



Analysis of Problems and Suggestions of “Counterfeit Seal”: A Case Study of “Sealand Securities”

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Abstract. The current market environment is complex and full of uncertainties. The counterfeit seal incident of Sealand Securities has exposed serious problems in its business structure, risk assessment, and internal supervision. This paper mainly studies and analyzes the problems of Sealand Securities, such as unreasonable business structure, unreasonable risk assessment, and internal supervision loopholes, and puts forward relevant suggestions. By means of business diversification, risk stratification management, and digital supervision, the company's compliance and risk-resistant ability can be improved, and similar incidents can be avoided. This study builds a comprehensive governance framework that includes the ‘triple line of defense’ mechanism and digital regulatory tools and provides operational solutions for securities companies to improve their internal control systems. Its value lies in revealing the risk transmission mechanism in aggressive expansion, innovatively applying smart seal and AI monitoring technology to financial supervision and providing reference for the industry to establish a synergistic system of ‘business, risk control, and supervision.’

Keywords: Internal Control, Business Structure, Risk Assessment, Internal Regulation.

1 Introduction

Enterprise internal control is the core to ensure the stable development of enterprises. A perfect internal control system can not only effectively prevent the risk of fraud and ensure the reliability of financial reporting but also enhance operational efficiency and safeguard asset security. By standardizing business processes and establishing a monitoring mechanism, it can enable enterprises to detect and correct operational errors in a timely manner, effectively reduce compliance risks, and help them achieve sustainable development.

In 2016, the turnip stamp incident broke out in Sealand Securities. The incident was due to a former employee of the company's bond team privately engraving a company seal and carrying out bond proxy transactions in the name of Sealand Securities in violation of the law, involving a huge amount. The incident had a huge impact on the bond market, triggering a market trust crisis and serious damage to the company's reputation, and caused the Securities and Futures Commission to suspend part of the business of

Sealand Securities for up to a year and impose a heavy fine. In addition, the incident caused the company's net profit to plummet by nearly 80 percent that year, which directly pushed the regulators to supervise the industry's internal controls.

This study takes the 'carrot chapter' incident of Sealand Securities as a typical case and analyzes in depth the systemic risk control deficiencies exposed in the rapid growth of business in the securities industry. This paper analyzes the core issues from three dimensions, and the results build a complete set of integrated governance solutions, which provide reference for the industry and are of great significance for the prevention of systemic financial risks.

2 Problems

2.1 Unreasonable Business Structure

Firstly, Sealand Securities relied heavily on high-risk businesses and neglected compliance management. Employees bypassed the company's approval process by privately engraving official seals and privately carrying out bond-holding transactions, reflecting a serious mismatch between the proportion of high-risk business in the business structure and the internal control capacity; second, the company's business expansion speed is not proportional to the risk control capacity. Sealand Securities radically expanded its bond business to achieve the purpose of rapidly increasing market share, but the supporting risk control system and personnel management could not reach the same level. The business structure attached importance to short-term interest orientation, ignoring long-term risk control. In addition, the enterprise business model was single, and risk-resistant ability was insufficient [1]. Sealand Securities focuses its attention on bond self-management and proxy trading, which are highly affected by market fluctuations and liquidity, and when a market downturn occurs or a credit risk arises, the business structure of the enterprise will magnify the loss of the enterprise, and compared with comprehensive brokerage firms, Sealand Securities has a weaker layout of low-risk business, leading to excessive concentration of risk; finally, the organizational structure of the enterprise and information isolation fail. The failure to identify forged official seals in a timely manner exposed loopholes in the firm's compliance review, and employees covered up risks by concealing counterparties and forging documents, reflecting a lack of collaborative supervision between corporate departments [2].

2.2 Unreasonably Assessed Risks

Firstly, Sealand Securities did not pay attention to the risk of operation [3]. Employees privately engraved official seals to sign the escrow agreement for months undetected, reflecting that the management did not pay attention to the assessment of the operational risk of the internal staff of the enterprise and lack of review and supervision; second, the internal compliance risk and legal risk awareness of Sealand Securities is weak. Employees signed the escrow agreement in a way that violated the regulatory requirements, while Sealand Securities did not classify it as a high-risk behavior, and the forged contract was not substantively reviewed by the relevant departments, reflect-

ing the insufficiency of the risk assessment mechanism of the authenticity of the contract of Sealand Securities; in addition, the impact of the extreme volatility of the market was not prejudged, and the leverage risk was ignored. The bond market underwent a drastic adjustment in 2016, but the risk of Sealand Securities on escrow was not taken seriously. Equity's market price fluctuation risk lacked dynamic assessment. The high leverage attribute was hidden in the escrow transaction, but Sealand Securities did not reasonably assess the possibility that the leverage would strengthen the loss; and finally, the imperfection of the risk early warning mechanism and contingency plan. No early warning was set for key indicators, leading to the accumulation of risks and inaction. In the face of the chain reaction triggered by the market decline, the company lacked the preparation of an emergency plan and could only be forced to deal with the situation, further reflecting the lack of reasonable assessment of risks and the disconnection of emergency management [4].

