以獨立方式計值（註5）；
- 在曾放硬性年假期間，蘇格蘭皇家銀行用作儲存硬性年假資料的電腦系統未能將曾的蘇格蘭皇家銀行電腦帳戶置於“登出”狀態，亦未能阻止曾使用蘇格蘭皇家銀行的應用程式；
- 對經遙距接達（即與蘇格蘭皇家銀行的內部系統的遙距連接）在蘇格蘭皇家銀行辦公室以外及／或在非一般辦公時間進行的交易欠缺監察程序；
- 為監督目的而向前線辦公室提供的管理資料不清晰及／或不充足，令主管難以偵察異常情況及就異常情況提出質疑；及
- 沒有向前線辦公室提供有關蘇格蘭皇家銀行前線辦公室的監督政策的培訓，亦沒有向晉升至主管職位的僱員提供有關其職責的培訓，導致前線辦公室的監督標準不一。

蘇格蘭皇家銀行在其新興市場利率業務方面的系統及監控嚴重不足，反映其程序、管理系統及內部監控存在重大缺失。

證監會法規執行部執行董事施衛民先生（Mr Mark Steward）表示：“蘇格蘭皇家銀行迅速行動，在星期六下午向證監會作出舉報，本會方能採取行動阻止曾離開香港。蘇格蘭皇家銀行的做法值得表揚。正是這個原因，今天對蘇格蘭皇家銀行作出較輕的紀律處分。證監會希望商號都能像本個案般，就失當行為作出即時舉報。”

證監會決定上述紀律處分時，已考慮所有相關情況，包括蘇格蘭皇家銀行在調查期間與證監會充分合作、沒有對客戶造成損失、蘇格蘭皇家銀行並無遭受紀律處分的紀錄，以及蘇格蘭皇家銀行已執行新的管治架構，包括前線辦公室的監督，以及對運作、資訊科技、遙距接達、業務單位監控部、集團內部稽核、合規事宜、硬性年假及交易簿冊的監控。

完

備註：

1. 蘇格蘭皇家銀行是根據《證券及期貨條例》獲註冊的機構，獲准進行第1類（證券交易）、第4類（就證券提供意見）及第6類（就機構融資提供意見）受規管活動。
2. 蘇格蘭皇家銀行的亞太固定收入、貨幣及商品（（Fixed Income, Currency and Commodities in Asia Pacific）（FICC APAC））在亞太區經營多項業務，當中包括新興市場業務。新興市場業務是其FICC APAC中的第二大業務，擁有四個獨立的交易部門，其中一個是利率（Rates）部門。
3. 2013年8月30日，曾被裁定一項欺詐罪名成立及判處監禁四年零兩個月。請參閱司法機構網站（[www.judiciary.gov.hk](http://www.judiciary.gov.hk)）所載的《判刑理由書》（DCCC326/2013）。
4. 蘇格蘭皇家銀行為進行對帳程序，會於不同時段從其系統中抽取相關的交易數據，導致出現時間缺口。曾利用這些時間缺口規避有關程序。蘇格蘭皇家銀行未有就對帳程序而產生及從其簿冊發現的“缺漏”所提供的解釋，作出足夠調查或質疑，便加以接納。

5. 蘇格蘭皇家銀行的硬性年假政策規定，僱員每年須一次性地連續休假最少14個曆日（包括公眾假期）。凡僱員在放硬性年假時，除其他事項外，均不得執行交易、更改正式的銀行紀錄、透過電話或電郵或遙距接達進行或影響業務的重大活動。蘇格蘭皇家銀行亦規定交易員每天為其持倉按市價計值，若交易員放硬性年假，其持倉必須交由另一名交易員每天代管及重新計值。
6. 有關上述事宜的[紀律處分行動聲明](#)載於證監會網站。

最後更新日期：2014年4月22日

## STATEMENT OF DISCIPLINARY ACTION

### 1. The Disciplinary Action

- 1.1. The Securities and Futures Commission (**SFC**) has taken the following disciplinary action against The Royal Bank of Scotland Public Limited Company (**RBS**) pursuant to section 196 of the Securities and Futures Ordinance (**SFO**):
  - 1.1.1. Publicly reprimand RBS pursuant to section 196(1)(b)(ii) of the SFO.
  - 1.1.2. Impose a pecuniary penalty of HK\$6,000,000 on RBS pursuant to section 196(2) of the SFO.
- 1.2. The disciplinary action is taken for RBS's failure to implement adequate and effective systems and controls to detect and prevent unauthorised trading activities and the conduct of its Emerging Markets Rates business in Hong Kong from May 2008 to October 2011(the "Relevant Period").

