

D. Some of the Supervisory Failures and/or Ineffective Compliance Function Cases where Enforcement Actions were Taken Against POs

Case D1: Supervisory lapses resulting in misconduct by employees

In 2008:-

❖ A fine of RM31,000 was imposed on a PO for the PO had failed to adhere to good business practice and to supervise the overall operations of its business activities and the activities of its employees resulting in misconducts by its employees and Registered Persons.

In this regard, the PO had, amongst others:-

- failed to ensure that the DR's user ID and passwords were not used by unauthorized persons to execute trades when the DR designated with the user ID was absent from the office;
- failed to monitor the whereabouts of its DRs or maintain proper attendance records;
- failed to put in place controls and processes to prevent unauthorized usage of user ID and passwords by unauthorized persons;

• allowed unlicensed persons to have access to dealing areas and carry out dealing activities and/or allowed unlawful delegation of DR's duties to unlicensed person(s); and

- failed to ensure registration of a trading clerk.

In 2013:-

- ❖ In 2013, a TP was imposed a private reprimand and fined RM5,000 for failing to ensure that its Registered Representative consistently voice logged his clients' trading instructions as required under the rules.

In this regard, it was noted that the compliance checks conducted by the TP (with random samples selected based on pre-determined dates and FBRs and checks were performed on the selected voice logging channels to determine whether clients' conversations were being recorded) were inadequate and flawed as it only allowed the TP to ascertain if the voice logging equipment worked. The TP's checks did not enable the TP to detect orders which were not placed through the voice logged dealing lines or were placed on a discretionary basis by FBRs. This failure by the TP had resulted in its Registered Representative being able to execute unauthorised trades which were not voice logged and operate a discretionary account through his client's account without his client's authorisation.

Case D2: Supervisory and internal control lapses resulting in multiple breaches

In 2009:-

- ❖ A fine of RM100,000 was imposed on a PO for insufficient level of supervision over the operations of its business activities and activities of its Registered Persons and ineffective compliance functions, based on, amongst others, the following inspection findings:-

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- (a) Trades for proprietary account were executed by staff other than the designated DR; proprietary trading were conducted on securities which were included in the 'Restricted List'¹ and the proprietary trading were carried out without prior approval by the PO's Executive Committee (EXCO), in contravention of the PO's formulated policies and procedures (P&P).
- (b) The PO's compliance department failed to discharge its duties in a reasonable manner, by omitting to carry out reviews on areas required under the rules as well as those planned by it (e.g. Corporate Finance (CF) activities, activities of its DRs, employees' transactions at its branch office, proprietary trading) and there was no compliance review carried out at its branch offices for certain periods.
- (c) Despite having established the relevant procedures and formulated a compliance review programme for carrying out review on its DRs as part of the monthly compliance review activities, no review was done on activities of DRs including their presence and activities in the office, their compliance with the requirements on no sharing of user IDs and passwords/DRs did not leave their BFE terminals unattended without temporary logging off.
- (d) The PO failed to inform and/or seek approval of Bursa on issues relating to its compliance personnel and registration (i.e., registration requirements of its Head of Compliance) which essentially related to governance issues.
- (e) The PO and/or its employees had engaged in activities or committed acts or omissions that could give rise to potential conflicts of interest. For instance, trading in securities listed under the Restricted List, publication of research material with comments and recommendations made by its Research Department on securities listed under the Restricted List and no Register for conflicts of interest (whether actual, potential or perceived) was maintained.

In 2012:-

- ❖ A PO was imposed a public reprimand and total fine of RM297,500 for (the Breaches):-
 - (a) there were supervisory/internal control lapses/weaknesses with regard to the discharge of compliance function (Supervisory Breaches). The review of the PO's overall compliance supervisory function showed that the extent of compliance reviews were inadequate and there were lapses in its compliance monitoring in the following areas:
 - (i) lack of supporting documentation on compliance review at the PO's Principal Office;
 - (ii) no evidence of compliance reviews on margin (including opening of margin accounts) section at the PO's Principal Office and a branch office;
 - (iii) delay in compliance reviews at the Principal Office ranging from 1 month to 9 months;

¹ List of the clients of a PO's Corporate Finance department which an insider is prohibited from trading or procuring trades of the securities of such clients and/or publishing research or other materials with comments, considerations or otherwise in respect of such securities.

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- (iv) discharge of compliance function at Principal Office not in accordance with the planned schedule and in contravention of the rules pertaining to supervision of compliance vis-a-vis the waivers granted from appointing a registered compliance officer for its branch office;
- (v) several essential compliance requirements involving exceptions noted in the area of corporate finance were not highlighted in the compliance reviews and consequently not reported to the board of directors and Bursa Securities;
- (b) failure to ensure a clear segregation of duties between those employees dealing in securities and those having duties of administrative/operational in nature as the chief operating officer was authorized to purchase and sell securities for the PO's IVT account;
- (c) failure to maintain a proper and adequate system of internal control which shall include the maintenance of adequate and comprehensive records and taping of conversations of DRs conducting proprietary trading as there was no voice recording of the designated DR undertaking proprietary trades;
- (d) not having internal policies and controls in place for the prevention of insider trading, misuse of confidential information and/or the commission of other offences relating to abuse of confidential information and the Restricted List and Watch List were not updated; and
- (e) failure to ensure that it had internal procedures to verify that all account opening documents had been duly and properly witnessed by its DRs under Rule 5.02A(2)(i) of the Rules of Bursa Depository (Account Opening Breach). There were numerous instances where the DRs did not verify and properly witness the Application for Opening of Account Forms in a manner required under the relevant Rules/procedures.

