
FINAL NOTICE

To: Société Générale

Of: SG House, 41 Tower Hill, London

Dated 25 August 2010

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS (“the FSA”) gives you final notice about a requirement to pay a financial penalty:

1. ACTION

- 1.1. The FSA gave Société Générale (“SocGen” or “the Firm”) a decision notice on 23 August 2010 which notified the Firm that pursuant to section 206 of the Financial Services and Markets Act 2000 (“the Act”), the FSA has decided to impose a financial penalty of £1.575 million, in respect of breaches of rules set out in chapter SUP 17 of the FSA Handbook which occurred between 5 November 2007 and 24 February 2010 (“the Relevant Period”).

- 1.2. SocGen is an incoming EEA branch passporting into the UK under Article 32 of the MiFID Directive. It is authorised by Autorité des Marchés Financiers (AMF), the French regulator, and by the Central Bank of France (Banque de France), for prudential purposes. The FSA is taking action in accordance with the jurisdictional powers assigned to it in Article 32(7) of the MiFID Level 1 Directive. The FSA takes no action in respect of SocGen's systems and controls (which are a matter for the home state regulator under MiFID).
- 1.3. The Firm confirmed on 19 August 2010 that it will not be referring the matter to the Upper Tribunal (Tax and Chancery Chamber).
- 1.4. Accordingly, for the reasons set out below, the FSA imposes a financial penalty on the Firm in the sum of £1.575 million.
- 1.5. This penalty is discounted by 30% pursuant to the Stage 1 early settlement discount scheme. Were it not for this discount, the FSA would have imposed a financial penalty of £2.25 million on SocGen.

2. REASONS FOR THE ACTION

Summary

- 2.1. Accurate and complete transaction reporting is essential to enable the FSA to meet its statutory objectives of maintaining market confidence and reducing financial crime. The primary function for which the FSA uses transaction reports is to detect and investigate suspected market abuse, insider trading and market manipulation.
- 2.2. A transaction report is a data set submitted to the FSA and relates to an individual financial market transaction which includes (but is not limited to) details of the product traded, the firm that undertook the trade, the trade counterparty and the trade characteristics such as buy/sell identifier, price and quantity.
- 2.3. In the Relevant Period, SocGen breached Chapter 17 of the Supervision Manual, which is part of the FSA Handbook (SUP 17), by failing to submit accurate transaction reports in respect of approximately 18.8 million transactions, representing 80% of its reportable transactions.

2.4. Additionally, SocGen breached SUP 17 by failing to retain all relevant transaction reporting data at the disposal of the FSA for at least five years.

2.5. The FSA considers these failings to be serious, particularly because of:

- (1) the very high proportion of transaction reports which SocGen failed to report accurately across all of its asset classes, and the significant number of transaction reports rejected and not re-submitted;
- (2) the separate and distinct breach of failing to retain, at the disposal of the FSA, a proportion of SocGen's relevant transaction reporting data, which has prevented the reconciliation of that data with information held by the FSA;
- (3) despite an earlier acknowledgement within the Firm of the need to conduct a review of its transaction reporting regime, the Firm's inaction prevented it from performing the necessary tests and reporting the results to the FSA until May 2009;
- (4) the sustained period over which these failings endured and their impact on the FSA's ability to detect potential market abuse and reduce financial crime. As the FSA has sent a large number of the Firm's incorrect transaction reports to other competent authorities in compliance with the FSA's obligations under MiFID, the errors also create a serious risk of hampering other competent authorities' work in maintaining market confidence; and
- (5) the fact that SocGen's failures occurred during a period of heightened awareness around transaction reporting issues as a result of the implementation of the Markets in Financial Instruments Directive ("MiFID") and public statements by the FSA.