### 2. Summary of Facts

- 2.1. On 15 October 2011, RBS self reported to the SFC serious irregularities in the trading books of one of its traders, Tsang Pui Yu Shirlina ("Tsang"). Tsang was a trader on the Emerging Market Rates desk in RBS's Hong Kong branch. After taking action to close out all RBS's positions relating to Tsang's unauthorised trading, the losses incurred by RBS were calculated at GBP 24.4 million (the "Loss").
- 2.2. RBS also reported the incident to the Hong Kong Monetary Authority ("HKMA") and the Hong Kong Police Department (the "Police"). On 17 October 2011, the Police arrested Tsang. On 30 August 2013, Tsang was convicted of one charge of fraud and subsequently sentenced to four years and two months imprisonment.
- 2.3. The Loss was caused by unauthorised activities conducted by Tsang during the Relevant Period. This includes mismarking of positions in Hong Kong Government debt instruments i.e. Hong Kong Government bonds, exchange funded notes and exchange funded bills, breaching futures trading limits and the mismarking of the HKD 1 month interest rate swap curve.
- 2.4. Tsang concealed her unauthorised activities from RBS's risk management systems and controls using the following methods.
  - 2.4.1. Manipulated the independent price verification ("IPV") process and influenced third party brokers to publish off market prices for the IPV process.
  - 2.4.2. Booked and cancelled fictitious bonds trades around IPV dates to circumvent RBS's valuation controls and conceal the variances in her positions.
  - 2.4.3. Cancelled and amended trades to conceal her unauthorised futures positions.

2.4.4. Mismarked the HKD swap curves.

- 2.5. The Emerging Markets Rates trading desk in the Hong Kong Branch was primarily managed and supervised from Singapore.
- 2.6. During the Relevant Period, RBS's internal systems and controls in relation to its Emerging Markets Rates business were seriously inadequate.

*Front office supervision and oversight*

- 2.7. In respect of supervision and oversight over individual traders by the Front Office, this was poorly executed and ineffective. The policy governing the supervisory framework and supervisory responsibilities was neither comprehensive nor clear. This led to supervisory gaps over Tsang as her supervisors did not sufficiently understand the extent of their supervisory responsibilities.
- 2.8. There were also no procedures or processes to encourage or reward its Front Office to self-identify issues and weaknesses. As such, there was little incentive for Front Office staff members to set and meet risk control objectives. This together with the absence of an unequivocal tone from RBS's senior regional management on strong controls contributed to the Front Office's primary focus on meeting revenue or other metric based targets.

*IPV control weaknesses*

- 2.9. Even though RBS had implemented an IPV control to mitigate the risk of inaccurate markings by traders of their positions, this was not effective despite being performed regularly twice a month.
- 2.10. The staff members in RBS responsible for carrying out the IPV process for Tsang's bonds positions did not have adequate knowledge and understanding of their roles. This led to them being unduly influenced by Tsang where they accepted her explanations of her bond prices without sufficiently challenging her or identifying issues for escalation.
- 2.11. RBS also did not have in place written policies or internal guidelines to determine the pricing hierarchies for the IPV process such as the selection of, and changes to, pricing sources and the minimum number of independent pricing sources that need to be obtained for a price to be verified. There were also no guidelines to monitor the independence of brokers and to ensure that they were truly independent from the traders. Had such guidelines been in place, this would have significantly undermined Tsang's ability to influence the third party brokers to provide quotes favourable to her for the IPV process.

*Block leave control weaknesses*

- 2.12. RBS's block leave controls<sup>1</sup> were inadequate in that there were no written guidelines or procedures on arrangement of cover during an employee's block leave nor on the adequacy and appropriateness of the cover. As a

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<sup>1</sup> Block leave was a control designed by RBS to ensure that a trader's positions were managed and valued by another trader daily over for a two week period at least once a year. During their block leave, traders were not permitted to effect transactions, alter official bank records, conduct or influence business activities via telephone or emails or remote access.

result, Tsang's bonds trading books were neither covered nor updated by another trader during her block leave in 2008, 2009 and 2010.

