



SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

Consultation Paper on Proposals to Enhance Asset Management Regulation and Point-of-sale Transparency

November 2016

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Foreword

The Securities and Futures Commission (SFC) invites market participants and interested parties to submit written comments on the proposals discussed in this consultation paper or to comment on related matters that might have a significant impact upon the proposals by no later than 22 February 2017. Any person wishing to comment on the proposals on behalf of any organisation should provide details of the organisation whose views they represent.

Please note that the names of the commentators and the contents of their submissions may be published on the SFC's website and in other documents to be published by the SFC. In this connection, please read the Personal Information Collection Statement attached to this consultation paper.

You may not wish your name and/or submission to be published by the SFC. If this is the case, please state that you wish your name and/or submission to be withheld from publication when you make your submission.

Written comments may be sent as follows:

By mail to: Securities and Futures Commission
35/F Cheung Kong Center
2 Queen's Road Central
Hong Kong

Re: Consultation Paper on Proposals to Enhance Asset
Management Regulation and Point-of-sale Transparency

By fax to: (852) 2877-0318

By online submission at: <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/>

By e-mail to: amrconsultation@sfc.hk

All submissions received before expiry of the consultation period will be taken into account before the proposals are finalised and a consultation conclusions paper will be published in due course.

Securities and Futures Commission
Hong Kong

23 November 2016



Personal information collection statement

1. This Personal Information Collection Statement (PICS) is made in accordance with the guidelines issued by the Privacy Commissioner for Personal Data. The PICS sets out the purposes for which your Personal Data¹ will be used following collection, what you are agreeing to with respect to the SFC's use of your Personal Data and your rights under the Personal Data (Privacy) Ordinance (Cap. 486) (PDPO).

Purpose of collection

2. The Personal Data provided in your submission to the SFC in response to this consultation paper may be used by the SFC for one or more of the following purposes:
 - (a) to administer the relevant provisions² and codes and guidelines published pursuant to the powers vested in the SFC;
 - (b) in performing the SFC's statutory functions under the relevant provisions;
 - (c) for research and statistical purposes; or
 - (d) for other purposes permitted by law.

Transfer of personal data

3. Personal Data may be disclosed by the SFC to members of the public in Hong Kong and elsewhere as part of the public consultation on this consultation paper. The names of persons who submit comments on this consultation paper, together with the whole or any part of their submissions, may be disclosed to members of the public. This will be done by publishing this information on the SFC website and in documents to be published by the SFC during the consultation period or at its conclusion.

Access to data

4. You have the right to request access to and correction of your Personal Data in accordance with the provisions of the PDPO. Your right of access includes the right to obtain a copy of your Personal Data provided in your submission on this consultation paper. The SFC has the right to charge a reasonable fee for processing any data access request.

Retention

5. Personal Data provided to the SFC in response to this consultation paper will be retained for such period as may be necessary for the proper discharge of the SFC's functions.

¹ Personal Data means personal data as defined in the Personal Data (Privacy) Ordinance (Cap. 486).

² The term "relevant provisions" is defined in section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571) and refers to the provisions of that Ordinance together with certain provisions in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32), the Companies Ordinance (Cap. 622) and the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615).



Enquiries

6. Any enquiries regarding the Personal Data provided in your submission on this consultation paper, or requests for access to Personal Data or correction of Personal Data, should be addressed in writing to:

The Data Privacy Officer
Securities and Futures Commission
35/F Cheung Kong Center
2 Queen's Road Central
Hong Kong

