

SFC reprimands and fines GMO-Z.com Forex HK Limited \$1.6 million

9 Feb 2017

The Securities and Futures Commission (SFC) has reprimanded and fined GMO-Z.com Forex HK Limited (GMOHK) \$1.6 million for deficiencies in its order execution and slippage handling procedures, and failures in its electronic trading system for leveraged foreign exchange contracts (Note 1).

In August 2016, the SFC and GMOHK jointly engaged an independent reviewer to review GMOHK’s controls, which found that:

- GMOHK’s order execution and slippage handling procedures and the relevant policies were inadequate, and resulted in 243 transactions of 17 clients involving more than \$270,000 being executed at the last tradable price instead of the next available price;
- GMOHK failed to adequately disclose to its clients its policy that the clients’ order execution would not be confirmed until GMOHK had hedged its risk exposure; and
- GMOHK’s electronic trading system for execution of client orders in leveraged foreign exchange contracts did not operate as intended and could affect the execution price and the execution time in certain circumstances.

The SFC considers that GMOHK’s failures fell short of the standards as set out in the Code of Conduct (Note 2).

In determining the sanction, the SFC considers that GMOHK’s cooperation has significantly expedited the investigation and disciplinary proceedings. Similar failures would have resulted in a substantially higher level of fine.

End

Notes:

1. GMOHK is licensed under the Securities and Futures Ordinance to carry on business in Type 3 (leveraged foreign exchange trading) regulated activity.
2. Among others, General Principles 2 (diligence) and 6 (conflicts of interest) of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission provide that a licensed corporation, in conducting business activities, should act with due skill, care and diligence, and in the best interests of its clients and try to avoid conflicts of interest, and when the conflicts cannot be avoided, should ensure the clients are fairly treated.

[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 publicly reprimanded and fined GMO-Z.com Forex HK Limited (**GMOHK**) \$1.6 million for deficiencies in relation to its order execution and slippage handling procedures, and failures in respect of its electronic trading system pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. GMOHK is licenced under the SFO to carry on business in Type 3 (leveraged foreign exchange trading) regulated activities.
3. In August 2016, the SFC and GMOHK jointly engaged an independent reviewer to review GMOHK's controls, which found that:
 - (a) GMOHK's order execution and slippage handling procedures and the relevant policies were inadequate, and resulted in 243 transactions of 17 clients involving more than \$270,000 being executed at the last tradable price instead of the next available price;
 - (b) GMOHK failed to adequately disclose to its clients its policy that the clients' order execution would not be confirmed until GMOHK had hedged its risk exposure; and
 - (c) GMOHK's electronic trading system for execution of client orders in leveraged foreign exchange contracts did not operate as intended and could affect the execution price and the execution time in certain circumstances.
4. The failures of GMOHK in relation to the order execution and slippage handling procedures and policies breached General Principle 2 (diligence) of and paragraph 61 of Schedule 6 to the Code of Conduct for Persons Licensed by or Registered with the SFC (**Code of Conduct**). The inadequate disclosure to clients about the hedging procedures breached General Principle 6 (conflicts of interest) of the Code of Conduct. The deficiencies in relation to GMOHK's electronic trading system breached General Principle 2 and paragraphs 18.5 and 1.2.2 of Schedule 7 to the Code of Conduct.

Summary of facts

5. In response to a complaint about the execution of a liquidation order on 24 August 2015 by GMOHK, the SFC made enquiries into the order execution procedures and slippage handling policies over the period from October 2015 to June 2016.
6. GMOHK cooperated with the enquiries by jointly engaged with the SFC an independent reviewer to review its order execution procedures and electronic trading system for leveraged foreign exchange trading.

7. The independent reviewer found a number of areas in which there was inadequate documentation of policies and procedures in relation to GMOHK's order execution procedures. In particular, there was a lack of policies and procedures on the process and controls over the making of manual adjustment on client order executions. Although manual adjustments appeared uncommon and were usually made in favour of clients, the lack of documented policies and procedures created a potential risk that inappropriate changes could be made to client order executions.
8. Notwithstanding GMOHK's slippage handling policies are found to be generally adequate, the independent reviewer considered that GMOHK should disclose to clients about the definition and treatment of gains and losses arising from differences in execution price of liquidation orders and GMOHK's hedging transactions.
9. It was found that GMOHK's order execution policies effective during the 12-month period before 25 August 2015 could result in the liquidation orders for clients being executed at the last tradable price instead of the next available price. During the relevant period, the reviewer identified the transactions of 17 clients were affected.
10. GMOHK was not involved in the design and testing of its electronic trading system. The system design and testing were the responsibility of GMOHK's group company in Japan. The independent reviewer found that there were inadequate and ineffective management controls for the electronic trading system, which resulted in changes being made to the system without GMOHK's knowledge and execution outcomes not consistent with GMOHK's understanding in certain circumstances.

Conclusion

11. As a licensed corporation, GMOHK has a duty to ensure regulatory compliance. Its failures breached the regulatory requirements under the Code of Conduct.
12. In deciding on the disciplinary action, the SFC took into account all relevant circumstances, including GMOHK:
 - (a) involved its senior management in the liaison with the SFC about the regulatory concerns at an early stage;
 - (b) took initiative to bring this matter to an early conclusion by fully and frankly discussing the regulatory concerns with the SFC;
 - (c) undertook a credible review with the SFC to address the regulatory concerns and identify the deficiencies in its internal controls;
 - (d) cooperated with the disciplinary action by resolving the SFC's regulatory concerns;
 - (e) took responsibility for the matter, including making adequate and reasonable compensations promptly to the affected clients and implementing the recommendations of the independent reviewer;

- (f) was receptive to the SFC's suggestions as to how future recurrence of the matter could be avoided; and
 - (g) has no disciplinary record before the present action.
13. In particular, the SFC considers GMOHK's cooperation is extraordinary and has significantly expedited the investigation and disciplinary proceedings. Therefore, a meaningful reduction in the level of fine is warranted and appropriate. But for the cooperation, similar failures would have resulted in a substantially higher level of fine.