2.6. The Firm took a number of steps which mitigate the seriousness of its failings. These include:

- (1) commissioning a formal review of the SocGen transaction reporting processes and controls by external consultants;

- (2) conducting an internal audit of the accuracy and completeness of historical transaction reporting;
- (3) implementing a remediation project to address the issues and errors identified by the review and audit;
- (4) developing a quality control process to ensure the accuracy and completeness of future transaction reporting to the FSA; and
- (5) co-operating fully with the FSA in the course of its investigation.

Relevant regulatory provisions

- 2.7. The FSA is authorised pursuant to section 206 of the Act, if it considers that an authorised person has contravened a requirement imposed on him by or under the Act, to impose on him a penalty in respect of the contravention, of such amount as it considers appropriate.
- 2.8. Maintaining market confidence and the reduction of financial crime are statutory objectives for the FSA under section 2(2) of the Act.
- 2.9. The transactions which are required to be reported to the FSA are defined in SUP 17.1.4R as follows:

“A firm which executes a transaction:

- (1) *in any financial instrument admitted to trading on a regulated market or a prescribed market (whether or not the transaction was carried out on such a market); or*
- (2) *in any OTC derivative the value of which is derived from, or which is otherwise dependent upon, an equity or debt-related financial instrument which is admitted to trading on a regulated market or on a prescribed market;*

must report the details of the transaction to the FSA.”

- 2.10. The time period for making reports is stipulated in SUP 17.2.7R:

“A firm must report the required details of the transaction to the FSA as quickly as possible and by not later than the close of the working day following the day upon which that transaction took place.”

- 2.11. SUP 17.4.1EU provides:

“Reports of transactions ...shall contain the information specified in SUP 17 Annex 1 EU which is relevant to the type of financial instrument in question and which the FSA declares is not already in its possession or is not available to it by other means.”

- 2.12. SUP 17.4.2R provides:

“The reports referred to in SUP 17.4.1 ... shall, in particular include details of the names and the numbers of the instruments bought or sold, the quantity, the dates and times of execution and the transaction prices and means of identifying the firms concerned.”

- 2.13. SUP 17.4.3R provides:

“A firm must keep at the disposal of the FSA, for at least five years, the relevant data relating to all transactions in financial transactions which it has carried out, whether on own account or on behalf of a client...”

- 2.14. SUP 17.4.4G provides:

“The requirement to keep information at the disposal of the FSA means that a firm should maintain that information in such a form that it can be readily gathered and transmitted to the FSA upon request...”

- 2.15. Annex 1 to SUP 17 provides lists of fields and mandatory information to be provided as the minimum content of a transaction report.

- 2.16. The FSA’s approach to exercising its enforcement powers is set out in the Decision Procedure & Penalties Manual (“DEPP”) and Enforcement Guide (“EG”).

Facts and matters relied upon

Background

- 2.17. SUP 17 requires transaction reports containing mandatory details to be submitted to the FSA by the end of the next business day following the day on which the

firm entered into the transaction. At the end of each working day, transaction reports received by firms are loaded onto the FSA's transaction monitoring system.

- 2.18. Firms are able to report transactions to the FSA using one or more Approved Reporting Mechanisms ("ARMs"), which are specialised systems approved by the FSA for the purpose of transaction reporting.
- 2.19. The implementation of MiFID across all European Economic Area ("EEA") Member states on 1 November 2007 (effective on 5 November for transaction reporting) introduced changes to the list of products in which transactions had to be reported and standardisation of the list of fields which were required to be included in the reports. SUP 17 was amended from 1 November 2007 to reflect these changes. Whilst the changes required to be implemented by firms were significant in respect of their MiFID transaction reporting obligations the mandatory content of the transaction reports for many products remained largely unaffected by the MiFID changes.
- 2.20. The FSA has provided regular and detailed information to firms in its "Market Watch" publication on transaction reporting issues prior to and during the Relevant Period. In order to assist firms with transaction reporting generally and with respect to changes introduced by MiFID, the FSA issued a Transaction Reporting User Pack (TRUP) in July 2007.
- 2.21. Reminders were given by the FSA in Market Watch in March 2007 and June 2008 (Issues 19 and 28 respectively) and TRUP, that firms should regularly review the integrity of transaction report data.
- 2.22. Issue 28 of the Market Watch in June 2008 stated:

"Firms must report transactions to us accurately to help us monitor for market abuse and maintain market confidence. Accuracy in transaction reports also reduces the number of requests for clarification that we need to make to firms."