7. A copy of the Privacy Policy Statement adopted by the SFC is available upon request.



Proposals to Enhance Asset Management Regulation and Point-of-sale Transparency

Executive Summary

1. A robust regulatory regime is fundamental to the development and growth of an international asset management centre. In strengthening Hong Kong's position as a leading asset management centre, it is important to ensure that the regulatory regime for the asset management industry is in line with international regulatory developments. In this connection, the SFC has kept the regulatory regime for the asset management industry under regular review.
2. Post-global financial crisis, international bodies such as the International Organization of Securities Commissions (IOSCO), the Financial Stability Board (FSB) and other regulatory bodies have published an increasing volume of financial policy reforms with implications for the asset management industry on both public and private funds, in relation to issues and in areas such as systemic risk, shadow banking, liquidity and risk management, enhanced custody requirements, securities lending and repos, and reducing conflicts of interest. All these strive to enhance financial stability and produce better investor outcomes.
3. In light of these international developments, the SFC has reviewed the current regulations governing the asset management industry in Hong Kong and proposes various enhancements.
4. In formulating the proposed enhancements, the SFC is mindful of the need to strike a proper balance between facilitating market development and competitiveness on the one hand, and ensuring protection of investors' interests and market integrity on the other hand, and has conducted extensive soft consultations on the proposals with different industry stakeholders and received general support. The SFC has also discussed the proposals with the SFC's Products Advisory Committee (PAC) to ensure a more comprehensive understanding and deliberation of the relevant issues involved. There was general support for the proposals from members of the PAC as well.
5. There are two parts to this paper. Part I sets out the SFC's proposed enhancements to be made in respect of the following key areas in the Fund Manager Code of Conduct (FMCC), some of which are codifications of existing requirements and practice:
 - (a) Securities lending and repurchase agreements (repos)
 - (b) Custodian / safe custody of fund assets
 - (c) Liquidity risk management
 - (d) Disclosure of leverage
6. Other updates and housekeeping changes to the FMCC to provide better clarity and guidance are also discussed in Part I.
7. Part II discusses the proposed amendments to be made to the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of



Conduct). These amendments mainly aim to enhance point-of-sale transparency and to better address the potential conflicts of interest in the sale of investment products by adopting a two-pronged approach:

- (a) governing the conduct of intermediaries when representing themselves as “independent” or as providing “independent advice”; and
 - (b) enhancing the disclosure of monetary benefits received or receivable that are not quantifiable prior to or at the point of entering into a transaction.
8. Other matters that the SFC considered in formulating our proposals but decided not to include in our proposals are also discussed in Part II.
9. The SFC invites comments on the proposed enhancements. A consultation conclusions paper will be published as soon as practicable after the end of the consultation period.



Part I Fund Manager Conduct

Section 1

Key proposals in the FMCC

Introduction

10. Taking into account international regulatory developments as well as feedback from industry stakeholders, it is proposed that enhancements be made in respect of the following key areas in the FMCC, some of which are codifications of existing requirements and practices:
 - (a) Securities lending and repurchase agreements (repos)
 - (b) Custodian / safe custody of fund assets
 - (c) Liquidity risk management
 - (d) Disclosure of leverage
11. Apart from these key areas, we are also proposing to make other updates and housekeeping changes to the FMCC for better clarity and guidance as discussed in more detail below.

Persons to whom the FMCC applies

Fund managers responsible for the overall operation of a fund

12. The business activities carried out by persons licensed or registered for Type 9 (asset management) regulated activity may include the management of collective investment schemes (CIS) (whether authorized or unauthorized) and/or discretionary accounts (in the form of an investment mandate or pre-defined model portfolio). In the context of the management of CIS (also referred to as funds in this paper), some fund managers may manage only a portion of the fund under a sub-manager arrangement.
13. The various IOSCO principles / FSB recommendations and other international regulations on funds that the SFC proposes to adopt as enhancements to the regulations governing the asset management industry in this consultation paper also recognise the heterogeneous nature of activities, structures and responsibilities of relevant parties involved in the management of funds. In this connection, the SFC notes that despite the board of directors of a fund may be the legal party responsible for formally making decisions relating to the fund (such as appointing a custodian and issuing the offering documents of the fund), in practice, funds are often structured by fund managers to meet the objectives of clients or target clients and the fund managers may in substance be responsible for the overall operation of the fund (or may have de facto control). Hence, various principles and standards proposed to be adopted as enhancements will be applicable to the fund manager where it is, in substance, responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) notwithstanding that legally it is not the entity responsible for formally making decisions relating to the fund.



14. It is noted that the IOSCO principles also recognise that certain principles and standards should only apply to a fund manager who is responsible for the overall operation of a fund, and not those who, for example, only manage a portion of a fund. In view of the above, we are proposing that certain requirements or proposed requirements in the FMCC, for example, the setting of liquidity management policy and the appointment of a qualified custodian, would only be applicable to a fund manager who is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund).
15. An example of a fund manager who may be considered to have de facto control of the oversight or operation of a fund would be where the representatives of the fund manager and/or its affiliate(s) constitute a majority of the board of directors of the fund. To the extent that a fund manager is not responsible for the overall operation of a fund (and has no de facto control of the oversight or operation of the fund), for example, where the Hong Kong fund manager is appointed as sub-manager to manage only an allocated portion of the fund, certain FMCC principles and requirements will not be applicable. However, the generally-applicable FMCC principles and requirements, such as organisation and management structure, staff ethics, record keeping and conflicts of interest requirements, should be complied with by all fund managers.