The sanctions were imposed upon considering, amongst others, the following:-

- The Supervisory Breaches involved repeated breaches which indicated that the level of supervision and compliance at the PO was still unsatisfactory despite being subject to enforcement action earlier for its Supervisory Breaches which involved various lapses of internal controls, supervision and ineffective compliance function (detailed above). The repeat breaches indicated the PO had failed to comply with Bursa's directive to take the necessary steps to address the breaches to ensure there were no similar occurrences/breaches. Notwithstanding the PO's rectification actions which were undertaken to address all the concerns raised by Bursa in the earlier enforcement action taken, its supervision and compliance functions were still lacking which gave rise to the PO committing repeated breaches.
- As for the Account Opening Breach, it is viewed by Bursa as a serious breach as it involved opening of clients' accounts which must be carried out in the manner prescribed by the Rules/procedures in order to protect the clients (i.e. to ensure accounts are opened with the knowledge and consent of the clients) and prevent/avoid abuses of clients' accounts. It was noted that the breach by the PO was not an isolated incident but was a practice at the PO to verify/witness the clients' account opening in a manner not in compliance with the Rules/procedures and there were a significant number of non-compliances detected.

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- (i) The Breaches involved/included repeat breaches by the PO as enforcement actions had earlier been taken against the PO for similar breaches.

Information on this case can be found in the POs' Circular and Bursa Depository's Circular both dated 21 December 2012 on E-Rapid Link.

In 2013:-

- ❖ A PO was imposed a public reprimand and fine of RM100,000 for the inadequate compliance reviews/lapses in compliance functions (Compliance Breach) and insufficient level of supervision by the PO (Supervisory Breach).
 - (a) With regard to the Compliance Breach, the 3 areas of ineffective/lapses in compliance functions were as follows:-
 - (i) the non-compliance by the PO with the Know Your Client (KYC) requirements;
 - (ii) inadequate compliance reviews of the opening of clients' accounts including failing to detect the red flags with regard to the opening of several accounts (Suspicious Accounts) and failure to carry out further investigation and/or ongoing monitoring of clients' activities as required by the Guidelines on Market Conduct and Business Practices for Stockbrokers and Licensed Representatives issued by the Securities Commission on 8 April 2008 (revised on 29 April 2011); and
 - (iii) the PO's failure to carry out on-site review at its branch offices in accordance with the approved branch office visitation schedule in accordance with the Bursa Securities Rules.
 - (b) With regard to the Supervisory Breach, there were 5 areas of ineffective level of supervision (which gave rise to, amongst others, the Compliance Breach) for the PO had failed to:-
 - (i) undertake remedial/rectification actions to ensure that there was a proper management of conflict of interest, whether actual, potential or perceived, which arise or may arise from the carrying out of corporate finance activities although the PO had previously been cautioned by Bursa;
 - (ii) ensure its Proprietary Day Traders who were deemed as "insiders" did not trade in securities which were included in the "Restricted List"²;
 - (iii) ensure compliance with the KYC requirements;
 - (iv) detect the red flags during review of the opening of accounts, in particular, the Suspicious Accounts and did not ensure that ongoing monitoring of clients' accounts were carried out which resulted in possible insider trading activities by its clients;

² See footnote 1 above.

- (v) carry out on-site review at the branch offices in accordance with the approved branch office visitation schedule; and
- (vi) monitor the trades in the Suspicious Accounts despite the red flags (e.g. common address, accounts opened on the same day and traded only in one listed issuer's shares with substantial purchases made via Direct Business Transactions and a substantial part of the shares were sold after the corporate announcement made by company) which ought to have raised the suspicion/alerted the PO as to the possible insider trading activities carried out in the clients' accounts.

Information on this case can be found in the POs' Circular No. G161 of 2013 dated 19 July 2013 on E-Rapid Link.

Case D3: Non-reporting of breaches in Compliance Report

A PO was imposed a fine of RM10,000 for failure to submit the entire compliance report to Bursa, for it was noted that the compliance report submitted to Bursa differed from the compliance report submitted to its Board of Directors in that the Compliance Officer (CO) did not submit certain parts of the compliance reports to Bursa which contained certain alleged breaches.

Case D4: Allowed irregular/unhealthy practice in the business conduct

A PO was fined RM5,000 for allowing an irregular/unhealthy practice to exist in the daily and professional business conduct of the PO as the management staff and the directors of a related company were appointed authorised signatories to operate the bank account of the PO.

