



Jeffrey Mak Law Firm  
麦振兴律师事务所  
www.jmaklegal.com

# Hong Kong Licensed Corporations Alert

## 香港持牌法团快讯

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### Hong Kong Securities and Futures Commission Announces the Launch of Investor Identification Regime in March 2023

On December 12, 2022, the Securities and Futures Commission (SFC) of Hong Kong announced that the investor identification regime for the securities market in Hong Kong (HKIDR) will be launched on March 20, 2023.

Upon the launch of the HKIDR which will be included in the new paragraph 5.6 of the Code of conduct for Persons Licensed by or Registered with the SFC (Code of Conduct), relevant licensed corporations (LCs) and registered institutions (RIs) are required to tag Broker-to-Client Assigned Numbers (BCANs) to securities orders to be executed on The Stock Exchange of Hong Kong Limited (SEHK) (or off-exchange trades reportable to it), and submit to SEHK's data repository the names and identity document information of their clients.

Main obligations of LCs and RIs subject to the HKIDR (Relevant Regulated Intermediaries (RRI)) are as follows:

- (a) ensure that a unique identification code, namely the BCAN, be assigned to Relevant Clients (scope of which as explained below) who have placed or propose to place (i) an on-exchange order or (ii) an off-exchange trade reportable to the SEHK under its rules, in securities listed or traded on SEHK's trading system (except for odd lots traded on SEHK's odd lot/special lot market);
- (b) ensure that up-to-date client identification data (CID) has been collected from each Relevant Client and is submitted along with the client's BCAN (by way of putting the BCAN and CID into a "BCAN-CID Mapping File") to a data repository to be maintained by SEHK by a prescribed time;
- (c) ensure that the Relevant Client's BCAN has been included in the order information for each on-exchange order as well as each off-exchange order and included in all reporting of off-exchange trades to

SEHK, and report any BCAN error of a matched and executed trade as soon as possible to SEHK by submitting a prescribed error notification form; and

- (d) adopt relevant data privacy and security measures to safeguard the data collected, transmitted and stored, including obtaining express consent from clients for the collection and handling of their personal data in compliance with data privacy laws.

The scope of "Relevant Client" is a direct client of an RRI, save that in the case of (i) a proprietary trade, the RRI should assign a BCAN to itself; and (ii) where an order is routed through a chain of RRI, the BCAN should be assigned to the first person which is not a RRI in the chain. As for investment funds (collective investment schemes) or discretionary account, a Relevant Client refers to a collective investment scheme, discretionary account holder or the asset management company, as appropriate, as the case may be, which has opened a trading account with the relevant licensed or registered person, through whose account an on-exchange order or off-exchange order is placed or proposed to be placed.

#### Implementation of the HKIDR

Before the HKIDR commences, there are a number of tasks that RRIs are expected to complete as part of their preparation for the implementation:

#### *Seek appropriate client consent*

RRIs should obtain written or other express consent from Relevant Clients who are individuals (i.e. natural persons) for the transfer of their personal data to SEHK and the SFC and the consent should include the purposes of use specified in the circular published by the SFC on September 13, 2021 (see <https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=21EC35>) (Consent Circular).

Alternatively, RRIs would not have to obtain new consent from individual clients if both the following criteria are met:

- (a) client consent on the use of personal data has already been obtained from these clients; and
- (b) the consent expressly includes the purposes of use specified by the SFC in the Consent Circular.

In general, consent may be obtained by written and signed acknowledgment on paper, or by electronic means including by email or instant messaging applications provided that the measures set out in the Consent Circular are observed.

#### *Updating individual and corporate clients' CID*

RRIs should ensure that the following information has been collected as CID from the Relevant Clients:

- (a) For an individual client, his or her: (i) full name as shown on his or her identity document; (ii) identity document's issuing country or jurisdiction; (iii) identity document type (order of priority: (1) HKID card; (2) national identification document; (3) passport); and (iv) identity document number on the identity document.
- (b) For a corporate client, its: (i) full name as shown on its identity document; (ii) identity document's issuing country or jurisdiction; (iii) identity document type (order of priority: (1) LEI registration document; (2) certificate of incorporation; (3) business registration certificate; (4) other equivalent documents); and (iv) identity document number on its identity document.
- (c) For a client that is a trust: (i) the CID of the trustee, which should be the same as that of a corporate or individual client as set out above; (ii) however, in the case of a trust which is an investment fund (i.e. collective investment schemes), the CID of the asset management company or the individual fund, as appropriate, which has opened a trading account with the RRI.
- (d) For clients of a joint account: the CID for all clients (in line with the above proposed requirements, depending on the nature of the client) named for a joint account should be provided under the same BCAN assigned to that account.

