

## Updating Your Study Manual

### Instructions for Inserting Version 1.5

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The followings serve as the instructions for updating **Topic 3: Regulation of Intermediaries: Licensing and Subsidiary Legislation** of Study Manual 6 for the Licensing Examination for Securities and Futures Intermediaries. Please be reminded that only the updated sections are provided for downloading. You may replace the relevant sections with this updated version for the study manual you possess.

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#### **Instructions:**

1. Download and print out the following pages.
  2. **Remove** pages 3-3 to 3-4            and            **Insert** new pages 3-3 to 3-4.
  3. **Remove** pages 3-7 to 3-8            and            **Insert** new pages 3-7 to 3-8.
  4. **Remove** pages 3-11 to 3-16        and            **Insert** new pages 3-11 to 3-16.
  5. **Remove** pages 3-19 to 3-20        and            **Insert** new pages 3-19 to 3-20.
  6. **Remove** pages 3-31 to 3-32        and            **Insert** new pages 3-31 to 3-32.
  7. **Remove** pages 3-35 to 3-36        and            **Insert** new pages 3-35 to 3-36.
  8. **Remove** pages 3-55 to 3-56        and            **Insert** new pages 3-55 to 3-56.
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## 1 Introduction and approach

- 1.1 Asset management is defined in the Securities and Futures Ordinance ('SFO') as (a) [real estate investment scheme management](#); or (b) [securities or futures contracts management](#) (Schedule 5, SFO).
- 1.2 In this topic the subsidiary rules relating to the regulation of intermediaries in asset management will be considered. The intermediaries may be broadly classified into three groups, persons conducting asset management (called 'asset managers' for convenience in this study manual), distributors and others.

### ***Asset managers***

- 1.3 Asset managers include fund houses, fund managers and portfolio managers. They should generally be licensed by or registered with the Securities and Futures Commission ('SFC') as conducting the regulated activity of asset management. As intermediaries engaged in activities related to asset management may be captured by the definitions of various regulated activities under the SFO regime, they will have to exercise care in checking the nature of their activities against the licensing requirements and may need to consult the SFC if clarification of their licensing status is required. They should also keep an eye on the Frequently Asked Questions ('FAQs') on the SFC's website and look out for any circulars and guidelines that the SFC may issue from time to time, as circumstances in the current dynamic environment may change. For the moment this manual is written using currently available public information and will be revised when any further changes and clarifications are announced by the regulators.

### ***Excluded categories (Schedule 5, SFO)***

- 1.4 The following groups are not deemed to be conducting the SFC-regulated activity of asset management:
- a corporation which manages a portfolio of securities or portfolio contracts solely for any of its wholly owned subsidiaries, its holding company which holds all its issued shares, or other wholly owned subsidiaries of that holding company;
  - persons licensed for Type 1 or 2 regulated activity who provide asset management services wholly incidental to the carrying on of that regulated activity;
  - an authorized financial institution ('AFI') registered for Type 1 or 2 regulated activity, which provides asset management services wholly incidental to the carrying on of that regulated activity;

- an individual entered on the register of the Hong Kong Monetary Authority ('HKMA') as conducting Type 1 or 2 regulated activity for an AFI and who provides asset management services wholly incidental to that regulated activity; and
- a solicitor, counsel, professional accountant or trust company which provides asset management services wholly incidental to their respective professional practices.

### ***Distributors***

- 1.5 These will include AFIs, insurers, independent financial advisers, securities dealers and financial planners. Fund houses can, of course, distribute direct to the investor through investment centres or otherwise.
- 1.6 Fund houses doing direct distribution may need to be licensed for dealing in securities and/or futures contracts, depending on the instruments they distribute. Distributors may generally have to obtain licensing endorsement to deal in securities.
- 1.7 AFIs are regulated by the HKMA. Where their activities fall within the description of activities regulated by the SFC, they will have to register with the SFC as registered institutions ('RIs') and be regulated by the HKMA as the front-line regulator. The HKMA will apply the principles developed by the SFC in regulating such activities.
- 1.8 Insurers are regulated by the Insurance Authority ('IA') and the self-regulatory organizations ('SROs') through which the IA regulates insurance intermediaries. If they conduct a regulated activity, they will need to be licensed by the SFC. Thus, insurers distributing collective investment schemes ('CIS') or insurance policies linked to CIS may need to get licences from the SFC.
- 1.9 Independent financial advisers ('IFAs') and securities dealers involved with asset management may have to be licensed by the SFC as dealers in securities and/or futures contracts, depending on their activities.

