

SFC's New Requirements on a Licensed Person's Reorganization and Structure

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Circulars Issued by the SFC

On June 2, 2017, the Hong Kong Securities and Futures Committee (SFC) issued a circular to licensed corporations on responsible officers and substantial shareholders (the "Circular"). The SFC found that there is an increasing number of licenses granted for corporations by the SFC through the purchase of a licensed corporation that has little or no business. This has added to the phenomenon of the holding of licensed corporations in Hong Kong by people who have not had sufficient experience in the securities industry in the past. At the same time, companies have to meet the requirements of having two responsible officers in order to be a licensed corporation. However, such responsible officers sometimes do not actually participate in the operation of the company and are only there to meet the requirement of the number of responsible officers. They do not carry out the functions of supervision and management, thus increasing the risk of compliance for the licensed corporation.

Furthermore, by the SFC's circular of June 16, 2017, all licensed corporations have been reminded to submit their managers-in-charge of core functions (MIC) information and organizational charts to the SFC on or before July 17, 2017. Moreover, MICs of overall management oversight function and key business lines function, who are not yet responsible officers, should apply for approval to become responsible officers on or before October 16, 2017.

New licensing applications should note the new filing requirements. In particular, applicants should now use (a) the revised the existing form, Supplement 8 - Business Plan and Proposed Business Activities, and (b) complete a new form, Supplement 8A - Manager-In-Charge of Core Function(s), in addition to other forms.

Requirements in the Circular

The SFC circular is divided into two sections; one for "responsible officers" and one for "substantial shareholders".

1. Responsible officers - it is not acceptable to hire responsible officers in name only

In the SFC circular, the SFC stated several requirements that need to be fulfilled by the licensed corporation.

- a. The responsible officer needs to have sufficient authority to supervise the business of regulated activity

The responsible officer of a licensed corporation shall have sufficient powers to oversee the business of the licensed corporation's regulated activities. Therefore, the SFC has made it clear that it will not accept persons who are nominally employed but who are not in fact involved in supervising the business of the Licensed Corporation or who do not have sufficient authority to supervise. If the SFC doubts whether the senior management of a licensed corporation is sufficiently competent to do its job properly and manage the risks involved in its business, the licensee and the responsible persons may be publicly reprimanded by the SFC and their license may be revoked.

- b. The responsible officer needs to carry out its duties

The responsible officers of the SFC need to specify in detail their functions, particularly their specific duties as responsible officers in overseeing the business of the licensed corporation. If needed, the SFC will liaise directly with the responsible officers to understand the scope of their duties and the business of the licensed corporation under their supervision. If the responsible officers do not actually participate in the supervision of

the business of the licensing corporation, the licensed corporation and the responsible officers might have committed an offence of providing false or misleading information to the SFC in support of their license applications.

2. Substantial shareholders

- a. The Licensed Corporation should carry out business operations – review of “substance” of operations

In considering the application for approval to become a substantial shareholder in a licensed corporation, the SFC will strictly review the “substance” of the proposed arrangements in the application and ensure that the new substantial shareholder application is not seeking to circumvent the normal assessment and vetting process involved with a new licensed corporation application.

- b. The application of the new substantial shareholder must ensure compliance on the part of the licensed corporation – the fit and proper person criteria

In considering an application for a new corporate license or an application for change of a substantial shareholder of an existing licensed corporation, the SFC must be satisfied that the relevant licensed corporation is still a fit and proper person if the application is approved. If the SFC is unable to ensure that the incorporation of a new substantial shareholder can guarantee that the licensed corporation complies with the requirements of the SFC and continues lawful operation, the SFC will refuse to approve the applicant as a substantial shareholder of the licensed corporation.

- c. A new substantial shareholder application is as strict as the application for a new licensed corporation

Previously, the SFC standards of a new licensed corporation application is comparably more stringent than those of the application for a new substantial shareholder. Generally, the SFC had only required the applicant to fill in some of the documents and provide some basic supporting information in the application process. However, the SFC will now examine the funding and financial capacity of substantial

shareholder applicants in the process of vetting new substantial shareholder applications to assess the legitimacy of the funds concerned and confirm that the ultimate beneficial owners who are substantial shareholders have applied for approval.

At the same time, the SFC will scrutinize the group structure and structure of the group before the reorganization. The licensee will also be required to provide a complete list of directors, including detailed personal particulars of the directors and affiliated companies. In order to ensure the stability and compliance of the licensed corporation operation, the SFC will also assess whether there will be any change in the business plans and senior management of the licensed corporation after the new substantial shareholder has joined. At the same time, the SFC will ensure that the board of directors and senior management of a licensed corporation should have sufficient skills and experience, and that the business of the licensed corporation can be adequately understood and properly operated by its management.

Further, the SFC will examine whether the business of a licensed corporation will change after the new substantial shareholder joins the licensed corporation and completes the ownership change of the licensed corporation. In the process, a licensed corporation must provide truthful and accurate information, or it may be fined by the SFC and sentenced to imprisonment. At the same time, licensed corporations must notify the SFC within seven business days when significant changes to its business plan or senior management occurs.

Conclusion

To sum up, the SFC’s circular of June 2, 2017 has tightened up the application procedures and the responsibilities of the responsible officers and the substantial shareholders. It is particularly important that the SFC clarifies the application requirements for the approval of new substantial shareholders and responsible officers of licensed corporations. The SFC circular is designed to ensure that licensed corporations can, under all circumstances, ensure that persons with

relevant experience are held responsible and that they operate properly. Recently, the SFC has also made it clear that it does not approve of illegal “backdoor licensing”. The new MIC regime is also now in place and licensed corporations should comply with the new requirements. In particular, MICs of overall management oversight function and key business lines function, who are not yet responsible officers, should apply for approval to become responsible officers on or before October 16, 2017.

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