RRIs should issue a notification to their existing securities trading account holders (regardless of nationality) to inform them of the waterfall of the identity documents and request an identity document required under the waterfall (if not already obtained) or updated identity document

information, as appropriate, before the launch of the HKIDR.

#### *Enhancing order management systems*

Upon the implementation of the HKIDR, SEHK's Exchange Participants (EPs) will need to submit a BCAN along with an order via the Cash Market Gateway (CMG). The Hong Kong Exchanges and Clearing Limited (HKEX) has published an information paper (HKEX Information Paper) on the operational logistics of the HKIDR. Please refer to the HKEX Information Paper for the technical setup (see [https://www.hkex.com.hk/Services/Trading/Securities/Overview/Trading-Mechanism/HKIDR?sc\\_lang=en](https://www.hkex.com.hk/Services/Trading/Securities/Overview/Trading-Mechanism/HKIDR?sc_lang=en)) (HKEX Information Paper). The related interface specifications of the proposed model was also published by SEHK in August 2021 (see [https://www.hkex.com.hk/Services/Trading/Securities/Overview/Trading-Mechanism/HKIDR?sc\\_lang=en](https://www.hkex.com.hk/Services/Trading/Securities/Overview/Trading-Mechanism/HKIDR?sc_lang=en)).

RRIs are also required to enhance their internal systems for submission of BCANs along with orders via CMG and BCAN-CID Mapping Files via SEHK's Electronic Communication Platform (ECP).

#### *Assigning BCANs to clients*

Each RRI is responsible for assigning a unique set of BCANs to its Relevant Clients (including to RRIs themselves in the case of proprietary trades). RRIs do not have to check with one another to determine if a single BCAN has been applied to a client.

The BCAN consists of a number not exceeding 10 digits in a standard format as set out in Appendix 2 to the HKEX Information Paper. To distinguish between BCANs assigned by different RRIs, the six alphanumeric CE Number (i.e. Central Entity Number) assigned by the SFC and a separator dot "." have to be inserted as a prefix before the BCAN when the BCAN field is populated in the trading system. A BCAN in the HKIDR may adopt the same BCAN used in the investor identification regime for northbound trading under Mainland-Hong Kong Stock Connect, or include reference to a Relevant Regulated Intermediary's internal client number or account number, provided that the BCAN remains compliant with the requirements as set out in the HKEX Information Paper. For further details about the generation, assignment and format of BCAN, please refer to the HKEX Information Paper.

For detailed requirements of BCAN assignment, BCAN tagging and order transmission where a RRI passes an order to other RRIs (i.e. in a chain of RRIs), please refer

to the new paragraphs 5.6(d) and (g) of the Code of Conduct (see <https://apps.sfc.hk/edistributionWeb/api/circular/openAppendix?lang=EN&refNo=21EC37&appendix=0>) and paragraphs 107-111 of the Consultation Conclusions on Proposals to, among others, implement the HKIDR issued by the SFC on August 10, 2021 (Conclusions) (see <https://www1.hkexnews.hk/listedco/listconews/sehk/2022/0908/2022090801232.pdf>).

The Conclusions also provided detailed requirements of BCAN assignment and/or BCAN tagging and order transmission in following situations: (a) where RRI books an order with an overseas broker (see paragraphs 59-65 and paragraphs 142-143); (b) investment funds managed by a fund manager (see paragraphs 66-68); (c) discretionary account management (see paragraphs 69-73); and (d) where an investor hold different types of accounts in a RRI (see paragraphs 74-79).

#### *Preparation and submission of BCAN-CID Mapping File*

The BCAN-CID Mapping File is a file containing the BCAN and CID of all the Relevant Clients of a RRI, in a designated format as set out in the HKEX Information Paper. Before the implementation of the HKIDR, each RRI is required to prepare a BCAN-CID Mapping File and submit it to SEHK's data repository.

RRIs will be allowed to submit the BCAN and CID of their clients in the BCAN-CID Mapping File to SEHK via ECP web interface and/or ECP (SFTP) interface commencing on December 19, 2022. RRIs should submit the latest BCAN-CID mapping data to SEHK, whenever available, from December 19, 2022 onwards prior to the launch of the HKIDR on March 20, 2023. Prior to the launch of HKIDR on March 20, 2023, RRIs are only required to submit the BCAN-CID Mapping File, and submission of the five reporting forms is not required. RRIs are strongly encouraged to submit the BCAN-CID Mapping File as early as possible to ensure that their clients' BCANs are registered in preparation for any trading by such clients upon the launch of the HKIDR.