Private funds

16. During the soft consultation process, the SFC received various comments and enquiries from fund managers seeking clarification on whether and how the FMCC is applicable to private funds which are not authorized by the SFC. Currently, the FMCC applies to persons licensed by or registered with the SFC whose business involves the discretionary management of CIS (whether authorized or unauthorized). Hence, the FMCC is applicable to all SFC licensed/registered fund managers, regardless of whether the funds they manage are public or private funds and whether the funds are domiciled in Hong Kong or overseas.
17. The SFC is aware that many of the proposed enhancements to the FMCC, which touch on areas such as liquidity management, leverage, custody of fund assets, valuation as well as fund reporting and disclosure requirements, may be perceived as more relevant to fund-level regulations whilst private funds are not currently subject to the SFC's regulation at the fund level.
18. In this connection, it should be noted that the focus of our regulations at the fund level remains on public funds offered to the investing public in Hong Kong³. The various proposed enhancements aim to reflect the latest international regulatory standards governing the conduct of fund managers, regardless of whether they are managing public or private funds, in order to reinforce good governance standards and enhance transparency. These IOSCO principles / FSB recommendations and other international regulations on CIS also do not specifically distinguish between public and private funds in their application. Instead, they focus on the activity of asset management and requirements at the fund manager level.
19. Accordingly, we consider that the application of the present proposals to both fund managers managing public funds and those managing private funds to be appropriate to

³ The relevant requirements are set out in the Code on Unit Trusts and Mutual Funds and the Overarching Principles Section of the SFC Handbook for Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Products.



ensure we continue to have in place a robust regulatory regime governing SFC-licensed / registered managers that is in line with international regulatory standards. This is important to reinforce Hong Kong's position as an international financial centre. The proposed enhancements would also give better protection to investors and allow the SFC to better monitor any systemic risks that may arise from asset management activities.

20. We are mindful of the potential implications of the proposed enhancements for private funds, including those domiciled in overseas jurisdictions. As such, the proposed requirements set out in the FMCC tend to be more principles-based to reflect the general principles laid down by IOSCO / FSB while more detailed requirements would be separately prescribed in the Code on Unit Trusts and Mutual Funds (UT Code) for public funds seeking the SFC's authorization for public offering.

Discretionary accounts

21. On a separate point, the SFC is of the view that all persons licensed by or registered with the SFC acting as managers of discretionary accounts (except for those offering such a service only as an ancillary part of their brokerage services for clients without establishing an investment mandate or a pre-defined model investment portfolio, and who do not receive management fee and/or performance fee as remuneration) should generally observe similar requirements that are applicable to managers of funds.
22. Hence, to provide clarity on the scope of application of the FMCC, we will make it clear in the revised FMCC that it applies to all persons licensed by or registered with the SFC whose business involves the management of CIS (whether authorized or unauthorized) and/or discretionary accounts (in the form of an investment mandate or a pre-defined model portfolio) (Fund Managers), including, where appropriate, their representatives⁴. The particular FMCC requirements that are not applicable to and other additional requirements applicable to managers of discretionary accounts will be set out in Appendix 1 to the FMCC.

Questions:

1. Do you have any comments on the proposed clarification that the FMCC applies to the business activities carried out by fund managers which would include the management of discretionary accounts?
2. Under the current proposal, some of the proposed enhancements are not applicable to all Fund Managers but only to those responsible for the overall operation of a fund or having de facto control of the oversight or operation of the fund. Do you agree with such an approach? If so, do you have any views on which of the proposed enhancements should only be applicable to those Fund Managers who are responsible for the overall operation of a fund or have de facto control of the oversight or operation of the fund? Please explain your views.

⁴ "Representatives" here has the same meaning as section 167 of the Securities and Futures Ordinance (Cap. 571).