### ***Others***

- 1.10 This residual class includes trustees, custodians, and other professionals such as accountants and investment advisers.
- 1.11 Trustees are regulated under the Trustees Ordinance. Trustees of unit trusts and custodians of authorized mutual funds, by their definition in the SFC's Fund Manager Code of Conduct ('FMCC'), fall within specific classes which are subject to supervision (e.g. trust companies and AFIs). AFIs who are trustees or custodians will be regulated by the HKMA.

person (these are the equivalents in banking of licensed representatives);

- for the issuing of two types of licence by the SFC, one to licensed corporations ('licensed corporations') and the other to individuals ('licensed representatives') (ss.116 and 120, SFO);
- for the accreditation of a representative to a licensed corporation, and where necessary, for the transfer of accreditation to another licensed corporation and the specification on the licence of the licensed representative that the licensed corporation is his principal (s.122, SFO);
- for the approval of persons who, in addition to being licensed representatives, also carry out supervisory functions, and are nominated as responsible officers by a licensed corporation (s.126, SFO) ([note: a licensed corporation should appoint not less than 2 responsible officers to directly supervise the conduct of each regulated activity, see paragraph 2.20 below](#));
- for the setting of fit and proper requirements for issuing licences (ss.116, 120 and 129, SFO); and
- that temporary licences are not available for the regulated activity of asset management (ss.117 and 121, SFO).

### **Restrictions on conducting regulated activities**

- 2.3 S.114, SFO forbids any person from carrying on, or holding himself as carrying on, a business in a regulated activity such as asset management, unless he is licensed by or registered with the SFC to do so.
- 2.4 A person who, without reasonable excuse, contravenes this provision commits an offence and is liable:
- on conviction on indictment to a fine of \$5 million and to imprisonment for 7 years, and in the case of a continuing offence to a further fine of \$100,000 for every day during which the offence continues; or
  - on summary conviction to a fine of \$500,000 and to imprisonment for 2 years, and in the case of a continuing offence, to a further fine of \$10,000 for every day during which the offence continues.
- 2.5 S.114 also forbids any person from performing, or holding himself out as performing, any regulated function in relation to a regulated activity such as asset management, unless he is a representative who is licensed for the regulated activity or is listed in the register maintained by the HKMA, and conducts it for his principal.

- 2.6 A 'regulated function' is defined in s.113, SFO as any function performed for or on behalf of or by arrangement with a person who is carrying on a regulated activity as a business, in relation to that activity, other than work ordinarily performed by an accountant, clerk or cashier.
- 2.7 A person who, without reasonable excuse, contravenes this provision commits an offence and is liable:
- on conviction on indictment to a fine of \$1 million and to imprisonment for 2 years, and in the case of a continuing offence, to a further fine of \$20,000 for every day during which the offence continues; or
  - on summary conviction to a fine at level 6 (see note below) and to imprisonment for 6 months and, in the case of a continuing offence, to a further fine of \$2,000 for every day during which the offence continues.

*Note:* Refer to the appendix to topic 6 for details of the current monetary amounts corresponding to the various levels of fines.

### **Transitional provisions for persons conducting regulated activities**

- 2.8 This section applies to asset managers and distributors who held securities dealer and/or investment adviser licences under the pre-SFO regime.

#### ***Licensed corporations, partnerships and sole proprietors under the pre-SFO regime***

- 2.9 During the transitional period of 2 years from the date of implementation of the SFO, an arrangement has been made whereby the old categories of licensed corporations, partnerships and sole proprietors will be deemed to be licensed to carry on certain regulated activities under the new regime. Details are as follows:

above table (paragraph 2.9) and be subject to the restrictions indicated. Their deemed licences will be for a period of 2 years from the implementation of the SFO.

### **New regime**

- 2.17 The remaining sections apply to the SFO regime. As the various activities of asset management and distribution are covered from a regulatory angle, references are made to asset managers and distributors collectively as intermediaries where the provisions may apply to both classes (as regulated by the SFC and the HKMA) and separately where they may apply only to one or other of them.