The RRI which assigns the BCAN to the Relevant Client should also be the one which collects the CID from the Relevant Clients and prepares the BCAN-CID Mapping File. Where there is an update to the BCAN-CID Mapping File, be it due to on-boarding of new clients, the closure of a client account or a change in CID information for existing clients, a complete file with the CID of all Relevant Clients should be uploaded to SEHK's data repository on the day an update has been made (even where the update is in relation to only one or some of the Relevant Clients). If there has been no update to the CID, the RRI does not

have to submit the BCAN-CID Mapping File again after the initial submission.

After completion of the BCAN-CID Mapping File, the RRI should submit it to SEHK's data repository in the following manner:

- (a) an EP can submit the BCAN-CID Mapping File to SEHK via a designated web portal, the ECP;
- (b) a non-EP Relevant Regulated Intermediary can submit the BCAN-CID Mapping File to SEHK via ECP (subject to the relevant requirements); or
- (c) a RRI (whether an EP or a non-EP RRI) can choose to submit its clients' BCAN-CID Mapping File to SEHK via another LC or RI through SFC WINGS platform, in which case it should encrypt such data in accordance with SEHK's requirements as set out in the HKEX Information Paper.

RRIs should take all reasonable steps to ensure that the individual client information (including the data constituting the CID) they collect and submit to SEHK's data repository is accurate and kept up-to-date, and to also promptly update SEHK of any changes via the BCAN-CID Mapping File submission. RRIs should also put in place measures to require clients to notify them of any updates to the CIDs. These may include obtaining representations and warranties from their clients as they consider appropriate to assist their verification and maintenance of CID. RRIs are also free to conduct a refresher of the CID exercise in the timeframe prescribed by the Guidelines on Anti-Money Laundering and Counter-Financing of Terrorism.

#### *Compliance with applicable data privacy laws including Personal Data (Privacy) Ordinance (PDPO)*

RRIs are reminded to ensure that all necessary authorizations and written or other express consents are obtained from each existing and new individual client regarding the collection, storage, processing, use, disclosure and transfer of personal data in relation to such client's BCANs and Client Identification Data (CID) in full compliance with all applicable laws including the Personal Data (Privacy) Ordinance (PDPO) before submitting any BCAN, CID and/or BCAN-CID Mapping File to the SEHK.

RRIs are also reminded that they should submit the BCAN-CID Mapping File containing BCAN and CID of their clients to SEHK's data repository before a cut-off time on or before the previous trading day prescribed by SEHK, otherwise their clients will not be allowed to place buy orders on the trading day, except for new clients who wish to trade on the day of account opening or dormant clients

whose accounts become re-activated on the day of entering into a trade, in which case RRI may submit the BCAN-CID Mapping File containing such client's BCAN and CID to SEHK's data repository by a deadline on the trading day prescribed by SEHK.

Source:

<https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=22PR102>

<https://apps.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=21EC37>

<https://www.hkex.com.hk/-/media/HKEX-Market/Services/Circulars-and-Notices/Participant-and-Members-Circulars/SEHK/2022/CT15722E.pdf>

[https://www.hkex.com.hk/-/media/HKEX-Market/Services/Trading/Securities/Overview/Trading-Mechanism/HKIDR/HKIDR-Information-Paper\\_e.pdf](https://www.hkex.com.hk/-/media/HKEX-Market/Services/Trading/Securities/Overview/Trading-Mechanism/HKIDR/HKIDR-Information-Paper_e.pdf)

### **Hong Kong Securities and Futures Commission Issues Phasal Consultation Conclusion on Licensing Depositories of SFC-Authorized Collective Investment Schemes (under New Regulated Activity 13)**

On February 22, 2022, the Securities and Futures Commission (SFC) of Hong Kong released consultation conclusions and began a further consultation on a proposal to regulate depositories (i.e., top-level trustees and custodians) of SFC-authorized collective investment schemes (CIS) under section 104 of the Securities and Futures Ordinance (SFO) (relevant CIS).

In 2019, the SFC launched a consultation proposing to introduce a new regulated activity, Type 13 regulated activity or RA 13 (providing depository services for a relevant CIS), to put depositories of SFC-authorized CIS under the SFC's direct supervision. Respondents were generally supportive of the proposal, with some seeking clarification of the proposed licensing scope and conduct requirements. The SFC is now consulting the public on proposed amendments to subsidiary legislation and SFC codes and guidelines to implement the regime.