Another PO was fined RM5,000 for allowing an irregular and/or unhealthy practice to exist or prevail in its daily professional conduct as it had allowed its EDO to execute the account opening form for a corporate client which was controlled by common shareholders and directors of, or persons related to, the PO. The EDO of the PO was one of the 2 persons authorised by the client to open and operate its trading account with the PO.

In another case, a PO was fined RM25,000 for allowing irregular/unhealthy practice to exist/prevail in the daily and professional business conduct of the PO as a client's clearing account was used to execute trades for its proprietary account. Instead of using its own proprietary account to execute its own trades, trades were executed in a client's clearing account and the trades were subsequently amended to the proprietary account of the PO.

A PO was imposed a private reprimand and fine of RM5,000 for it had:-

- (a) failed to take all reasonable steps to ensure that all essential particulars and information about its clients (including but not limited to the clients' financial standing or credit worthiness and clients' investment objectives) were obtained and failed to satisfy itself that all such information were accurate before opening any trading account for them; and
- (b) allowed irregular and/or unhealthy practice to exist or prevail in its daily and professional business conduct as there were abnormalities/irregularities noted with regard to the operation of some of the clients' accounts and trust monies.

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It was noted that:-

- (i) The PO had allowed several corporate trading accounts to be opened and accorded high trading limits without proper evaluation and/or documentation to determine the identity or net worth and financial strength/credit worthiness of the beneficial owners of the accounts.
- (ii) There were several accounts where significant sum of monies were deposited as trust monies although the outstanding balance in the respective clients' trading accounts were either nil or have minimal balances and there were minimal recent trading activities, contrary to the PO's claim that the funds were deposited by the clients for their own investment and trading objectives.
- (iii) In addition, the placement of the clients' trust monies on daily and/or weekend REPOs by the PO without the clients' further instructions were inconsistent with the normal practice whereby instructions would be communicated by clients to the PO's authorised DR or personnel by phone.
- (iv) The PO had granted waiver of handling and administration fee to numerous clients. Although the PO's policies and procedure gave the management discretion to grant such waivers, there was no documentation to show the basis for granting such waivers to the clients and that the waivers were approved by the Board of Directors.

Case D5: Lapses of supervision and monitoring resulting in abuses of clients' accounts

A PO was fined RM125,000 for lapses of supervision and monitoring of its business activities and the activities of its Registered Persons where the accounts of some clients including a clearing account at a branch office had been used to execute trades for other clients. Upon execution of the trades, the contracts were subsequently amended to the intended clients' accounts. In this instance, there were elements of manipulative trading activities for the securities executed in some clients' accounts/clearing account and subsequently amended to the other clients' accounts/clearing account.

In another case, a PO was fined RM20,000 for failing to maintain a proper and adequate supervisory and compliance system pertaining to the operations and maintenance of the share buyback account of a corporate client resulting in the misconduct of a DR as the DR had used the share buyback account to execute transactions in respect of several securities for an individual client for a period of about 2 weeks and subsequently amended the trades from the clearing account to the individual's account.

Case D6: Supervisory lapses resulting in abuse of contract amendment facility by DR

Enforcement action was taken against a PO for there were lapses in the supervision and monitoring by PO over its DRs' activities. In this regard:-

- (a) It was noted that the PO did not have an effective supervision and monitoring method on the contract amendments carried out by its DRs and failed to ensure that the Contract Amendment Rules were complied with at all times by its DRs (Contract Amendment Breach).

It was further noted that there were frequent contract amendments carried out by one DR from one client's account to another client's account including amendments made to the DR's wife's account. The DR had transferred/amended trades from other clients' accounts into his wife's account. This resulted in the transfer of profitable trades to his wife's account to the disadvantage of the original clients over a period of

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time (DR's Breach). The failure to put in place proper and effective supervisory controls resulted in failure to detect the DR's aforesaid unlawful activities (including conducting trades in his wife's account and undertaking contract amendments to benefit his wife), which was a situation of conflicts of interests. In this regard, the PO was found to have failed to comply with Rule 404.1(7)(b) of the Rules of Bursa Securities (Supervisory Breach relating to DR's Breach); and

- (b) there were numerous instances of trades carried out in some clients' accounts/Clearing Accounts by its DRs and subsequently amended to other clients' accounts/Clearing Accounts. This was in breach of the prohibition against sharing of Clearing Accounts and co-mingling of clients' accounts in Paragraph 3.2(a) of R/R 18 of 2005 (Clearing Accounts Breach).

The PO was imposed a fine of RM15,000 for the Contract Amendment Breach, RM42,000 for the Supervisory Breach relating to DR's Breach and RM25,000 for the Clearing Accounts Breach. The Deferred Fine Policy was applied in regard of the fines of RM15,000 and RM25,000.

Case D7: Supervisory lapses resulting in misconduct by employees

A fine of RM5,000 was imposed on a TP for the TP had:-

- (a) accepted orders on behalf of its clients through a person who was not a Registered Representative (Miss A) over a period of 2 months. This was in contravention of the requirement that TPs can only accept orders on behalf of clients through its Registered Representatives; and
- (b) failed to ensure that it has a proper supervisory system to prevent/detect acceptance of clients' orders by a person who was not a Registered Representative and ensure that its Registered Representatives/employees complied with the Rules.