### **Cessation of accreditation**

- 2.18 S.123, SFO provides that if a licensed representative ceases to act for his principal, he then ceases to be accredited to that principal and
- within 7 business days of the cessation:
    - the principal should notify the SFC; and
    - the representative should return the certificate to the SFC; and
  - if, within 180 days, the representative has not applied to the SFC for transfer of his accreditation to another licensed corporation, his licence is deemed to have been revoked.
- 2.19 Failure to make the 7 business day notification is an offence and the principal and the licensed representative are respectively liable on conviction to a fine at level 6 (see Appendix to topic 6).

### ***Responsible officers (ss.125 and 126, SFO)***

- 2.20 A responsible officer is an officer who actively participates in or supervises a regulated activity and is nominated by the licensed corporation and approved by the SFC as a responsible officer. He must be a licensed representative. A licensed corporation shall not conduct a regulated activity unless:
- every individual executive director is approved as a responsible officer by the SFC;
  - it has at least two individuals approved as responsible officers for every regulated activity for which it is licensed, at least one being an executive director (s.125, SFO); and

- it has one responsible officer available at all times to supervise the regulated activities for which it is licensed (s.118(1)(a)(ii), SFO) (see paragraph 2.2 above).

2.21 A licensed corporation which contravenes this provision, without reasonable excuse, commits an offence and is liable on conviction to a fine at level 6 and, in the case of a continuing offence, to a further fine of \$2,000 for every day during which the offence continues.

***Executive officer (Schedule 1, SFO)***

2.22 An executive officer is defined in Schedule 1, SFO, in relation to the respective entities named as being:

- a responsible officer of a licensed corporation;
- an executive officer of a registered institution under the Banking Ordinance; or
- a director of an associated entity, who is directly responsible for supervising the receiving or holding by the associated entity of client assets of the intermediary.

***Substantial shareholder (Schedule 1(6), SFO)***

2.23 The status of substantial shareholder has special relevance to the application of the licensing regime. A person may not become or continue to be a substantial shareholder of a licensed corporation without first being approved by the SFC as such.

2.24 A substantial shareholder is formally defined in s.5, Schedule 1, SFO. In simple terms for the purposes of this manual, it may be taken to refer to a person who alone or together with his associates:

- has an interest in **more than 10%** of the nominal value of the issued share capital; or
- directly or indirectly has more than 10% of the voting power at a general meeting; or
- is able to exercise 35% or more of the voting power of another corporation which in turn has more than 10% of the voting power of the licensed corporation.

2.25 A person who contravenes the provision commits an offence and is liable:

- on conviction on indictment to a fine of \$1 million and to imprisonment for 2 years, and to a further fine of \$5,000 for every day during which the person continues to commit the offence; or

- on summary conviction to a fine at level 6 and to imprisonment for 6 months, and to a further fine of \$500 for every day during which the person continues to commit the offence (s.131, SFO).

2.26 A defence available to a person charged is that he was not aware, and could not have found out using reasonable diligence, that he had become a substantial shareholder, and that when he found out he applied for approval. (The time limit allowed is ‘as soon as reasonably practicable or in any event within three days’.) Until the shareholder receives SFC approval, he may not exercise any voting powers (s.131, SFO).

2.27 The SFC has powers under s.133 to direct the licensed corporation which has a ‘non-approved substantial shareholder’ to not permit his participation in the management or in voting at meetings. Where an application to be a substantial shareholder is rejected by the SFC, it may direct the person to reduce his interest in the shares.

*Note:* It should be noted that the above definitions in the SFO, of responsible officers, executive directors, executive officers and substantial shareholders, are given specific and limited meanings applicable to intermediaries and their associated entities. The respective terms may have other meanings in other situations.

***Registered institution (‘RI’) (s.119, SFO)***

2.28 Authorized financial institutions (including banks) that are regulated by the HKMA and conduct SFC-regulated activities [have to register with the SFC](#), the status of registered institution (‘RI’) having been set up as a special category because of the special features of AFIs. They [are](#) jointly regulated by the HKMA and the SFC, with the HKMA being the front-line regulator that will apply all the SFC regulatory criteria, including fitness and properness and business conduct, the handling of client securities and the audit requirements in supervising them. They will have their own capital adequacy requirements as laid down by the HKMA. All references to registration will generally apply to this category, as the term ‘licensing’ will be used for all businesses and persons directly supervised by the SFC.

