

SFC reprimands and fines Citigroup Global Markets Asia Limited \$4 million for alternative liquidity pool failures

10 Jul 2018

The Securities and Futures Commission (SFC) has reprimanded and fined Citigroup Global Markets Asia Limited (CGMAL) \$4 million over CGMAL's regulatory breaches in relation to the operations of its alternative liquidity pool (ALP) (Notes 1 & 2).

The disciplinary action followed an SFC investigation on CGMAL, which found that the operations of Citi Match, the ALP of CGMAL, failed to comply with the relevant requirements from December 2015 to August 2016 as set out in the Code of Conduct (Note 3).

CGMAL was expected to operate Citi Match with due skill, care and diligence, and required to:

- provide the ALP Guidelines to users to ensure that they are fully informed on how the ALP operates; and
- ensure that only qualified investors are permitted to be users of the ALP (Notes 4, 5 & 6).

However, due to an incorrect system setting of client profiles, over 130 clients had accessed Citi Match without being assessed whether they were qualified investors. CGMAL also failed to provide the clients with the ALP Guidelines prior to routing their first orders to Citi Match.

In reaching the resolution, the SFC took into account all relevant circumstances, including that CGMAL:

- took remedial actions to rectify the situation shortly after identifying the incorrect system setting and subsequently implemented enhanced measures to ensure compliance; and
- took the initiative to bring this matter to a conclusion by cooperating with the SFC to resolve the regulatory concerns.

End

Notes:

1. CGMAL is licensed under the SFO to carry on business in Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 5 (advising on futures contracts), Type 6 (advising on corporate finance) and Type 7 (providing automated trading services) regulated activities.
2. Code of Conduct for Persons Licensed by or Registered with the SFC.
3. Paragraph 19 of and Schedule 8 to the Code of Conduct, which came into effect on 1 December 2015, set out the requirements for ALP operations.
4. General Principle 2 of the Code of Conduct provides that in conducting its business activities, a licensed corporation should exercise due skill, care and diligence, in the best interests of its clients and the integrity of the market.
5. Paragraph 19.7 of the Code of Conduct provides that a licensed corporation operating an ALP should, by means of ALP Guidelines (as defined in paragraph 19.2(a)), provide sufficiently comprehensive information to the users (as defined in paragraph 19.2(g)) of the ALP to ensure that they are fully informed as to the manner in which the ALP operates, and prior to routing any order to an ALP on behalf of a client for the first time, a licensed corporation should ensure that the ALP Guidelines have been brought to the attention of the person placing or originating the order.
6. Paragraph 19.4(a) and paragraphs 7 and 8 of Schedule 8 to the Code of Conduct provide that a licensed corporation should establish and implement measures to ensure, and all reasonable steps have to be taken to ascertain, that only qualified investors (as defined in paragraph 19.2(f)) are permitted to be users of ALP. Paragraph 19.4(b) provides that a licensed corporation should only route orders to an ALP on behalf of clients where such orders are placed or originated by a person who is a qualified investor.

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

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STATEMENT OF DISCIPLINARY ACTION

The Disciplinary Action

1. The Securities and Futures Commission (**SFC**) has publicly reprimanded and fined Citigroup Global Markets Asia Limited (**CGMAL**) \$4 million pursuant to section 194 of the Securities and Futures Ordinance (**SFO**).
2. CGMAL is licensed under the SFO to carry on business in Type 1 (dealing in securities), Type 2 (dealing in futures contracts), Type 4 (advising on securities), Type 5 (advising on futures contracts), Type 6 (advising on corporate finance) and Type 7 (providing automated trading services) regulated activities.
3. The disciplinary action is taken according to an agreement pursuant to section 201 of the SFO dated 5 July 2018 for CGMAL's failures to comply with the regulatory requirements in relation to the operations of its alternative liquidity pool (**ALP**).