Therefore, we encourage all firms to review the integrity of their transaction report data regularly. Our Transaction Monitoring Unit is happy to provide firms a sample of reports we have received so that firms can check those transaction reports against their own records..."

We will be undertaking regular reviews of the quality and completeness of firms' submissions. We expect firms now to be fully compliant with the transaction reporting requirements set out in SUP 17. Where we identify problems with transaction reporting we will consider the use of our enforcement tools. In doing so, we will take into account the appropriateness of the firm's systems and controls, including its monitoring programme around transaction reporting."

SocGen transaction reporting processes

- 2.23. As a branch of an EEA authorised firm, SocGen was not required to comply with the FSA transaction reporting requirements prior to MiFID. Post-MiFID, the Firm's transaction reporting regime relied upon a variety of internal systems and external ARMs across its different business areas.
- 2.24. The Firm reported transactions during the Relevant Period in three asset classes: cash equities or "CAR"; equity derivatives or "DAI"; and "FICC", comprised of the Firm's bonds and credit derivatives businesses.
- 2.25. Within the CAR asset class existed a system whereby market side trades executed on the London Stock Exchange ("LSE") UK SETS Order Book platform were reported via an external ARM to the FSA. Facilitation of the reporting of the remaining CAR transactions was undertaken by Société Générale Securities Services ("SGSS").
- 2.26. Reporting of trades which fell within the DAI and FICC asset classes relied on processing by their respective internal systems and onward transmission by an external ARM.
- 2.27. A total of four distinct structures therefore existed within the SocGen transaction reporting process. No system of complete oversight of the process existed within SocGen during the Relevant Period.

Identification of transaction reporting problems

- 2.28. In May 2008, it was identified that a small proportion of CAR trades were affected by a price truncation issue, such that the price information did not incorporate prices in pence. This amounted to a systems error and the affected trades were remediated upon its discovery.

- 2.29. Prior to October 2008, SocGen recognised the need to undertake a complete review of its transaction reporting process, at least in respect of CAR transactions. However, this review was delayed, the Firm neglecting to request from the FSA relevant data extracts to permit the appropriate testing.
- 2.30. In December 2008, an internal report entitled “MiFID Implementation for FICC and CAFI/IFD Activities” was published. However, it identified no “major anomalies” in respect of the Firm’s transaction reporting regime.
- 2.31. In February 2009, the Firm requested and received from the FSA the relevant data extract, but did not make resources available to conduct the appropriate analysis.
- 2.32. In May 2009, the FSA was notified by the Firm of its failure to report an estimated total of 22,000 CAR market side transactions (and which later transpired to amount to approximately 32,000 transactions) executed on the International Order Book (“IOB”) of the LSE.
- 2.33. In June 2009, the Firm advised the FSA that approximately 324,000 transactions had been rejected due to the use of obsolete MIC codes. The rejections arose from a failure by SocGen, from February 2009 onwards, to act upon statements from the FSA advising that MIC codes for the Milan (XMIL) and Stockholm (XOME) exchanges had been updated and would no longer be accepted.
- 2.34. In July 2009, the Firm confirmed to the FSA the existence of an issue affecting trade times, and concerning 382 trades. This was the result of a systems error which allocated incorrect times to trades.
- 2.35. Also in July, the Firm instructed external consultants to review the design of their transaction reporting processes and controls, at the same time initiating a sample-based internal audit review of its historic transaction reporting.
- 2.36. In October 2009, the Firm contacted the FSA to advise that their external consultants’ report had revealed “*significant material deficiencies in processes*”, whilst the internal audit review had discovered “*material inaccuracies in the quality of reporting with large percentages of deals wrong or not reported*”. Both documents were disclosed to the FSA.
- 2.37. The Firm again contacted the FSA in October 2009 to advise of the identification of a system error which had resulted in a failure to report any trades executed after

2230hrs. The issue affected 10,165 transactions from August 2008, and was not identified previously due to the absence of adequate safeguards.