Securities lending and repurchase agreements (repos)

Background

23. The global financial crisis exposed how the ability of non-bank entities and transactions could operate on a large scale in ways that create bank-like risks to financial stability. Since then, much focus has been placed on the “shadow-banking system”, that is, the part of the financial system that extends credit but is outside the regular banking sector. To deal with the issues emerging from the shadow banking system, the FSB set up, amongst other workstreams, the Workstream on Securities Lending and Repos to assess financial stability risks and develop policy recommendations, where necessary, to strengthen regulation of securities lending and repos markets.
24. The FSB reports, *Strengthening Oversight and Regulation of Shadow Banking: Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos*⁵ and *Transforming Shadow Banking into Resilient Market-based Finance: Regulatory framework for haircuts on non-centrally cleared securities financing transactions*⁶, together set out 18 key policy recommendations for addressing financial stability risks in relation to securities lending and repos.
25. In the context of funds, SFC-authorized funds may engage in securities lending, repo and similar over-the-counter (OTC) transactions subject to relevant requirements in the UT Code and SFC Products Handbook⁷ which generally require that the transactions should be conducted in the best interests of holders and the associated risks have been properly mitigated and addressed. On the other hand, the FMCC currently does not expressly place obligations on a Fund Manager where a fund under its management engages in such activities. In view of the FSB recommendations, some of which are to be implemented by 2017, the SFC proposes to adopt certain FSB recommendations to address shadow banking risks in securities lending and repos in the funds arena.

Proposals

Collateral valuation and management policy

26. It is proposed that where a Fund Manager engages in securities lending, repo and similar OTC transactions on behalf of the funds it manages, it should put in place a collateral valuation and management policy which should include certain minimum valuation and margin requirements.

Eligible collateral and haircut policy

27. The Fund Manager should also put in place an eligible collateral and haircut policy which should cover the types of acceptable collateral and the methodology to calculate haircuts on collateral received in connection with these transactions. The Fund Manager should

⁵ Strengthening Oversight and Regulation of Shadow Banking: Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos issued by the FSB on 29 August 2013.

⁶ Transforming Shadow Banking into Resilient Market-based Finance: Regulatory framework for haircuts on non-centrally cleared securities financing transactions issued by the FSB on 12 November 2015.

⁷ SFC Handbook for Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Products.



consider and assess the acceptability of collateral when formulating their collateral and haircut policy.

28. The haircut methodology should be designed on the basis that haircuts are set to cover the maximum expected decline in the market price of the collateral asset (over a conservative liquidation horizon) before a transaction can be closed out. A Fund Manager is expected to exercise professional judgment and give due consideration to the specific nature of each fund it manages when designing the haircut methodology taking into account relevant international regulatory standards and FSB recommendations⁸. The SFC will provide guidance on standards for designing haircut methodologies which would reflect the standards set by the FSB in its recommendations by way of Frequently Asked Questions (FAQs). Further details of the proposed requirements are set out in Appendix C to this consultation paper.

Reinvestment of cash collateral

29. We also propose that where a Fund Manager engages in securities lending, repo and similar OTC transactions on behalf of the funds it manages, and reinvests cash collateral received by the funds, it should put in place a cash collateral reinvestment policy which seeks to ensure that assets held in the cash collateral reinvestment portfolio are sufficiently liquid with transparent pricing and low risk to meet reasonably foreseeable recalls of cash collateral, and should stress test the ability of a cash collateral reinvestment portfolio to meet foreseeable and unexpected calls for the return of cash collateral on an ongoing basis.
30. In designing its cash collateral reinvestment policy, it is expected that a Fund Manager should consider setting specific requirements for the cash collateral reinvestment portfolio and/or liquidity pool maintained to meet cash collateral recalls, including requiring a minimum portion of the cash collateral to be kept in short-term deposits, held in highly liquid short-term assets, or invested in short tenor transactions; and setting specific limits for the weighted average maturity and/or weighted average life.
31. During the SFC's soft consultation with various industry bodies, the question on whether non-cash collateral can be re-hypothecated was raised. It is our view that, in the case of non-SFC-authorized funds, if non-cash collateral received is re-hypothecated, there should at least be adequate disclosure made by the Fund Manager who is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) to investors in respect of the details of the re-hypothecation, for example, non-cash collateral re-use arrangements, and related risks, so that investors can understand the relevant risks and exposures to the fund. However, non-cash collateral should not generally be re-hypothecated in the case of SFC-authorized funds and the relevant requirements under the UT Code and the SFC Products Handbook should be complied with.

Reporting to fund investors

32. It is proposed that where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), a summary of the securities lending, repo and similar OTC transactions policy and the risk management

⁸ Please refer to [Transforming Shadow Banking into Resilient Market-based Finance: Regulatory framework for haircuts on non-centrally cleared securities financing transactions](#) issued by the FSB on 12 November 2015.



policy (including haircut policy, selection criteria of securities lending counterparties, collateral policy and the relevant provisions in the securities lending arrangements) should be disclosed in the offering documents of a fund.

