Subject: ITE302x

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Answer to Assignment 2

***1. Peter Gumble, European editor for Fortune magazine, comments, “Kerviel is a stunning example of a trader breaking the rules, but he’s by no means alone. One of the dirty little secrets of trading floors around the world is that every so often, somebody is caught concealing a position and is quickly—and quietly—dismissed…. [This] might be shocking for people unfamiliar with the macho, high-risk, high-reward culture of most trading floors, but consider this: the only way banks can tell who will turn into a good trader and who won’t is by giving every youngster, it hires a chance to show his mettle. That means allowing even the most junior traders to take aggressive positions. This leeway is supposed to be matched by careful controls, but clearly they aren’t foolproof.”***

***What is your reaction to this statement by Mr. Gumble?***

I maybe someone who is “unfamiliar with the macho, high-risk, high-reward culture of most trading floors” as mentioned in Mr Gumble’s statement so I am a bit surprised to find out how these systems work under the deep level, not just on the surface.

I think there will be no right or wrong about this statement because Mr Gumble just share some information, or so-called secrets.

The case of Kerviel may set a bad example of putting a youngster in an inappropriate position and I think part of the responsibility in this case is the oversight of SocGen company. However, I believe banks have more than that one option of “*allowing even the most junior traders to take aggressive positions”,* such as keeping them as assistant under good control of someone with more experience, or testing their code of ethics under certain circumstances, assigning them small tasks first.

Three types of computer crime were mentioned in this module: for money, for socio-political reasons, and government who attack its citizens. As mentioned in the article, Kerviel’s motivation belongs to the first category, simple to “boost his income by making successful trades far beyond his trading limits, thus earning large bonuses (his total salary and bonus for 2007 was a relatively modest €94,000)”

***2. What can there be an explanation for the failure of SocGen’s internal control system to detect Kerviel’s transactions while Eurex detected many suspicious transactions?***

First, I think the problem with SocGen’s internal control system is that they lay too much trust on an individual instead of a team and they lack in frequent checks and updates to see if something is wrong with the system. Second, there seem to be some security holes in SocGen’s control system. In addition, the company seemed to be too relaxed upon warnings from a third party about the risks involved “The SocGen risk-control expert used information provided by Kerviel and his supervisor as well as a compliance officer at a SocGen subsidiary as the basis of both of his replies to Eurex”

On Kerviel’s side, I believe he has great skills in computer. Specifically, he was able to evade the famous internal controls system in SocGen and take advantage of the trust his boss gives him to continue his fraud for such a long time.

On Eurex’s side, they detected the problem and sent out warnings but it was not done thoroughly “Following another two-week delay, SocGen provided further details, and both Eurex and SocGen let the matter drop”. In this case, Eurex could have reported to an independent investigative agent for further investigation.

The economic impact of the security problems is significant. The company’s fame is heavily tarnished, its market value dropped 50 percent over the course of just a few months and a loss of more than €4.9 billion.

Finally, there were severe ethics problems in this case. First, as regards JK, he clearly took advantage of his position as a trader to exceed his trading limit to get money for himself. Even after Eurex’s warnings, he continued his misconduct to cover his crime. Second, SocGen discovered the problem but just let it be instead of acting upon it. Third, Eurex should have been more radical in their investigation to prevent further losses.