**Permissions and restrictions on licences**

<b>Type of Activity Covered by Licence</b>	<b>Any Other Activity Automatically Covered</b>
1	4, 6 or 9 (if incidental to 1)  May provide financial accommodation (Type 8) to facilitate acquisitions or holdings of securities by the licensed person for his client
2	5 or 9 (if incidental to 2)
Others	None, but may apply to be licensed or registered for additional regulated activities

**Exclusions from regulated activities**

2.29 There are certain persons some of whose activities might otherwise fit into the descriptions of regulated activities listed in Part 1, Schedule 5, but for the fact that these are specifically excluded from the definitions of regulated activities given in Part 2 of the Schedule. These will not need licensing in respect of those activities. They include:

- professional accountants, solicitors and counsel conducting Types 4, 5, 6 and 9 activities that are wholly incidental to their professions (see paragraph 2.30 below);
- trust companies conducting Types 4, 5, 6 and 9 activities wholly incidental to the discharge of their trustee duties;
- persons licensed to conduct Type 9 activities who carry out Types 1 and 2 activities solely for the purposes of their Type 9 activities; and
- corporations carrying out Types 4, 5, 6 and 9 activities solely for their wholly owned subsidiaries, holding companies holding all their issued shares or other wholly owned subsidiaries of the holding company.

The above list of activities and persons conducting them comprise only some of the exclusions from the licensing requirements, and readers wishing to identify the full list should refer to Schedule 5, SFO.

**Solicitors and accountants**

2.30 The position regarding solicitors and accountants referred to in paragraph 2.29 above is further clarified in the Frequently Asked Questions ('FAQs') available on the SFC's website.

### **Information to be provided by applicants for licensing, etc.**

- 2.31 The SFC has made the Securities and Futures (Licensing and Registration) (Information) Rules ('the Information Rules') under ss.128 and 397, SFO, specifying the information which should be provided by applicants for licensing. Applications will have to be made for:
- licensing of corporations or individuals;
  - approval of accreditation and transfer of accreditation of individuals;
  - approval to be a responsible officer;
  - variation of the type of regulated activity for which a person is licensed;
  - approval of premises for storing records;
  - approval to become or continue to be a substantial shareholder;
  - modifications or waivers (requests may be made by an applicant for a licence, a licensed person, substantial shareholder or associated entity); and
  - any other matter requiring the SFC's approval under Part V, SFO.

### ***Corporations***

- 2.32 The information required from corporations includes:
- certain basic information from the applicant corporation in respect of the applicant, its controllers (defined to include directors and substantial shareholders), responsible officers, subsidiaries and related corporations conducting regulated activities, and associated entities and their directors, including any registrations and authorizations by other regulators and memberships of exchanges;
  - contact persons and complaints officers appointed by the applicant;
  - any matters relevant to the fitness and properness of the applicant, including, regarding the other persons referred to above:
    - convictions, relevant disciplinary actions and investigations by regulators or other authorities, or involvement in the management of a business which has been investigated concerning fraud and dishonesty offences; and
    - involvement in judicial proceedings that are material or relevant to fitness and properness, insolvency or potential insolvency (for a corporation) or bankruptcy or potential bankruptcy (for an individual);

- for individuals mentioned above, their academic, professional and employment records;
- financial information to show the FRR position, business plans and structures, capital structure and basic information re shadow directors, etc.; and
- details of applicant's bank accounts, auditors, business addresses and premises where records will be stored.

### ***Representatives***

- 2.33 Individual applicants will generally be required to provide the information listed above in so far as they apply to individuals.

(For information to be submitted with other applications, please refer to the Information Rules.)

### **Licensing booklet**

- 2.34 The licensing booklet gives full details of the licensing requirements and the procedure for applying for a licence. [The version issued in August 2003 has been updated to align with the SFO and the new subsidiary legislation.](#)

### ***Fit and proper requirements (s.129, SFO)***

- 2.35 The four categories of the fit and proper requirements relating to financial status, competence (including educational qualifications for individuals), capability and character will apply to asset management as well.

### **Fit and proper guidelines for licensed corporations**

- 2.36 Fit and Proper Guidelines ('FPG') have been issued by the SFC and reflect broadly the requirements earlier issued as the Fit and Proper Criteria. They should be read together with the new Guidelines on Competence ('GC'), which replace the Guidance Note on Competence and the new Guidelines on Continuous Professional Training ('GCPT'), which replace the Guidance Note on Continuous Professional Training.
- 2.37 The three guidelines, the FPG, GC and the GCPT, apply to:
- persons applying to be licensed by or registered with the SFC and persons who are already licensed or registered to carry out regulated activities;

### ***Character and integrity***

- 2.46 An individual applicant must meet the same requirements as in paragraph 2.42 above.

