

# OTHER TOPICS RELATING TO THE SFO

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## Complaints officer or emergency contact person

Can an unlicensed staff member be nominated as a complaints officer or an emergency contact person of a licensed corporation?

Posted on 17.3.2003

(1) Yes. For group companies, it is preferable that the emergency contact person should have sufficient authority and be familiar with the overall affairs of the group.

## Submission of audited accounts

Under the previous regime, an investment adviser or commodity trading adviser firm was only required to submit its audited accounts on the anniversary date of its licence. Thus, the submission period may be longer than 4 months after its financial year-end, which is the period during which submission by a licensed corporation has to be made under the SFO. The question is, if the financial year end of a deemed licensed corporation, which was previously a registered investment adviser or commodity trading adviser, falls on 31 March 2003, when will it be required to submit its audited accounts for that relevant financial year?

Posted on 16.4.2003

(2) The licensed corporation will be required to submit its audited accounts for the financial year ended 31 March 2003 on the anniversary date of its licence. However, its audited accounts for the year ending 31 March 2004 will have to be submitted by 31 July 2004, and not on the anniversary date of its licence. It may be added that if such a licensed corporation's financial year end falls on or after 1 April 2003, it will be required to submit its audited accounts within 4 months of its financial year end.

## Notification on change of information

For entities belonging to the same group of companies, is it acceptable for a licensed corporation (or registered institution) to make a notification required under the Securities and Futures (Licensing and Registration)(Information) Rules (Information Rules) on its behalf and on behalf of other group entities in respect of the same change in information?

Posted on 18.6.2003

(3) Yes. In the case of entities belonging to the same group, a licensed corporation (or registered institution) may make a notification required under the Information Rules on its behalf and on behalf of other group entities in respect of the same change in any specific information. The notification should state clearly on whose behalf it is made, and the represented entities should be aware of the notification. In addition, the necessary information should be provided. For example, in the case of the resignation of a licensed representative (or director), the use of Form 5 with the provision of the required information would be appropriate.

The Information Rules (Item 2 of Part 3, Schedule 3) require a licensed representative to notify the SFC of changes in the status of any authorization to carry on a regulated activity in Hong Kong or elsewhere. In the case of registrations to carry on regulated activities in the United States, please clarify my understanding that the notification requirement is aimed at registrations with the Securities and Exchange Commission (SEC), National Association of Securities Dealers (NASD), Commodity Futures Trading Commission (CFTC) and National Futures Association (NFA) only.

Posted on 04.03.2005

3(a) In regard to registrations with the regulatory authorities in the United States, the focus of the notification requirements is on registrations with the SEC, NASD, CFTC and NFA.

## Premises for keeping records or documents

If a licensed corporation outsources the administration functions such as data processing to a service provider, does it need to apply for approval under section 130 of the SFO in respect of the premises of that service provider for keeping records or documents?

Posted on 18.6.2003

(4) If the original documents are kept by the licensed corporation at its approved premises and only imaged records or data are sent to the service provider for processing and the processed data is also maintained by the licensed corporation, it is not necessary for the licensed corporation to seek approval from the SFC in respect of the premises of the service provider for keeping records or documents.

However, the licensed corporation is required to notify the SFC of such outsourcing arrangement in compliance with the Securities and Futures (Licensing and Registration)(Information) Rules.

If a licensed corporation sets up new branches, does it need to apply for approval under section 130 of the SFO in respect of the premises of each branch?

Posted on 18.6.2003

(5) You will need to seek approval for the premises of each branch office. This is so even for those licensed corporations which transfer all their records from the branches to the head office because it is likely that at some points in time, there may be records kept by the branch but not in the head office.

Certain records or documents of an intermediary are required to be kept at the premises approved by the SFC under section 130 of the SFO. Will the SFC approve overseas premises under section 130 of the SFO?

Posted on 1.8.2007

(6) It is not the SFC's practice to approve overseas premises for the keeping of records or documents under section 130 of the SFO.

The reason why the SFC will only approve premises that are located in Hong Kong is that section 130 of the SFO must be read in the light of the SFC's related powers under Parts VI and VIII of the SFO and the related obligations of intermediaries in respect of the keeping of their records. The SFC, by way of example, has the power under Part VIII of the

SFO to enter premises to inspect the records of an intermediary, but would be precluded from exercising this power in the event of the premises being located outside Hong Kong. By way of further example, the Securities and Futures (Keeping of Records) Rules stipulate the records that must be kept by intermediaries and that they must be kept in a manner that will enable an audit to be conveniently and properly carried out.

The SFC considers that, in the event of it approving overseas premises under section 130 of the SFO, these types of powers and obligations could be undermined. Accordingly, the SFC insists that all records and documents required to be kept by an intermediary under the SFO must be kept at approved premises in Hong Kong.

My firm is considering outsourcing some of the back office functions to a third party. If some of the records or documents of my firm are kept outside Hong Kong by the service provider, would it be necessary for my firm to obtain the SFC's approval for the overseas premises under section 130 of the SFO?