The fine of RM5,000 was imposed taking into consideration, amongst others, mitigating factors including that the breach was self-reported by the TP and the rectification/remedial actions initiated by the TP.

In addition to the fine, the TP was also directed to carry out a review and submit a report to determine whether there are sufficient controls/measures put in place to prevent any of its unlicensed personnel from accepting orders from its clients or engaging in any trade practices that is usually performed by a licensed FBR to Bursa.

It was noted that the TP had failed to establish/maintain a proper system to supervise the activities of its FBR. The TP could have detected and/or curbed the order acceptance by Miss A earlier if it had reviewed/checked its voice logging system in view of the numerous instructions accepted by Miss A over a period of 2 months.

In relation to this, action was also taken against the FBR in charge of supervising the trainee where a fine of RM10,000 was imposed (**see case C10 above**).

Case D8: Breach by Principal Officer resulting in supervisory lapses/unhealthy business practice by PO

Against Principal Officer:

In this case, action was taken against the Head of Operations (HOO) of a PO in relation to granting of financings to clients for IPO via placement of shares which were granted under normal trading account instead of margin

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account. The HOO of the PO was found to have failed to perform her duties as the HOO efficiently and fairly which resulted in the PO's breaches (set out below) for the HOO had:-

- (a) allowed the granting of several financings by the PO which:-
 - (i) did not fall within the activities permitted to be carried out by the PO under the Rules; and
 - (ii) constituted another type of financing for the purpose of subscription and purchase of securities other than margin financing without obtaining the Exchange's prior determination/approval of the same as the financings were granted under normal trading account instead of margin account; and/or
- (b) allowed the granting of the financings and issued Letters of Offer/Undertaking without:-
 - (i) the relevant resolutions from the Board of Directors approving the granting of the financings and/or issuance of the Letters of Offer/Undertaking;
 - (ii) the relevant supporting documents from the clients;
 - (iii) formal financing agreements between the PO and the clients; and
 - (iv) proper assessments being carried out on the clients' financial standing and credit worthiness prior to granting the financings to the clients; and
- (c) issued the Letters of Offer/Undertaking against the PO's company policy and Approving Authority Matrix.

The HOO was imposed a fine of RM3,000 having considered, amongst others, that the HOO had instructed the Internal Audit of the PO to carry out the investigation on the granting of one of the financings (Financing A) which subsequently led to the breach being self-reported to Bursa Securities by the PO.

Against PO:

The PO was imposed a total fine of RM15,000 for supervisory breach/unhealthy business practices for various breaches. In this regard, upon considering, amongst others, that the PO had had self-reported 1 out of the several financings to Bursa, a fine of RM3,000 was imposed on the PO for the following:-

- (a) carried out unpermitted activities in contravention of Rule 503.2(1) of the Rules of Bursa Securities as the financings did not fall within the activities permitted to be carried out under the said rule;
- (b) provided another type of financing for the purpose of subscription and purchase of securities other than margin financing and/or failed to obtain the Exchange's prior determination/approval of the same in contravention of Rule 703.2(1) of the Rules of Bursa Securities as the financings were granted under normal trading account instead of margin account; and/or
- (c) allowed irregular and/or unhealthy practice to exist or prevail in its daily and professional business conduct.

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Another RM12,000 was imposed as fine against the PO for there were supervisory and/or monitoring weaknesses/lapses and/or internal control weaknesses in relation to granting the financings as the PO did not have in place adequate controls/procedures to ensure that:-

- (i) the financings were made in accordance with the Rules; and/or
- (ii) the financings were granted with proper assessment of the financial standing and credit worthiness of the clients and documentation and the necessary authority.

The following weaknesses/lapses were noted:-

- (a) The financings were not supported with any relevant documents from the clients and there were no proper documentation such as proper/formal financing agreements and merely based on instructions given by the PO's Executive Director of Dealing (EDD) via email.
- (b) The Letters of Offer/Undertaking were not properly issued/addressed to the relevant party and in respect of Financing A, it was issued by the HOO against company policy and not in compliance with the Approving Authority Matrix of the PO. In this regard, there was no authority given to the HOO to approve any other kind of financing such as Financing A.
- (c) No proper assessments were carried out on the clients' financial standing and credit worthiness prior to granting the financings to clients with substantial values.
- (d) For some of the financings, the authorisation for the payment was given to the bank by the PO prior to the approval of the internal authorisation for the payment.
- (e) The PO and/or its staff did not detect 3 other prior financings as the staff was inexperienced in the arrangement of financing which showed that the PO did not have adequate internal controls/procedures to detect/prevent the granting of financings in contravention of the Rules.