An individual applicant whose application is successful should continue to meet the requirements in paragraphs 2.43 to 2.46 on an ongoing basis.

### ***Continuous Professional Training ('CPT')***

- 2.47 The Guidelines on Continuous Professional Training ('GCPT') set out the SFC's expectations regarding CPT. These will also be applied as appropriate by the HKMA.
- 2.48 The SFC expects every individual licensee to clock up a minimum of 5 CPT hours every calendar year per regulated activity with proportional hours for incomplete years. CPT may be obtained through attendance at courses, workshops, lectures and seminars, distance learning, self study with submission of assignments by recognized institutions, research, publications, speeches and so on. As with other similar programmes, normal work and the reading of financial journals and newspapers and other technical publications which do not involve interaction with other individuals will not count towards CPT.

### **HKMA requirements for staff engaged in regulated activities**

- 2.49 The HKMA expects staff of registered institutions responsible for or conducting regulated activities to comply with the SFC's FPG, GC and GCPT requirements. This compliance will be monitored by the HKMA.
- 2.50 The equivalents of responsible officers for registered institutions are called executive officers. There should be at least 2 executive officers for each type of regulated activity. At all times, there must be at least one executive officer available to supervise the regulated activity concerned. In addition, other staff of a registered institution conducting regulated activities must be on a register maintained by the HKMA of such persons. These are the equivalents of licensed representatives of licensed corporations.

Revision questions:

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- Question 1: Is an AFI conducting asset management activity required to register with the SFC?

Question 2: Will an exempt dealer engaged in asset management who is deemed to be a licensed corporation during the transitional period be required to meet FRR requirements under the SFO?

Question 3: What are the requirements for a licensed corporation relating to responsible officers?

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### **3 SFC's special requirements for the asset management industry**

#### *SFC's licensing guidelines for intermediaries advising on securities incidental to the marketing of MPF schemes only*

- 3.1 These guidelines were issued by the SFC in July 1999 and may need to be revised or absorbed into revised licensing guidelines. For the moment, the basic points of the July 1999 guidelines are discussed here.
- 3.2 The guidelines consider the position of persons advising on securities incidental to the marketing of MPF schemes and indicate that in certain circumstances they may require licensing as advising in securities (Type 4 regulated activity). Suggested activities triggering off licensing requirements are stated as:
- comparing the advantages and disadvantages of investing in different underlying products, and in so doing making reference to specific securities; or
  - commenting on their performance, merits, demerits, etc.
- 3.3 On the other hand, registration is generally not required in situations where:
- advice is simply given on the structure of an MPF scheme; or
  - generic advice is given on the constituent fund without advising on the underlying products that are securities.
- 3.4 The following guidelines are given for those whose sole activity requiring licensing may be that of giving advice on the underlying securities incidental to the marketing of MPF schemes.
- 3.5 *For corporations, the requirements are:*
- for a company, it must be incorporated in Hong Kong or be an overseas company registered with the Companies Registry with a valid Hong Kong business registration;

### **CPT**

- 5.4 Every individual licensee must attend at least 5 hours of CPT every calendar year for each regulated activity for which he is licensed, with proportionate hours for incomplete years. CPT may be obtained through:
- attendance at courses, workshops, lectures, seminars, distance learning, self-study with submission of assignments all with institutions acceptable to the SFC; and
  - relevant research, publications and speeches, and so on.
- 5.5 The SFC's Guidelines on CPT ('GCPT') gives guidance on the content of the training appropriate for representatives and directors and responsible officers. The Academic and Accreditation Advisory Committee ('AAAC') has approved certain institutions as acceptable for the operating of courses recognized for the [CPT](#).

### **Notification of changes**

- 5.6 Notification has to be made to the SFC in relation to changes in any information provided under Part V, SFO within seven business days of the change. The changes may relate to an application that has not been finalized or to a continuing regulated activity after licensing.