- 2.13. At the time of Tsang's block leave:
  - 2.13.1. In 2008, her bonds trading books were mismarked by about GBP 6.4 million.
  - 2.13.2. In 2009, her bonds trading books were mismarked by about GBP 5.34million.
  - 2.13.3. In 2010, her bonds trading books were mismarked by about GBP 11 million.
- 2.14. RBS's computer systems also failed to lock out Tsang from its applications during her block leave in 2009 and 2010. Tsang therefore accessed both her email account at RBS via remote access and engaged in Bloomberg chats during this period.
- 2.15. Furthermore, staff members in BUC did not know Tsang was on block leave or were not fully conversant with the rules associated with block leave as her interactions with them were neither challenged nor escalated to senior management.
- 2.16. There was also no management information or reports to show that Tsang's bonds positions had not been marked on a daily basis or the extent of her remote access activity during her block leave.

*Control failures with respect to futures reconciliation controls*

- 2.17. RBS's key futures reconciliation controls were not effective with discrepancies in the trading data not being adequately investigated. Between 1 August 2011 and 14 October 2011, there were 79 trade breaks revealed in Tsang's futures positions. A "trade" break was a discrepancy in trade positions between RBS's different systems in terms of either price or quantity or both. RBS did not adequately investigate these trade breaks and accepted Tsang's explanations without conducting further investigation or following up on how they were resolved. Furthermore, Tsang's line supervisor did not challenge the number or the nature of Tsang's trade breaks despite receiving a list of all trade breaks and accompanying explanations on a daily basis.

*Control failures with respect to the cancellation and amendment reporting for bonds and futures trades*

- 2.18. In respect of futures and bonds trades, RBS did not have any management information or reports on the level of cancellation and amendment activity for such trades prior to May 2011. Tsang's supervisors therefore had no effective means to identify and monitor such activities.
- 2.19. Subsequent to May 2011, RBS captured all post-trade cancellations including bonds and futures trade made by the Front Office in a cancellation and amendment report. However, the cancellation and amendment report was inadequate in that it did not capture pertinent information such as changes in counterparties and did not identify trends in cancellation and amendment

activities. The reports were also poorly designed and did not facilitate effective review and analysis.

*Inadequate monitoring of use of remote access*

- 2.20. RBS allowed traders to conduct trades away from the office and/or out of normal business hours via remote connection to its systems. From 15 April 2011 to 14 October 2011, Tsang logged onto RBS's systems 386 times via remote access, frequently between 6pm to midnight (Hong Kong time) and occasionally past midnight from 1am to 2am (Hong Kong time). However, there were no monitoring or reporting controls to capture Tsang's remote access use and therefore her trade cancellations and amendments in the early hours of the morning or late at night went undetected.

*Trading book controls*

- 2.21. RBS's controls for opening, closing, review and user access for its trading systems and trading books were inadequate in that it allowed, among other things, traders to access multiple trading books due to a "cloning" process whereby identical access is granted to a user by copying the profile assigned to another user. As a consequence, Tsang had access to and could book trades into over 1,600 trading books at RBS. The ability to clone books increased the risk of unauthorized trading being undetected.

*Training*

- 2.22. In respect of training, there was no clear framework and training curriculum for specific roles and supervisory responsibilities such as for the Front Office, new employees and employees promoted to supervisory roles. Instead, line managers adopted supervision methods which they had employed in previous jobs which led to inconsistencies in the standards of supervision. In addition, there was heavy reliance on line managers to determine relevant topics and to deliver on-the-job training.

**3. Conclusion**

- 3.1. Having regard to the extensiveness and prolonged nature of RBS's internal controls failings in its Emerging Markets Rates business and the risks that such failings posed to the SFC's regulatory objectives to protect the investing public, the SFC has decided to take the disciplinary action against RBS as described in paragraph 1.1. above.
- 3.2. In coming to the decision to take disciplinary action against RBS for its failures, the SFC has taken into account:
- 3.2.1. The serious deficiencies in RBS's internal controls and systems in its Emerging Markets Rates business.
  - 3.2.2. No losses were apparently suffered by RBS's clients or other third parties.
  - 3.2.3. RBS's prompt reporting of Tsang's conduct to the SFC and the Police which prevented Tsang from fleeing the jurisdiction.
  - 3.2.4. RBS's full co-operation with the SFC's investigation.



- 3.2.5. RBS has a clean disciplinary record.
- 3.2.6. The considerable resources (approximately HK\$96 million) expended by RBS to date in dealing with Tsang's unauthorised trading and mismarking activities.
- 3.2.7. The significant measures taken by RBS to remediate its internal control deficiencies.