In another case, a PO/ADA was imposed a private reprimand and a fine of RM5,000 and its Head of Branch (HOB) was imposed a fine of RM1,000 for:-

Against PO/ADA – failing to comply with the CDS Procedures Manual in relation to transfer of shares and there were insufficient level of supervision over the operations of business activities and activities of registered persons in relation to:-

- (a) an over-transfer of shares by the PO from a client's (Client A) margin account maintained at the PO/ADA to her margin account in another PO (1st Transfer);
- (b) arising from the over-transfer of shares, there were insufficient shares/a shortfall of shares in Client A's account maintained at the PO/ADA for purposes of delivery for sale transactions done earlier; and
- (c) in rectifying the situation of over-transfer in the 1st Transfer, the PO/ADA had effected a transfer of shares from one client's account (Client B) to Client A's account under B2 Approved Reasons For Transfer (2nd Transfer) (which only allows transfer involving change of beneficial ownership where the transferor and transferee are family members).

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In this regard, it was noted that:-

- (i) There were lapses in the supervision/monitoring by the PO/ADA of its branch operations staff, in the oversight by its management including the Head of Margin/Operation at the Principal Office who had failed to correctly verify the free balance of the shares in Client A's account before granting approval for the transfer request made by the Branch office.
- (ii) The incidences in regard to the 1st Transfer and 2nd Transfer of shares showed that the PO/ADA had also failed to maintain a proper and adequate supervisory and compliance system with a view to preventing any contravention of the Rules including Depository Rules. It also showed the PO/ADA's failure in the aspects of maintaining a proper supervisory programme and a system of internal controls which must take into account the PO/ADA's operations including its function as an ADA/proper conduct of its business and proper undertaking of its risk management, which has led to its failure to ensure compliance of the relevant Rules including Depository Rules.

Against HOB - failure to carry out supervisory functions leading to the breaches by the PO in regard to the over transfer of shares and inaccurate declaration in the transfer form. In this regard, the HOB failed to:-

- (a) ensure that the request for 1st Transfer was in order including the correct number of available shares in the client's account at the PO;
- (b) ensure that the relevant supporting documents in the 2nd Transfer were obtained from the depositor to support the reason for transfer of the shares under B2 ART;
- (c) reject the 2nd Transfer for non-compliance of Appendix 67 of the CDS Procedures Manual as the transfer request was not supported by the relevant supporting documents evidencing that the transferor and transferee were family members before effecting a transfer under B2 ART as declared in the FTF 010 – 2nd Transfer; and
- (d) obtain prior approval for transfer involving change of beneficial ownership from Bursa Depository before effecting the 2nd Transfer.

In 2014:-

- ❖ PO A, its Head of Branch/Branch Head of Operations (HOB/BHOO) and Head of Dealing (HOD) and/cum Acting Head, Retail Services (the 2 Principal Officers) and 2 DRs (who were DRs of PO X at the material time) were imposed the following sanctions for breach of the Rules involving prohibited commission sharing arrangement between PO A and two DRs whilst they were still engaged as DRs of PO X:-

PO A - public reprimand and fine of RM500,000;

The 2 DRs - public reprimand, fine of RM500,000 and RM210,000 respectively, 6 months suspension and requirement to undergo training program (Mandatory Training); and

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The 2 Principal Officers - public reprimand, fine of RM20,000 each, 1 year suspension/restriction and mandatory Training

in relation to:-

- (i) the payment by PO A of commission to the 2 DRs referred to as referral fees for the transactions undertaken in their clients' accounts (which clients had opened their accounts with the PO and/or transferred their shares from PO X to the PO upon the introduction/recommendation by the 2 DRs) whilst they were still attached to/DRs of PO X and/or pending registration of their transfer to PO A (the Arrangement); and
- (ii) one of the DR's access to PO A's dealing floor whilst the said DR was still a DR of PO X and not an employee/DR of PO A.

In this regard, the following was noted:-

- (1) Whilst the 2 DRs were still attached to/DRs of PO X and/or pending registration of their transfer to PO A:-
 - (a) pursuant to the Arrangement between PO A and the 2 DRs, both DRs had received large sum of monies which were in substance commission from PO A over a period of time for the transactions undertaken in their clients' accounts (which clients had opened their accounts with the PO and/or transferred their shares from PO X to the PO upon the 2 DRs' introduction/recommendation); and
 - (b) one of the DR was allowed access to PO A's dealing floor whilst he was still a DR of PO X and not an employee/DR of PO A.
- (2) With regard to the Arrangement, it was noted that:-
 - (a) PO A had facilitated the opening of clients' accounts with/transfer of clients' shares from PO X to PO A over a period of time by designating DRs to attend to the 2 DRs' clients and specific BFE User ID and Dealer Code for execution of trades for their clients and to monitor and capture their trading activities, thus ensuring that the trades of the 2 DRs' clients were clearly identified for the purpose of calculation of commission;
 - (b) the payment of monies to the 2 DRs indicated that both of them were treated as/acting as if they were DRs of PO A whilst they were still DRs of PO X and/or before they were registered as DRs of PO A;
 - (c) although the payments by PO A to the 2 DRs were couched as/ referred to as referral fees, these payments which were calculated based on a percentage of the gross brokerage earned from the transactions of the 2 DRs' clients were in essence/substance commission payments; and
 - (d) the payments by PO A to the 2 DRs and their acceptance thereof tantamount to the sharing of commission with another PO which was not the PO that had engaged them as the DRs at the material time of the breaches, which were prohibited under the Rules.