- 2.38. The external report dealt largely with processes and controls. As a matter of jurisdiction, the FSA is concerned only with systemic issues to the extent that they explain specific rule breaches.
- 2.39. The internal audit revealed significant discrepancies in both accuracy and completeness of reporting. However, its statistical approach, and specifically its limited sample selection was such that the audit could not be relied upon as a comprehensive review. Accordingly, the FSA commenced its investigation on 24 February 2010 and required a fully comprehensive review to be undertaken.
- 2.40. That comprehensive review, disclosed to the FSA in April 2010, revealed that approximately 17.1 million transactions had not been reported in accordance with SUP 17 requirements. The errors identified affected all business areas and included:
 - (1) 320,728 trades not reported at all
 - (2) 348,675 trades rejected and not re-submitted
 - (3) 16,432,043 transactions inaccurately reported including:
 - a) erroneous trade reference, date or time affecting 531,266 trades;
 - b) erroneous counter-party code affecting 14,655,723 trades; and
 - c) erroneous instrument description affecting 100,765.
- 2.41. Further to that review, other issues affecting the quality of the Firm's transaction reporting were identified by the FSA and the Firm, resulting in the following additional errors:
 - (1) 4,929 trades not reported at all
 - (2) 1,678,218 transactions inaccurately reported due to:
 - a) erroneous trade times; and
 - b) erroneous MIC codes.
- 2.42. The trade times issue in fact affected 10,430,063 transaction reports, the majority of which were afflicted by other errors and therefore had already been identified under alternative heads as inaccurate reports.

- 2.43. It also emerged in the course of the review, that the Firm was unable to readily retrieve transaction data, upon request from the FSA, across two asset classes over sustained periods following MiFID implementation. Whilst extrapolated figures were used to reasonably estimate the level of errors affecting these classes, the failure to retain records of itself constitutes a breach of SUP 17.4.3 R.

Inadequate transaction reporting process post MiFID implementation

- 2.44. The breaches of SUP17 described above arose and persisted throughout the Relevant Period, due in part to the following factors:

- a) transaction reporting within the Firm was not subject to a level of risk assessment, review and monitoring commensurate with that appropriate for what is a fundamental regulatory obligation;
- b) there was a widespread use of inaccurate static data, or a misapplication of accurate static data across all business lines. This failing is principally responsible for the accumulation of the inaccurate reports;
- c) the Firm lacked a co-ordinated and effective procedure for ensuring re-submission of reports following rejection; and
- d) post-MiFID implementation, the Firm did not seek to obtain from the FSA, data extracts with which to conduct appropriate testing until February 2009. That testing was not performed and reported to the FSA until May 2009, and when eventually undertaken, it became apparent that an earlier internal report in December 2008 had failed to identify the problems in existence.

Analysis of Breaches

- 2.45. During the Relevant Period, SocGen was in breach of SUP 17.1.4 R by failing to report transactions entirely or by failing to resubmit rejected reports.

Description	Transactions <i>not reported</i> in the Relevant Period
Transactions not reported at all	325,657
Transactions submitted but rejected, and not resubmitted	348,675

- 2.46. During the Relevant Period, SocGen was in breach of SUP 17.4.1 EU by inaccurately reporting transactions.