2.3 Loopholes

First of all, the internal control process of Sealand Securities is in vain [5]. The use of the entity's official seal is not strictly approved and recorded, and the employees involved in the private engraving of the official seal avoid the use of the company's seal process. With the development of the business model and the degree of digitalization, the traditional supervision model of the enterprise is not sufficient to maintain full-spectrum supervision of the enterprise [6]. Bonds on behalf of the transaction are not in accordance with the provisions of the enterprise-level, level-by-level approval; the employees involved in the forged documents or fictitious information about the other side of the direct operation reflect the lack of an in-depth internal approval process. Secondly, the internal information isolation of Sealand Securities and the failure of the reporting mechanism. The lack of real-time synchronization between the transaction data and the central control system and the fact that the clearing department relies mainly on manual transmission of information resulted in the management not being able to obtain a complete transaction mapping in a timely manner, employees deliberately concealing the transactions, and some of those who knew about the transactions choosing to remain silent due to their interests, which reflects the lack of smooth reporting of irregularities; in addition, the failure of the authority allocation and checks and balances mechanism of the Sealand Securities. Branches are given too much authority, resulting in employees being able to carry out high-risk business on their own, and employees at the same time master the transaction decision-making, contract signing, and risk management authority, so that the responsibilities of different positions are mixed, making it more convenient to cover up the irregularities of the operation; finally, the technological system of Sealand Securities and the monitoring tools are backward [7]. Enterprises have not established a monitoring platform for real-time transactions, are unable to automatically warn of abnormal transactions, and the key links are more dependent on manual labor, without introducing relevant technical means.

3 Solutions

3.1 Optimizing Business Structure

Compress the scale of high-risk proprietary trading of Sealand Securities, set a cap on the scale of high-risk businesses such as bond holding and leveraged trading, and ensure that their proportion of net assets meets regulatory requirements. Gradually shift the business center to capital-light businesses such as investment banking and asset management and increase the proportion of fee income. Promote a diversified business layout, focus on core competencies, and select complementary tracks. Collect existing strengths, identify extendable areas, and select areas with strong synergies with the main business and fast market growth [1]. Carry out resource synergy and establish a unified data center to support customer profiling and risk pricing for multiple business lines. Withdraw from inefficient business areas, clean up non-core business, and return capital for strategic direction investment. Avoid blind expansion and establish evaluation mechanisms. New businesses need to pass strict screening, simulate contingency plans for new businesses with excessive losses, and set up an exit mechanism for businesses with consecutive huge losses and no improvement trend. High-risk businesses should be operated by independent legal entities, while internal and external risk penetration management should be carried out to avoid the transmission of hidden leverage.

3.2 Systematic Risk Assessment Framework

Firstly, Sealand Securities should clarify the core dimensions of risk assessment, risk classification, and the priority ranking of operational risk, market risk, compliance risk, reputation risk, and technology risk. Secondly, the first layer of defense is constructed as self-examination of the business department; the business team fills in the Risk Self-Examination Form before each transaction, carries out embedded risk assessment, and at the same time does a good job of case matching; the second layer of defense is the independent supervision of the risk control department, which simulates the situation of employees' private engraving of official seals and defaults on behalf of the employees carries out stress tests, and analyzes the employees' operation records through AI, and triggers an early warning if there is any abnormal operation; the third layer of defense is the internal auditing and The third line of defense is the internal audit and rectification tracking; the internal audit department randomly checks the original high-risk business documents and timely implementation of rectification of the 'triple line of defense' mechanism [8-9]. In addition, the deployment of key technical systems of Sealand Securities, the establishment of a risk data center, the integration of trading systems, risk control systems, external data sources, and the establishment of a unified risk data lake [7]. Finally, risk assessment is added to the business process of Sealand Securities, and the management is required to submit the Risk Heat Map to the board of directors on a regular basis and mandatory disclosure of major risk events to the regulatory reporting within 24 hours.

3.3 Strengthening Technical Supervision

Strengthening the independence and authority of the internal supervision of Sealand Securities and actively build the 'three lines of defense' and the joint regulatory bodies,

the use of separation of powers, and checks and balances for key positions [10]. At the same time, with digital penetration of the risk blind spot, the use of an intelligent seal system, the official seal built-in IoT chip, with the seal automatically collecting its location, time, the use of the seal of biological information, and timely record, so that the forged seal cannot be carried out. Scanning the difference in microscopic characteristics between document seals and filing impressions. Introduce blockchain deposit technology in key contracts to ensure that they are not tampered with [11]. In addition, build a real-time risk monitoring platform for Sealand Securities, deploy an AI monitoring system to identify abnormal behavior of employees, scan for keywords of risk in communications, and use network analysis to draw a correlation map of counterparties [5]. Establish a permission matrix with a real-time adjustment mechanism that automatically shrinks trading privileges when market volatility exceeds a threshold. For departing personnel, complete authority recovery within 72 hours to reach digital footprint removal. Integrate internal systems and external data to establish dynamic risk mapping. Functional threshold management for indicators such as bond substitution and leverage.

4 Conclusion

The ‘counterfeit seal’ incident of Sealand Securities exposed the internal control deficiencies that existed in the securities industry in the midst of high-speed expansion, and in 2016, employees of Sealand Securities illegally carried out bond trading by engraving official seals, reflecting the systemic loopholes of financial institutions in terms of their business structure, risk assessment, and supervisory system. This paper also analyzes in depth the three core issues: the contradiction between excessive concentration of high-risk business and lack of internal control, the absence of dynamic risk assessment mechanisms, and the existence of technical and management blind spots in the supervisory system. Targeted solutions such as business structure optimization, intelligent risk control system construction, and blockchain supervision technology application are proposed. A comprehensive governance framework has been constructed, which provides a reference for improving the internal control system of enterprises in the future.

This study is mainly based on a single case and lacks first-hand information within the enterprise, so the feasibility and universality of the solutions need to be fully verified. In addition, the cost and adaptability of the technology implemented are not fully explored. The implementation of policies may face internal resistance or legal enforcement difficulties.

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