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- (3) The 2 Principal Officers (both of whom had supervisory roles/duties including the duty to ensure compliance with the rules) had compromised the duties entrusted to them as the HOB/BHOO and HOD respectively, failed to discharge their responsibilities and perform their duties efficiently in ensuring compliance of the Rules. In this regard:
- (a) The HOB/BHOO had allowed/condoned/failed to refrain from participating or being involved in the Arrangement and/or make further enquiries to ensure that the Arrangement would not be in breach of the Rules pertaining to the prohibited commission sharing and in addition, he had allowed one of the DR access to the dealing room of the PO before the DR was officially registered as a DR of the PO; and
 - (b) The HOD had allowed/condoned the Arrangement which was carried out with his approval/knowledge and/or were supported by him without any objections and/or without making the necessary enquiries to ensure that the Arrangement was not prohibited under the Rules. In addition, he had allowed/condoned the access to the dealing floor by one of the DRs.
- (4) PO A knew or should have known of the Arrangement for the evidence clearly showed that it had allowed/authorized the payment of commission referred as referral fees to both the 2 DRs pursuant to the Arrangement for a substantial period of time. As such, PO A had participated in/allowed the irregular or unhealthy practice and failed to adhere to principles of good business practice. In relation to this, PO A did not have proper and adequate procedures/internal controls/system and there were lapses/weaknesses in the PO's supervision/internal controls over its business activities and the activities of its Registered Persons and employees including the 2 Principal Officers.
- (5) Arising from the Arrangement, PO A had profited from a substantial sum of brokerage earned over a period of time in respect of the trades undertaken through the Arrangement which was in contravention of the Rules.

Information on this case can be found in the POs' Circular dated 1 July 2014 on E-Rapid Link.

D9: Breach relating to PO's compliance function

A PO was imposed a fine of RM10,000 in relation to its compliance function whereby its Compliance Officer (CO) had failed to:-

- (a) ensure that the monthly Compliance Report for the two months were tabled to the PO's Board of Directors (BOD); and
- (b) report the exceptions noted in relation to the employees' transactions executed prior to obtaining approval.

In this regard, it was noted that:

- (i) With regard to the exceptions noted in relation to the employees' transactions for the instances of transactions executed prior to obtaining approval, the CO had reviewed and rectified the exceptions prior

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to the Inspection on the PO. However, the said exceptions were not reported in the compliance report submitted to the Exchange.

- (ii) Bursa Securities was made to understand that the concern in relation to the employees' transactions executed prior to obtaining approval were also raised by the Securities Commission during their inspection earlier but this was also not reported in the monthly compliance report.

D10: Supervisory breach by TPs

In 2012:-

- ❖ A TP was imposed a fine of RM25,000 for supervisory breach. In this regard, in relation to the TP's clients' margin and position limits, the TP was found to have failed to (1st Breach):-
 - (a) establish and maintain a proper system to supervise the activities of each Registered Representative, agents and other personnel and that is reasonably designed to achieve compliance with the Rules of Bursa Derivatives; and
 - (b) enforce its written procedures to supervise the type of business in which it engages and to supervise the activities of its Registered Representatives and that are reasonably designed to achieve compliance with the Rules of Bursa Derivatives.

In regard to the above, the TP had:-

- (i) on several occasions allowed its clients to initiate new trades (in the manner that would increase the existing exposure of the clients) even though there were outstanding margin calls exceeding 3 market days from the transaction day (T+3) in breach of Rule 614.1 of the Rules of Bursa Derivatives and item 3.2 of Trading Members' Circular No. 6/2000 (TMC 6/2000); and
- (ii) not applied the formula for computing the margin call stipulated in Item 2.2 of TMC 6/2000 in its margin call computation.

In addition, the exceptions noted in 2 years with regard to the 1st Breach were not reported by the Compliance Officer in the monthly Compliance Report to the Exchange (2nd Breach).

The breach in relation to allowing clients to initiate new trades (in the manner that would increase the existing exposure of the clients) even though there were outstanding margin calls exceeding 3 market days from the transaction day (T+3) is a repeat breach by the TP as:-

- the Securities Commission (SC) had raised the same issues in the SC's earlier report; and



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- the TP was previously reprimanded by Bursa Securities for similar breach involving several clients, one of whom was also one of the clients in the current inspection finding.

This showed that the TP had persistently violated Rule 614.1 of the Rules of Bursa Derivatives and item 3.2 of TMC 6/2000 which constitutes a major offence under Rule 510.2(o) of the Rules of Bursa Derivatives.

The margin requirements and position limits under the rules must be strictly adhered to and the TP's repeated / prolonged failure to do so indicated supervisory breach/lapses and/or systemic failure with regard to the management of its clients' margin requirements and position limits and computation of margin call.