### **Information in annual returns to the SFC**

- 5.7 The information to be notified is set out in paragraph 5 and Schedule 3 to the Information Rules and includes for licensed persons the reporting periods, CPT returns, and any changes to information earlier provided which have not yet been notified to the SFC.
- 5.8 It should be noted that the annual return will be supplemented with annual audited financial statements. However, the annual return should be submitted within one month of the anniversary date of licensing or such other date as the SFC may approve, whereas the audited financial statements are to be submitted within 4 months of the financial year-end.

### **Particulars to be included in the public register maintained by the SFC**

- 5.9 The information to be contained in the public register maintained by the SFC is specified in s.136(2), SFO and in Schedule 4 of the Information Rules. The information includes:
- the names and addresses (including any electronic mail address and e-mail address) of the licensed corporation and its responsible officers;

- the CE ('Central Entity') identifying number issued by the SFC, the date of grant of the licence and whether or not it is suspended;
- the regulated activity or activities for which it is licensed and dates;
- the conditions, modifications and waivers, if any, on the licence and the effective date of their imposition;
- a record of each public disciplinary action (if any) taken by the SFC against the licensed corporation in Hong Kong (excluding any action that has been successfully appealed or is the subject of a pending appeal) (each such recorded action will be retained for a period of 5 years);
- the contact details of the assigned complaints officer; and
- a list of accredited representatives and the respective dates of accreditation.

(See Schedule 4 of the Information Rules for full details.)

- 5.10 The register, or a reproduction, should be available to the public for inspection at all reasonable times, and copies or extracts should be made available on payment of a fee. A copy or an extract certified by an authorized office of the SFC shall be admissible as evidence in any legal proceedings.
- 5.11 The register should also be made available to the public by the SFC in an on-line form.

***Annual fees (s.138, SFO)***

- 5.12 The annual fees are payable at the same time as the submission of the annual return, i.e. 1 month after the anniversary date of licensing. If a licensed person fails to pay the annual fee in full by the due date, he must pay additional penalty payments or be otherwise penalized as follows:
- 10% of the fee or such part of the fee that remains unpaid for the first month;
  - 30% of the fee or such part of the fee unpaid by the second month;
  - 50% of the fee or such part of the fee unpaid by the third month;
  - deemed suspension if remaining unpaid by the fourth month; and
  - deemed revocation if remaining unpaid by the fifth month.

Revision question:

### **Minimum required liquid capital for licensed corporations ('RLC')**

A licensed corporation should maintain liquid capital of not less than the amount specified in Table B for the regulated activity for which it is licensed. (Once again, if it is licensed for more than 1 regulated activity, the highest amount from Table B should be taken.)

**Table B**

<b>Regulated Activity</b>	<b>Liquid Capital</b>
Dealing in securities <ul style="list-style-type: none"> <li>• where it is an approved introducing agent or trader</li> <li>• others</li> </ul>	\$500,000 \$3m
Dealing in futures contracts <ul style="list-style-type: none"> <li>• where it is an approved introducing agent, futures non-clearing dealer or trader</li> <li>• others</li> </ul>	\$500,000 \$3m
Advising in securities <ul style="list-style-type: none"> <li>• and may not hold client assets</li> <li>• others</li> </ul>	\$100,000 \$3m
Advising on futures contracts <ul style="list-style-type: none"> <li>• and may not hold client assets</li> <li>• others</li> </ul>	\$100,000 \$3m
Asset management <ul style="list-style-type: none"> <li>• and may not hold client assets</li> <li>• others</li> </ul>	\$100,000 \$3m

6.5 [deleted]

***Calculation of liquid assets, ranking liabilities and financial adjustments using the asset manager's balance sheet***

- 6.6 While a responsible officer should be broadly aware of the bases used for making the calculations of the various classes of liquid assets, ranking liabilities and financial adjustments using the items in the balance sheet, examination candidates will not be tested on these matters.
- 6.7 General principles are that:
- the assets and liabilities and profit and loss accounts must be drafted on generally accepted accounting principles;
  - the bases used must recognize the substance of transactions;
  - Liquid capital = Approved assets – Ranking liabilities; and
  - the Liquid Capital ('LC') must exceed the minimum Required Liquid Capital ('RLC') at all times.