Summary of facts

4. Following a thematic review of ALPs conducted between 2016 and 2017 to assess whether licensed corporations were in compliance with the relevant requirements set out in the Code of Conduct for Persons Licensed by or Registered with the SFC (**Code of Conduct**), the SFC became concerned about CGMAL's ALP, Citi Match. The SFC therefore investigated into the operations of Citi Match.
5. As a licensed corporation, CGMAL has to conduct its business activities with due skill, care and diligence¹ and comply with the applicable regulatory requirements. In particular, the ALP requirements set out in paragraph 19 of and Schedule 8 to the Code of Conduct² provide that a licensed corporation operating an ALP should:
 - (a) by means of ALP Guidelines³, provide sufficiently comprehensive information to the users⁴ of the ALP to ensure that they are fully informed as to the manner in which the ALP operates, and prior to routing any order to an ALP on behalf of a client for the first time, a licensed corporation should ensure that the ALP Guidelines have

¹ General Principle 2 of the Code of Conduct

² These requirements came into force on 1 December 2015

³ Paragraph 19.2(a) defines "ALP Guidelines" as the guidelines that are required to be prepared by a licensed corporation operating an ALP, for the purpose of providing guidance to the users of the ALP concerning its operation

⁴ Paragraph 19.2(g) defines "user" as a qualified investor whose orders are placed into or whose transactions are conducted in an ALP, and includes any qualified investor which is ultimately responsible for originating the instruction in relation to an order placed into, or a transaction conducted in, an ALP

been brought to the attention of the person placing or originating the order (paragraph 19.7); and

- (b) establish and implement measures to ensure, and all reasonable steps have to be taken to ascertain, that only qualified investors⁵ are permitted to be users of an ALP (paragraph 19.4(a), paragraphs 7 & 8 of Schedule 8), and it should only route orders to an ALP on behalf of clients where such orders are placed or originated by a person who is a qualified investor (paragraph 19.4(b)).
6. Prior to 1 December 2015, CGMAL made preparations for compliance with the ALP requirements including reviewing the qualified investor status of some clients and providing them with the ALP Guidelines. However, it overlooked that its system had defaulted certain clients as allowed to match trades in Citi Match, when their orders should not have been enabled access to ALP.
7. The incorrect default setting was not discovered until the SFC's thematic review in 2016. As at 1 August 2016, the default setting of over 470 clients was incorrect and the orders of over 130 clients were routed to Citi Match for execution without having assessed the clients as qualified investors and without providing them with the ALP Guidelines.
8. Although the affected clients appear to be qualified investors, CGMAL was still responsible for ensuring that they were fully informed as to how Citi Match operates by bringing the ALP Guidelines to their attention. The Consultation Conclusions Concerning the Regulation of ALPs have made it clear that *"no matter how sophisticated a qualified investor is, it would still be crucial for the investor to be provided with comprehensive and accurate ALP Guidelines for the assessment of the risks and features of an ALP."*

Conclusion

9. The SFC considers disciplinary action should be taken against CGMAL for its failures to ensure compliance with the ALP requirements under the Code of Conduct.
10. In reaching the resolution, the SFC took into account all relevant circumstances, including that CGMAL:
 - (a) took remedial actions to rectify the situation in August 2016 after the incorrect default setting issue was discovered in late July 2016. Subsequently, it also implemented enhanced measures to ensure compliance. The evidence suggests all users who were onboarded after August 2016 were qualified investors and were provided with the ALP Guidelines before their first access to Citi Match; and
 - (b) took the initiative to bring this matter to a conclusion by cooperating with the SFC to resolve the regulatory concerns.

⁵ Paragraph 19.2(f) defines "qualified investor" as a person: (i) falling under paragraphs (a) to (i) of the definition of "professional investor" in section 1 of Part 1 of Schedule 1 to the SFO; or (ii) within the meaning of sections 3(a), (c), (d)(i), (d)(iii) or (d)(iv) of the Securities and Futures (Professional Investor) Rules. Essentially, this includes all professional investors except those who are individuals