As such, a fine of RM25,000 was imposed on the TP for the 1st and 2nd Breaches.

- ❖ Another TP was imposed a fine of RM5,000 for there were lapses in its supervision as indicated by the following:-
 - (a) the TP had failed to ensure that its Compliance Officer (CO) carried out review on the front office function of the TP and the areas covered were limited to back office and accounting related areas only. In this regard, it was noted that if the CO had initiated some form of front office reviews e.g. checking the voice recording of orders placed by clients, the issues highlighted by the inspection with regard to front office related areas could have been brought much earlier to the attention of the Board and management of the TP;
 - (b) there was no Board meeting held since the TP commenced its operations as a TP; and
 - (c) since the commencement of its business, no internal audit review has been carried out. In this regard, the TP had appointed a third party as its internal auditors. However, the TP had yet to execute the Service Level Agreement with the third party and submit the application to Bursa Derivatives for approval to outsource its internal audit function to the third party.

The weaknesses and non-compliances noted in paragraphs (a) – (c) above indicated that the overall management supervisory system in the TP was poor and ineffective which had directly and indirectly contributed to the weaknesses and non-compliances noted in the inspection.

In 2013:-

- ❖ A TP was imposed a private reprimand and fine of RM50,000 for various compliance and supervisory breaches. With regard to the compliance breach, there were several weaknesses/lapses noted in the compliance reviews/functions undertaken by the TP as follows:-
 - (a) the compliance personnel did not use the compliance checklist stipulated in the TP's Compliance Manual which resulted in inadequate daily compliance reviews as these were confined to limited areas; and
 - (b) there were no formal compliance review procedures established for review of:-

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- (i) voice logging records, as there were no independent review procedures on recording of conversations between FBRs and clients which would enable the detection of any incidence of front running and assist in the monitoring of front-office activities;
- (ii) error trades; and
- (iii) Office of Foreign Assets Control (OFAC) upon admission of a new client to ensure that OFAC screening was conducted for the TP's new clients.

As for the supervisory breach, there were insufficient/ineffective levels of supervision in the following areas:-

- (a) the TP had failed to detect/ensure that its clients' funds were properly safeguarded and segregated from the company's funds and that non-client transactions were not carried out using the clients' segregated account;
- (b) the TP had failed to detect/take reasonable steps to ensure compliance with the voice logging requirements and rules on appointment of Designated Representatives resulting in:
 - (i) many instances where a group of clients' (said group of clients) orders were not voice logged;
 - (ii) no written authorisations from its clients on the appointment of their Designated Representative; and
 - (iii) breach of the prohibition against 1 Designated Representative acting for more than 1 client;
- (c) the TP had failed to maintain its Adjusted Net Capital (ANC) at above the early warning levels for several months and failed to take proactive measures to strengthen its financial position. Further, despite a weak financial position, the TP had utilised its funds towards payments and advances to its director and holding company; and
- (d) the TP had failed to safeguard the interest of the company as despite its weak financial position, with its ANC at below the early warning level of 150%, the TP had utilised its funds to grant interest free loans to and making payments on behalf of its holding company.

In 2014:-

- ❖ A TP was imposed a private reprimand and fined RM50,000 coupled with enforceable conditions³ for allowing/failing to ensure that its FBRs refrained from using their clients' accounts as facilitating accounts (FAs) for its FBRs had executed trades in one client's account and subsequently transferred/amended the trades to another client's account. This indicated that the FBRs were using their clients' accounts as FAs.

In this regard, it was noted that:-

³ The TP was required to pay upfront 50% of the fine (i.e. RM25,000) within a stipulated time frame whereas payment of the balance of RM25,000 was deferred subject to fulfillment of enforceable conditions by the TP.

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- (a) There were numerous instances where trade transfers were carried out by several FBRs over a period of time.
- (b) One of the FBRs, i.e. FBR A, who had executed a significant number of trade transfers had explained that this was to ensure fast execution.
- (c) Although the TP's policy and procedures (P&P) on trade adjustments and trade transfer reserves the right to outright reject requests for trade adjustment if the trade adjustment was too frequent, the TP did not take reasonable steps to verify the reasons for the aforesaid trade transfers.
- (d) Instead, a significant number of trade transfers were allowed by the TP over an extended period of time without any review of the reasons for the trade transfers. The TP had failed to comply with its own P&P and verify the reasons for the frequent trade transfers, which if done, would have detected/curbed the practice of using clients' accounts as FAs by its FBRs.
- (e) The Rules provide for the use of a FA when the FBR is unfamiliar or uncertain of the correct client code in order to facilitate the fast execution of trades. By discontinuing the operation of its FA to discourage its FBRs from abusing the FA, the TP ought to have exercised proper supervision/monitoring over the trade transfers undertaken by the FBRs to ensure that client's account were not used as a FA. However, the TP failed to supervise/monitor the trade transfers and instead approved the trade transfers without reviewing the reasons for the same.
- (f) The prohibition against using client's account as a FA is for the protection of the client's account and hence, Bursa views the Breach seriously in view of the potential abuse of the client's account which may arise if such a practice is not curbed.
- (g) The TP had acknowledged and admitted to the breach and assured Bursa Derivatives that such incidence will not be repeated.