#### Proposed scope

The SFC proposed to introduce a new type of regulated activity (Type 13) under Schedule 5 to the SFO, providing depository services for a relevant CIS. This will be RA 13. The SFC's policy intent is to capture only top-level trustees or custodians (i.e. depositories) which carry on a business in RA 13 in Hong Kong. A depository's delegates (such as its sub-custodians) will not fall within the proposed scope of RA 13, regardless of whether such delegates operate within or outside Hong Kong.

#### Exemptions

A relevant CIS would be one which is authorized by the SFC under section 104 of the SFO, i.e., unit trusts, mutual fund companies, real estate investment trusts, pooled retirement funds authorized under the SFO and open-ended fund companies registered and authorized under the SFO, but excluding MPF products.

Given that MPF-approved trustees are already subject to the MPFA's regulation and supervision, to minimize regulatory duplication, the SFC proposed to exclude them from the scope of RA 13 insofar as the trustee services relate only to MPF products. However, the carve-out will not include approved pooled investment funds (APIFs) which may be offered to both MPF schemes and directly to retail investors (Retail APIFs) as these funds should be distinguished from pure MPF products.

#### Licensing and conduct requirements

RA 13 will be defined as an activity of "providing depository services for a relevant CIS" with reference to two core functions of a depository, being (a) custody and safekeeping of scheme property and (b) oversight of the operation of the relevant CIS to ensure that it is operated in accordance with its constitutive documents. The licensing scope applicable to individuals will be aligned with the two core functions as follows:

With respect to the custody and safekeeping of scheme property:

- (a) where a depository delegates this function to another entity (e.g. a sub-custodian), staff of the depository responsible for monitoring the performance of the delegate will need to be licensed or registered for RA 13; and
- (b) where a depository performs part or all of this function within the firm, staff of the depository who are empowered to approve instructions or transactions for custody-related purposes (e.g. approving payments or asset transfers, signing-off cash reconciliation) in respect of a relevant CIS and those who assume oversight duties over the performance of this function will need to be licensed or registered for RA 13; whereas staff who are engaged in custody operations without such approving powers or oversight duties will generally not be subject to the licensing obligations under the RA 13 regime.

With respect to the oversight of scheme operations, staff of a depository responsible for performing the duties of this function in respect of a relevant CIS should be licensed or registered for RA 13. Broadly speaking, oversight duties



encompass the monitoring of various operations of the CIS including, amongst others, compliance with investment and borrowing restrictions, cash flow, fund accounting and valuation, as well as the issue, repurchase, redemption and cancellation of the units or shares of the CIS. Nevertheless, where a depositary also acts as the fund administrator, transfer agent or registrar for a relevant CIS, staff of the depositary who are engaged to provide such services are generally not required to be licensed or registered for RA 13, unless they also have an oversight responsibility in respect of these operations based on the particular business model and governance structure adopted by the depositary.

Managers-in-charge (MICs) of the overall management oversight function and MICs of key business lines of a licensed corporation (LC) should be ROs. The MICs of other core functions are generally not required to be licensed. In view of the revised approach for defining RA 13, the marketing of a depositary's services by itself does not fall within the scope of "providing depositary services for a relevant CIS". Therefore, individuals who solely perform marketing activities for a depositary will not be subject to the licensing obligation under the RA 13 regime. The SFC will provide a grandfathering arrangement (i.e., attending training courses in lieu of passing local regulatory examinations) for practitioners when implementing the RA 13 regime. In addition, an individual may apply for an exemption from the recognized industry qualification and the local regulatory framework paper requirements if he or she satisfies the exemption criteria set out in the Guidelines on Competence.

#### Financial Resources Requirements

In line with other types of regulated activity, RA 13 licensed corporations must maintain adequate financial resources under the Securities and Futures (Financial Resources) Rules (Financial Resources Rules). The SFC proposed:

- (a) a minimum paid-up share capital of HK\$10,000,000 which is similar to the current requirement under the Product Codes; and
- (b) a minimum liquid capital of HK\$3,000,000.

The minimum liquid capital required may increase as a consequence of an increase in the size of the corporation's operations and liabilities.

#### Professional indemnity insurance requirement

The SFC proposed to impose a non-statutory requirement for RA 13 depositaries to maintain a professional indemnity insurance policy which provides adequate coverage for claims for liability arising from breaches of duty in the course of carrying on its RA 13 business. This proposal is in line with a similar requirement for licensed or registered fund managers under the Fund Manager Code of Conduct (FMCC).