Posted on 1.8.2007

(7) The SFC recognises that outsourcing practices involving overseas third parties are sometimes adopted by intermediaries and that these practices might involve identical records or documents being contemporaneously kept both at the overseas premises of such a third party and at the Hong Kong premises of an intermediary which have been approved by the SFC under section 130 of the SFO. However, the SFC does not interpret section 130 as requiring such overseas premises to be approved under section 130.

Intermediaries are reminded that these outsourcing practices do not in any manner alter the obligations of an intermediary at all times to keep all required records or documents at the premises in Hong Kong that have been approved by the SFC under section 130 of the SFO.

If an intermediary enters into an outsourcing arrangement of the type mentioned above, it must ensure that all relevant records or documents, which are kept by an overseas

third party, are also contemporaneously kept by the intermediary in an appropriate form (including electronic) at the Hong Kong premises that have been approved for this purpose by the SFC under section 130.

Corporation provides asset management, advising on securities and advising on futures contracts to its group company

In Schedule 5 to the SFO, the definition of “asset management” excludes a corporation providing portfolio management service solely to any of its wholly owned subsidiaries, its sole holding company or other wholly owned subsidiaries of that holding company. Similar exclusions are also provided in the definitions of “advising on securities”, “advising on futures contracts” and “advising on corporate finance”.

(i) Does this mean that a Hong Kong corporation providing portfolio management service under a delegation agreement on behalf of its group company (which may be an offshore fund manager) need not be licensed to provide asset management service, notwithstanding that the assets under management belong to the clients of that group company?

(ii) If the Hong Kong corporation were to only advise its group company on securities/futures contracts, does it need to be licensed to advise on securities/futures contracts?

Posted on 10.3.2004

(8) (i) The group company exclusion is only applicable to a corporation providing asset management service to its group company (on a wholly owned basis) in respect of that group company’s assets. It should not be read as applying to the management of assets belonging to the group company’s clients. Managing assets belonging to third parties would constitute “asset management” and attract a licensing requirement.

(ii) In the case of the Hong Kong corporation advising its group company pertaining to the investment of that company’s assets, the exclusion should apply, but it should not be read as applying to the Hong Kong corporation advising its group company in respect of that group company’s client assets. However, where the investment advice and/or related research reports are provided to the group company for its own consumption, notwithstanding that the group company may rely, in whole or in part, on such

advice/research reports to service its clients, the above exclusion will still apply if the advice/research reports are issued to the clients by the group company in its own name and that group company has assessed the Hong Kong corporation's input before issuing such advice/research reports.

## Hedging activities

Our company was previously registered as an Investment Adviser to carry on the business of asset management under the former regime. According to the transitional provisions under the Securities and Futures Ordinance, it is now deemed to be licensed for Type 9 regulated activity (asset management) apart from other types of regulated activity. Its deemed licence is also subject to a condition that it may not provide a service of managing a portfolio of futures contracts for another person. In this circumstance, can it carry out hedging of the investment portfolios under its management by using futures contracts?

Posted on 26.6.2003

(9) No. This is because the company's deemed licence is subject to the condition that it may not provide a service of managing a portfolio of futures contracts for another person. However, it may apply to the SFC for uplifting of the licensing condition concerned under section 134(1) of the Securities and Futures Ordinance. In that regard, it must demonstrate that it is competent to carry out the proposed functions in relation to futures contracts. The applicable fee is \$2,000.

## Display of licence or certificate of registration

Under section 3 of the Securities and Futures (Miscellaneous) Rules, an intermediary is required to display its licence (or copy) in a prominent place at each of its place of business.

What is a prominent place?

In displaying copies of its licence, can an intermediary display copies that are of smaller size (A4 size) instead of the original A3 size?

Posted on 23.06.2004

(10) A prominent place is where the licence (or certificate of registration) so displayed can be easily seen by the intermediary's clients, such as the client reception area.

Copies not smaller than the A4 size are acceptable if they are prominently displayed and can be clearly seen by clients.

Under section 3 of the Securities and Futures (Miscellaneous) Rules, an intermediary is required to display its licence (or copy) in a prominent place at each of its place of business.

If an intermediary's place of business consists of several floors in the same building, does the intermediary need to display the licence at each floor?

Posted on 16.9.2003

(11) If the intermediary's business place consists of more than one floor in the same building, it may not be necessary to display the licence at each of the floors if all the floors share a common client reception area and the licence is displayed therein.

## Board Resolution for licensing / registration applications

In the licensing/registration application forms for licensed corporations/registered institutions/responsible officers, the applicants are required to declare that the board of directors has passed a resolution approving the application.

Would it be sufficient if the board has passed a resolution authorizing a specified committee or person to approve the application?

Posted on 6.10.2003

(12) It would be acceptable if the board of directors has passed a resolution approving/authorizing a specified committee or person to approve the application and that committee or person has so approved the application.

## Approval dates of licence / regulated activity / accreditation

I am a licensed individual. Where can I find the approval dates of my licence, (each) regulated activity, and accreditation to my existing principal(s)?