In respect of the fine of RM50,000, the TP was directed to pay upfront RM25,000. The payment of the balance of the fine was deferred subject to enforceable conditions, which included:-

- (i) the review of its P&P to achieve effective supervision and monitoring of its FBRs' trade transfers to ensure compliance by its FBRs with the prohibition against using client's account as a FA;
- (ii) monthly reporting on the status and progress of the above by the Head of Compliance of the TP to Bursa Derivatives;
- (iii) the carrying out and providing of an independent audit report on the aforesaid conditions within a specified period of time; and
- (iv) the full and effective implementation of the measures, monitoring and reporting mechanisms in place so as to ensure the non-recurrence of the breach of the same nature within a specified time frame.

In relation to the case above, FBR A was imposed a private reprimand, fine of RM10,000 and mandatory training (**See Case C18 above**).

D11: Supervisory breach by PO resulting in market offences by DR

A PO was imposed a private reprimand and a fine of RM150,000 for its supervisory breach which gave rise to/allowed the continuance of the manipulative dealing activities in the securities of one counter (the said Counter) by its DR, which involved churning activities, cross trades, bidding up activities and depression of share price of the said Counter (Manipulative Trading Activities).

The details of the breach by the PO showed that:-

- (a) There were lapses in the PO's supervision/monitoring of its DR's dealing activities in the said Counter as despite the irregular/manipulative characteristics of the trading activities by the DR and red flags (i.e. domination of trading activities, common address(es) amongst some of the clients and some of the clients had significant trading activities which trades were frequently crossed with/rolled over to each other), the PO had failed to promptly detect the same and/or refrain the DR from continuing with the Manipulative Trading Activities.
- (b) The PO had failed to ensure that it had effective internal controls/system in place in its supervision and monitoring of its DR's trading activities in the said Counter and to immediately take remedial, preventive and corrective actions to prevent/deter/curb the Manipulative Trading Activities from being undertaken/continued by the DR at the PO.
- (c) The PO had continued to provide/grant additional and frequent ad hoc trading limits (Additional Ad Hoc Limits) to its DR's clients at the DR's requests over a period of time without:-
 - (i) proper assessment/review as to the orderliness of the trading activities undertaken during the relevant period in the clients' accounts; and
 - (ii) thereafter monitoring the utilisation of the said limits,

which had facilitated the Manipulative Trading Activities by its DR in his clients' accounts.

In this regard, the Additional Ad Hoc Limits granted to the DR's clients were essentially utilised by the DR for trading in the said Counter in almost all of the DR's clients' accounts, which in turn gave rise to the purchases of a significant number of the shares of the said Counter undertaken in these clients' accounts during the relevant period.

- (d) The PO had failed to ensure that there were in place internal controls/system or adequate internal controls/system to closely/properly/adequately monitor and supervise its DR's dealing activities in the said Counter during the relevant period, which should include:-
 - (i) not only the supervision and monitoring from the perspective of credit control/credit evaluation but also from the aspects of ensuring that the PO had discharged its obligations towards orderliness of trading activities in the clients' accounts at the PO which were undertaken by its DR; and
 - (ii) a proper assessment/evaluation/review by the PO including as to how the Additional Ad Hoc Limits granted by the PO to its DR had been utilized by him in carrying out his dealing activities, in

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particular the dealing activities in the said Counter in the DR's clients' accounts, prior to the granting of any of the subsequent Additional Ad Hoc Limits or increase of the trading limits.

- (e) The PO acknowledged/admitted that notwithstanding the controls it had in place to monitor unhealthy dealing activities of its DRs, there were lapses in its supervision and it was unable to promptly detect the DR's unhealthy activities.

D12: Other supervisory breaches by PO

In 2014, a PO was imposed a private reprimand and a fine of RM4,000 for there were gaps/lapses in the PO's supervision, internal controls and policy and procedure (P&P) in relation to issuance of contract notes. In this regard, the PO had issued contract notes which did not reflect the actual quantity of the securities transacted. The following gaps/lapses in the PO's supervision, internal controls and P&P were noted:-

- (a) inadequate written P&P to prevent continued contravention of the rules/requirements on issuance of contract notes by its Registered Persons and employees; and
- (b) failure by the PO to take prompt, adequate and effective actions (including to amend its P&P) to ensure that contract notes which did not reflect the quantities transacted would not be issued particularly after enforcement action was taken against the PO in 2013 for similar breach and despite being reminded to ensure similar breach did not recur.

The sanctions were imposed upon considering, amongst others:-

- (i) the PO's continued failure to comply with and/or blatant disregard of the rules/requirements for the PO had on 3 occasions issued contract notes which did not reflect the actual quantity of the securities transacted and despite enforcement actions being taken against the PO in 2013; and
- (ii) the PO only amended its P&P after enforcement actions had been taken against the PO in 2013. If the PO had taken the necessary actions earlier, the subsequent breaches could have been prevented.