**Notifications and returns**

- 6.8 A licensed corporation, including an asset manager, must notify the SFC (s.146, SFO and ss.56 and 57, FRR):
- as soon as practicable if it fails to meet the minimum RLC and minimum paid-up share capital requirements, and cease to conduct business unless permitted by the SFC to continue;
  - within 1 business day if its LC falls below 120% of the RLC, or below the RLC, or below 50% of the LC last reported, or would fall below the RLC if it did not have an approved subordinated loan;
  - within 1 business day if it exceeds any borrowing limits, is unable to meet any repayment demands from lenders, or any lenders have liquidated or have notified an intention to liquidate any collateral security;
  - within 1 business day of becoming aware:
    - that the aggregate of its commitments, etc., or claims made against it, exceeds \$5 million or, if deducted from its LC, would reduce it to below 120% of the RLC;
    - if it has made any insurance claim under its professional indemnity insurance policy; or
    - any commitment, including a guarantee, has been provided on its behalf by a group company to an exchange or clearing house; or

## Checklist

Below is a checklist of the main points covered by this topic. Readers should use this checklist to test their knowledge.

- The intermediaries in the asset management industry include asset managers, distributors and others, including trustees and custodians.
- Asset managers include fund management houses, management companies, portfolio managers and the Hong Kong representatives of management companies located overseas.
- Distributors include AFIs, insurers, securities dealers, investment advisers, independent financial advisers and financial planners.
- Nevertheless, the SFC does place basic requirements on trustees and custodians of authorized CIS; e.g. they must be AFIs, trust companies that are subsidiaries of AFIs or registered under the Trustee Ordinance, or similar entities located overseas subject to acceptability by the SFC.
- The general licensing requirements on SFC-licensed corporations include the maintenance of insurance requirements, the approval of at least 2 responsible officers, one of whom must be an executive director and at least one responsible officer must be available at all times to supervise the business.
- It is an offence to carry on the activity of asset management without holding a valid SFC licence or being, in the case of an AFI, registered with the SFC.
- Under the transitional provisions, holders of licences as security dealers, commodity traders, investment advisers and commodity trading advisers may conduct the business of asset management subject to restrictions which basically distinguish between activities relating to securities and futures contracts (see table in paragraph 2.9 above).
- Exempt dealers under the pre-SFO regime may continue to act as securities dealers, securities advisers, commodity trading advisers and asset managers for 2 years after which they will have to apply for a licence to conduct any regulated activity.
- The fit and proper criteria for SFC licensing of corporations and individuals include matters relating to financial position, competence, capability and integrity; similar criteria are applied by the MPFA in registering individuals.
- Persons licensed to deal in securities (who do not carry on margin financing) and in futures contracts, to advise on securities and on futures contracts, and to conduct asset management (who in the last 3 cases may hold client assets) must have paid-up issued share capital of \$5 million.

- Persons licensed to deal in securities and in futures contracts should in each case have minimum liquid capital of:
  - (for those who are approved introducing agents) \$500,000; or
  - (for those who are not approved introducing agents) \$3 million.
- Persons licensed to advise on securities and on futures contracts, or to conduct asset management, are required to have:
  - (for those who do not in each case hold client assets) \$100,000; or
  - (for those allowed to hold client assets) \$3 million.
- A licensed corporation, including an asset manager, must notify the SFC as soon as practicable if it fails to meet the minimum paid-up capital or minimum liquid capital requirements, and must cease business unless and until the SFC permits it to continue its business.
- A licensed corporation, including an asset manager, must notify the SFC within 1 business day, if its liquid capital falls below 120% of its required minimum, below the required minimum, below 50% of the liquid capital last reported, or would fall below the required minimum if it did not have an approved subordinated loan.
- A licensed corporation that is not prohibited from holding client assets must submit a monthly declaration statement with supplementary returns within 3 weeks of the month-end, including a liquid capital calculation.
- A corporation licensed to conduct Type 4, 5 or 9 activity which is not allowed to hold client assets should submit a declaration statement for every 6 months and in June and in December of each year, with supplementary returns including a liquid capital computation and, in the case of an asset manager, an analysis of the assets under management.
- Refer to paragraph 6.13 for a list of offences relating to the FRR requirements.
- The Client Securities Rules do not apply to a fund manager that does not hold client assets but has discretion to operate client accounts and to instruct custodians to deal with client securities for settlement purposes; they will apply to a discretionary client portfolio run by an asset manager.
- The Client Money Rules do not apply to a fund manager who has discretion to operate clients' bank accounts and to instruct custodians to deal with clients' money for settlement purposes; they will apply to discretionary client portfolios.