#### Conduct and internal controls requirements

Once licensed or registered, RA 13 depositaries and individuals must comply with the applicable legal and regulatory requirements, such as the SFO, and the SFC's codes and guidelines, including the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of Conduct) and the Management, Supervision, and Internal Control Guidelines for Persons Licensed by or Registered with the Securities and Futures Commission (Internal Control Guidelines). In addition to these requirements, RA 13 depositaries will be expected to continue to meet the existing provisions in the product codes, i.e., the Code on Unit Trusts and Mutual Funds (UT Code), the Code on Real Estate Investment Trusts (REIT Code), the Code on Pooled Retirement Funds (PRF Code) and the Code on Open-Ended Fund Companies (OFC Code) (collectively, Product Codes) which apply to trustees and custodians.

Under the existing UT Code, trustees or custodians of SFC-authorized CIS are required to engage independent auditors to review their internal controls and systems and submit internal control reports reviewed by auditors to the SFC annually, unless a trustee or custodian is prudentially regulated and supervised by an overseas supervisory authority which is acceptable to the SFC.

With the introduction of RA 13, depositaries of relevant CIS will be subject to the SFC's supervision, or in the case of registered institutions, the HKMA's supervision as the frontline regulator. The requirement to submit the annual internal control reports to the SFC will be removed.

The SFC also proposed to introduce a new schedule 11 to the Code of Conduct (Schedule 11) to set out the updated and detailed guidance on the internal controls depositaries should have in place in Appendix G to the UT Code. It will be the responsibility of the senior management of an RA 13 depositary to exercise professional judgment in designing suitable internal controls and systems and ensure that these are adequately, effectively and properly implemented.

### Scope of schedule 11

Under the proposed scope of RA 13, depositaries have oversight obligations over the operation of a CIS. Where a depositary carries out these operational functions itself (e.g. by acting as the transfer agent or fund administrator), it would be held primarily responsible for them.

### Relevant operators

A core function of a depositary is to have oversight of a relevant CIS to ensure that it is operated in accordance with the constitutive documents. Under the UT Code, the oversight obligations of a depositary include, for example, oversight of the issue of units or shares of the relevant CIS. These activities may be carried out by the board of directors of an OFC, the management company or other operators. Hence, the board of directors is a “relevant operator” while sub-custodians are delegates of the depositaries and are not “relevant operators”.

### Communication with management company

A Depositary should communicate with the management company in an effective and timely manner in the course of discharging its function(s) and obligation(s) with respect to a relevant CIS. Specifically, the depositary will need to notify the management company of material exceptions to its business continuity plan which may have a material adverse impact on the operation of the CIS or the discharge of the depositary’s obligations.

### Delegation

Depositaries are required to have oversight of the relevant CIS to ensure that it is operated in accordance with the constitutive documents of the CIS. In order to discharge this oversight function, depositaries are responsible for monitoring the relevant operational activities, whether they are carried out by delegates appointed by the depositary itself, or third parties appointed by other operators (including but not limited to the management company).

### Pricing error or exception reporting

Depositary should maintain effective communication with the management company, particularly in relation to pricing errors or exceptions which would need to be reported under the regulatory requirements or may adversely impact the operations of the CIS, the orderliness of the market or investors’ interests.

### Cash flow monitoring

A depositary must ensure relevant operators have effective controls in place for obtaining all necessary prior written consent from the depositary for connected party transactions. All cash flows which are inconsistent with the operations of the relevant CIS should be identified, even if they are insignificant.

### Investment monitoring

A depositary should provide the management company with its reconciled records of relevant CIS property and transactions executed on behalf of the relevant CIS to facilitate the management company’s verification of the accuracy of its investment records.

### Custody and safekeeping of relevant CIS property

A depositary should ensure payments and asset transfers or other dealings of any relevant CIS property on behalf of the relevant CIS are properly authorized in accordance with the constitutive documents of the relevant CIS. Where the relevant payments or asset transfers or other dealings of relevant CIS property need not be authorized by the Depositary under the constitutive documents of the relevant CIS, the Depositary should have proper oversight of the management company to ensure that it the management company has properly authorized or has obtained the relevant authorization.

Custody risks need to be managed and not just monitored in order for the depositary to discharge its obligations. In addition, a depositary should safeguard all assets and not only physical assets.

### Key operators

Even though the management company is also regulated by the SFC, a depositary should also have oversight of the relevant CIS to ensure that it is operated (or in the case of a relevant CIS that is a Pooled Retirement Fund, administered) in accordance with the provisions of the constitutive documents of the relevant CIS.

Source 来源:

<https://apps.sfc.hk/edistributionWeb/api/consultation/openFile?lang=EN&refNo=19CP3>

<https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=22PR9>

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