

Securities and Futures (Financial Resources) Rules



FRR in support of the single licensing regime

- ◆ Liquid capital requirement to replace net tangible asset requirement currently applies to advisers
- ◆ Where a licensed corporation conducts more than one regulated activity, the highest applicable required liquid capital floor requirement and minimum paid-up capital requirement shall apply

Transitional period

Advisers/ Asset Managers

- 6-month grace period, s.t. continuous compliance with \$500,000 NTA requirement

Exempt dealers/advisers

- Deemed licensed from effective date of SFO
- 6-month grace period

Required liquid capital (RLC)

- ◆ The higher of
 - “Floor” requirement
 - Variable required liquid capital (VRLC)
- ◆ VRLC =
 - 5% of the aggregate of
 - adjusted liabilities
 - initial margin requirements and/or amount of margin required to be deposited in respect of clients’ open f/o positions
 - In case of forex traders, + 1.5% of aggregate gross foreign currency position

RLC - Floor requirement

<u>Type</u>	<u>Requirement</u>
Dealing in securities	\$3M (<i>\$0.5M for approved introducing agent or trader</i>)
Dealing in futures contracts	\$3M (<i>\$0.5M for approved introducing agent, non-clearing dealer or trader</i>)
Leveraged foreign exchange trading	\$15M (<i>\$3M for approved introducing agent</i>)
ATS	\$3M
Securities margin financing	\$3M

RLC - Floor requirement (cont'd)

<u>Type</u>	<u>Requirement</u>
Advising on securities	\$3M (\$100,000 if subject to specified licensing condition)
Advising on futures contracts	ditto
Advising on corporate finance	ditto
Asset management	ditto

Specified licensing condition

- ◆ Defined in the FRR to mean the licensing condition that the licensed corporation shall not hold client assets.
- ◆ Many of such licensing conditions have been imposed in the past with slightly different wording.
- ◆ Existing licensing conditions not affected by SFO.

Paid Up Share Capital requirements

- Does not apply to approved introducing agent (except LFET), non-clearing futures dealers, traders or advisers/asset managers subject to specified licensing condition
- \$30M for forex traders (\$5M if approved introducing agent)
- \$10 million for securities margin providers or securities dealers providing securities margin financing
- \$5 million for other securities dealers, futures dealers, or advisers not subject to specified licensing condition



Paid Up Share Capital requirements - Transition for the Unincorporated

Sole proprietorships / Partnerships

- ◆ Deemed licensed corporation during the 2 years from effective date of SFO
- To maintain capital accounts of like amount instead of maintaining paid-up share capital.

New investments, Valuation & Haircut

Include in liquid assets:

- ◆ ELI listed on SEHK

(Haircut same as underlying)

- ◆ CDs issued by AFI/Approved Bank

(only maturity term haircut, accept issuer's quotes)*

* for other debt securities, accept quotes from 2 banks, licensed corporations or overseas securities dealers who customarily deal in such debt securities

New investments, Valuation & Haircut (cont'd)

- ◆ Related securities no longer considered together in CDF calculation
- ◆ HS Hong Kong Large Cap constituent stocks enjoy same haircut percentage as HSI stock, i.e. 15%
- ◆ HS Hong Kong MidCap constituent stocks enjoy same haircut percentage as previous HS100 stock, i.e. 20%

Rolling Balance Cash Clients

If client has authorized in writing disposal of his securities for settlement of outstanding debts & set-off trade receivables and trade payables

➤ Liquid assets

= Lower of

(Net receivable - specific provision) Or

(MV of securities held – Haircut)

Cash and Interest etc. accruals

Include in liquid assets:

- ◆ House money (e.g. commission) not yet withdrawn from segregated account
- ◆ Accrued interest on time deposits up to 6 months
- ◆ Other RA-related interests, fees etc billed/due and has been outstanding for not more than 1 month after billing/due date

Facilitate introducing business

New exception from capital charge

- ◆ introduction to group company
- ◆ direct contractual relationship between that company & the client i.r.o. execution / clearing
- ◆ Introducing firm has no legal liability to the client

Approved Introducing Agent

- ◆ can carry out Type 4, 5 and 6 RA subject to specified licensing condition

Client Money Segregated Overseas

- ◆ Adjusted liabilities to also exclude amount payable to clients in respect of client money held in overseas in separate account* with AFI or approved banks incorporated outside HK
- * the account must be separate from the house account of the firm

Excluded Liabilities for FX Adjustment

- ◆ FX net position to exclude FX liabilities for amount payable to clients in respect of client money held in
 - segregated /separate accounts with AFI
 - separate account with approved banks incorporated outside HK
 - segregated account with recognized clearing house

Relief for Cross Currency LFE Contracts

- ◆ currently treated as 2 positions for calculating Gross Principal Value[#] under existing LFET(FR)R
- ◆ 1996 Review suggested relief to count as one position
- Suggest only count the higher of the reporting currency equivalents of the 2 contracted currencies as the GPV

[#] 3% of GPV is taken as the minimum margin for LFE contracts for the purpose of determining margin shortfall for LFET (FR)R purpose

Relief for “locked” LFET positions

“locked” LFET positions = simultaneously holding a pair of offsetting contracts with a client

- ◆ FX risks have offset each other
- ◆ Unreasonable to count twice in FRR
- ◆ 1996 Review suggested relief and should count once

Relief for “locked” LFET positions (Cont’d)

Aggregated Gross foreign currency position

- ◆ Suggest only count the contract which gives the higher gross foreign currency position

Gross Principal Value

- ◆ Suggest only count the contract which gives the higher GPV



Admission of new exchanges and depository institutions

Additional specified exchanges

- ◆ Korea Futures Exchange
- ◆ Malaysian Derivatives Exchange Berhad

New depository institutions

- ◆ Korea Securities Finance Corporation

FRR Returns

- ◆ Monthly / Quarterly /Semi-annually returns
- ◆ May use own fiscal reporting cycles for monthly returns (28 to 35 days)
- ◆ May use own fiscal reporting period end date (must be + / - 7 days from calendar month end)
- ◆ Submission Channels:
 - FinNet (e-FRR) + digital signature
 - FinNet (e-FRR) + *signed hardcopy*
 - Diskette + *signed hardcopy*
 - Signed hardcopy