Description	Transactions <i>inaccurately reported</i>
Total number of inaccurate reports	18,110,261
Percentage of reportable transactions inaccurately reported	77%

- 2.47. The sum of SocGen's transactions reports in breach of SUP 17 during the Relevant Period is therefore:

Description	Transaction reports in breach of SUP 17
Total number of reports in breach	18,784,593
Percentage of reports in breach	80%

- 2.48. During the Relevant Period, SocGen was in breach of SUP 17.4.3 R by its failure to retain at the disposal of the FSA, for at least five years, the relevant data relating to all transactions in financial instruments

Asset class	Period for which data unavailable to the FSA
FICC	5/11/07 - 15/05/08
DAI	5/11/07 - 16/07/08

3. SANCTION

- 3.1. The FSA's policy on the imposition of financial penalties and public censures is set out in DEPP and EG. In determining the financial penalty, the FSA has had regard to this guidance. The principal purpose of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefits of compliant behaviour.
- 3.2. The FSA considers that the seriousness of this matter merits the imposition of a significant financial penalty.
- 3.3. The FSA has had regard to the following factors:
 - (1) the vast proportion of transaction reports which the Firm failed to report accurately across all of its asset classes, and the significant number of transaction reports rejected and not re-submitted;
 - (2) the separate and distinct breach of failing to retain, at the disposal of the FSA, a proportion of SocGen's relevant transaction reporting data; which has prevented reconciliation of that data with information held by the FSA;
 - (3) despite an earlier acknowledgement within the Firm of the need to conduct a review of its transaction reporting regime, the Firm's inaction prevented it from performing the necessary tests and reporting the results to the FSA until May 2009;
 - (4) the sustained period over which these failings endured, and their impact on the FSA's ability to detect potential market abuse and reduce financial crime. As the FSA has sent a large number of the Firm's incorrect transaction reports to other competent authorities in compliance with the FSA's obligations under MiFID, the errors also create a serious risk of hampering other competent authorities' work in maintaining market confidence; and

- (5) the Firm's failures occurred during a period of heightened awareness around transaction reporting issues as a result of the implementation of MiFID and public statements by the FSA.
- 3.4. The FSA has also had regard to the following steps taken by the Firm, which mitigate the seriousness of its failings. These included:
- (1) commissioning a formal review of the SocGen transaction reporting processes and controls by external consultants;
 - (2) conducting an internal audit of the accuracy and completeness of historical transaction reporting;
 - (3) implementing a remediation project to address the issues and errors identified by the review and audit;
 - (4) developing a quality control process to ensure the accuracy and completeness of transaction reporting to the FSA going forward; and
 - (5) full co-operation with the FSA throughout its investigation.

4. CONCLUSIONS

- 4.1. The FSA considers in all the circumstances that the seriousness of the breaches merits a substantial financial penalty. In determining the financial penalty the FSA has considered the need to deter SocGen and other firms from committing similar breaches. The FSA has also had regard to penalties in other similar cases.
- 4.2. The FSA considers that a financial penalty of £2.25 million is appropriate, discounted to £1.575 million after the applicable Stage 1 discount for early settlement.

5. DECISION MAKERS

- 5.1. The decision which gave rise to the obligation to give this Notice was made on behalf of the FSA by the Settlement Decision Makers.

6. IMPORTANT

- 6.1. This Final Notice is given to SocGen in accordance with section 390 of the Act

Manner of and time for Payment

- 6.2. The financial penalty must be paid in full by the Firm to the FSA by no later than 8 September 2010, 14 days from the date of the Final Notice.
- 6.3. If all or any of the financial penalty is outstanding on 9 September 2010, the FSA may recover the outstanding amount as a debt owed by the Firm and due to the FSA.

Publicity

- 6.4. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to you or prejudicial to the interests of consumers.

FSA contacts

- 6.5. For more information concerning this matter generally, SocGen should contact Celyn Armstrong (020 7066 2818) or Kenneth McArthur (020 7066 4120) at the FSA.
-

Tracey McDermott

Head of Department

FSA Enforcement and Financial Crime Division