Posted on 4.2.2004

(13) These approval dates can be found in the **Public Register of Licensed Persons and Registered Institutions** on the SFC's website at <http://www.sfc.hk/sfc/html/EN/intermediaries/trading/licensed/licensed.html>

## Disclosure of warning record

I am applying for a representative licence and I had previously received a warning from a regulator many years ago. Do I have to disclose such a warning record in the application form?

Posted on 25.4.2005

(14) Where the warning was not issued by the SFC, you should disclose such a warning record in the application form (Question 4.1 of Form 3) to enable the SFC to make an assessment on a fully informed basis.

If I disclose to my employer the fact that I had previously received a warning letter from the SFC, will I be in breach of any secrecy provisions of the SFO.

Posted on 4.2.2004

(15) The SFC is of the view that such a disclosure (including the content of the warning letter) does not breach any secrecy provisions of the SFO.

## Business Premises

My firm is applying for a licence to become an asset manager in Hong Kong. I heard that the SFC does not allow licensed firms to carry on their businesses in business centres or shared offices, or to move regularly from one office to another. Is this true?

Posted on 7.5.2007

(16) The SFO and its related rules do not prescribe the type of office from which a licensed corporation must operate. However, the business premises that a firm chooses must be suitable for the business activities that it has been licensed under the SFO to carry on.

Licensed corporations must ensure, at all times, that their office arrangements are suitable. This is a continuing obligation and any failure to comply with it will give rise to concerns on the part of the SFC and might well result in the SFC taking regulatory action.

As a matter of general principle, the SFC does not distinguish business centres or shared offices from other types of business accommodation. However, there will be some business centres or shared office arrangements which the SFC will not regard as suitable, particularly where self-contained and secure space is not available.

The SFC is not in favour of firms regularly moving from one temporary office to another and encourages licensed corporations to carry on business from a “fixed abode”.

As a matter of general principle, a licensed corporation should satisfy itself that the business premises occupied by it are appropriately secure and that confidential/non-public information (such as price sensitive information) and client privacy will be

sufficiently safeguarded against unauthorized access or leakage.

In considering whether the location of a licensed corporation's office in particular premises is appropriate, the following factors would suggest that premises are likely to be unsuitable for that purpose:-

- Where there is no secured and properly segregated office area, which is able to be locked and which is designated for the firm's own and exclusive use, and in which its business records, particularly those relating to clients, are able to be securely held;
- Where essential office equipment and telecommunication systems are installed in such a way that they are not situated within an enclosed area that is secure and accessible only by the firm's staff and authorized personnel;
- Where no or insufficient measures are taken to prevent confusion to clients that might be caused by the existence of other

business entities occupying the same premises;

- Where the nature of the firm's business demands frequent face-to-face dealings / meetings with clients at the firm's premises, during which client information and instructions are likely to be exchanged, and practical difficulties exist in the firm being able to ensure confidentiality during such meetings;
- Where the firm has not ensured that its office premises will always be accessible for all formal regulatory visits, including investigations and inspections.

Although the above factors are considered by the SFC to be of principal concern to it in respect of the appropriateness or otherwise of business premises occupied by licensed corporations, they should not be considered to constitute an exhaustive list because circumstances might exist in certain situations that give rise to particular accommodation needs or requirements. Licensed corporations have an ongoing obligation to

anticipate such matters and to ensure that their business premises are, at all times, suitable for the purposes for which they are being used.

Can a compliance officer or in-house legal counsel obtain a licence under the SFO?

Posted on 11.5.2009

(17) Normally, the SFC will not license back office staff, including compliance officers and in-house legal counsel.

If a person who is employed by a licensed corporation in such a role does not perform functions that directly relate to the conduct of the regulated activity for which the corporation is licensed, the SFC will neither license him/her as a representative nor approve him/her as a responsible officer.

The SFC takes the view that competent compliance officers or in-house legal counsel do not necessarily possess the qualifications and experience necessary to be approved as responsible officers. Frequently, they do not possess such qualifications and experience.

The SFC also considers that the functions of compliance officers and in-house legal counsel are inherently different from those of representatives who are licensed to carry on

regulated activities for the licensed corporation to which they are accredited. One of the primary functions of a licensed corporation's compliance officer or in-house legal counsel is to ensure regulatory compliance both on the part of the licensed corporation and also on the part of the licensed representatives accredited to it. As a matter of general principle, the SFC considers it necessary for there to be segregation between the performance of this function and the performance of the activities that constitute the carrying on of regulated activities. Without such segregation, there would be inherent conflict arising out of a compliance officer or in-house legal counsel carrying on the regulated activities for which the corporation employing him/her is licensed and, at the same time, being responsible for supervising such activities for the purposes of regulatory compliance.

This is underscored in paragraph 1 of Part V of the SFC's Management, Supervision and Internal Control Guidelines For Persons Licensed By or Registered with the Securities

and Futures Commission, which states, *“Management establishes and maintains an appropriate and effective compliance function within the firm which, subject to constraint of size, is independent of all operational and business functions, and which reports directly to the Management”*.

As a matter of general principle, compliance officers and in-house counsel who are employed by a licensed corporation should refrain from carrying on the regulated activities for which the corporation is licensed.