33. It is further proposed that a Fund Manager should provide, at least on an annual basis and upon request, information relating to securities lending, repo and similar OTC transactions to clients (and, where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the fund's oversight and operations), to fund investors). The minimum requirements on the information that should be disclosed is set out in Appendix C to the consultation paper and will be set out in FAQs to be issued by the SFC.
34. In the course of its soft consultation with industry stakeholders, the SFC received comments and enquiries that generally, a fund would appoint a third-party agent to conduct securities lending and repo activities on its behalf. It was expressed that due to such an agency arrangement, the relevant Fund Manager would not have access to information on a fund's securities lending, repo and similar OTC transactions, including information on a fund's cash collateral reinvestment portfolio, or have control over the agent. However, the SFC is of the view that Fund Managers should obtain access to the relevant information from the third-party agent. For instance, Fund Managers should ensure that the trustee / Board of Directors of the fund can exercise their power to receive information on such transactions from the agent (for example, by way of its contract with the agent) and pass on the information to the Fund Manager.

Questions:

3. Do you have any comments on the above proposals which will be applicable to a Fund Manager which engages in securities lending, repo and similar OTC transactions on behalf of the funds it manages?
4. Do you have any views or comments on the proposal that Fund Managers should design their haircut methodologies which should reflect the standards set by the FSB in its recommendations⁹?
5. Is the requirement to disclose details of non-cash collateral re-hypothecation sufficient to enable investors to understand the relevant risks and exposures to the fund? Please explain your views.
6. Do you have any comments on the proposed requirements on reporting to fund investors? In particular, do you have any comments on the minimum disclosure requirements proposed?

Custodian / safe custody of fund assets

Background

35. After the global financial crisis, heightened attention has been placed on the protection of investors' assets globally. In the context of funds, key risks relevant to the custody of fund

⁹ Please refer to [Transforming Shadow Banking into Resilient Market-based Finance: Regulatory framework for haircuts on non-centrally cleared securities financing transactions](#) issued by the FSB on 12 November 2015.



assets include, but are not limited to, operational risk, misuse of fund assets, and risk of fraud or misappropriation. These risks have intensified given the increasing trend of funds investing in more complex instruments and the increase in the diversification and internationalisation of fund portfolios. Such trends have expanded the scope and complexity of assets under custody and have given rise to the need to appoint sub-custodians in foreign jurisdictions, thus lengthening and amplifying the complexity of custody chains.

36. In response to these market developments, regulatory authorities in overseas jurisdictions have been carrying out reviews and reforms of their respective safe custody regimes. At the international level, IOSCO issued a report, *Standards for the Custody of Collective Investment Schemes' Assets* in November 2015 to clarify, modernise and further develop standards for the custody of CIS assets consistent with the core IOSCO principles, *Objectives and Principles of Securities Regulation*, June 2010. The SFC proposes to adopt the latest relevant principles under the IOSCO standards which are mostly enhancements to the current FMCC requirements in relation to custody of fund assets.

Proposals

37. "Custody" is broadly defined by IOSCO to consist of the safekeeping and record-keeping of CIS assets (depending on the type of asset owned by the CIS) to ensure the physical and legal integrity of the asset.

Safekeeping of fund assets and independence

38. Proper segregation of fund assets is a fundamental principle for the safekeeping of fund assets. It enables the identification of ownership and protects against commingling of fund assets, which in turn mitigates the risk of loss of fund assets as a result of the insolvency of a custodian along the custody chain. In view of this, the SFC proposes to codify in the FMCC current requirements governing the safety of client assets to expressly require that fund assets should be segregated from the assets of the Fund Manager, and, unless they are held in an omnibus account, also segregated from the assets of affiliates and other clients of the Fund Manager while retaining the general principle that fund assets entrusted to a Fund Manager should be properly safeguarded.
39. Where fund assets are held in an omnibus client account, the Fund Manager should ensure that adequate safeguards are put in place such that fund assets belonging to each client are appropriately recorded with frequent and appropriate reconciliations being performed. Regardless of how fund assets are held and recorded, the key underlying principle is that fund assets should be at all times readily identifiable in the custodian's (and in the case of self-custody, the Fund Manager's) books and records as belonging to the fund.
40. In order to minimise and manage conflicts of interest arising from custodial arrangements, we propose to expressly require that where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), the Fund Manager should arrange for the appointment of, and entrust the fund assets to, a custodian that is functionally independent from it.
41. The SFC notes that some Fund Managers managing private funds may adopt a self-custody arrangement. To extend this concept of independence to self-custody arrangements, it is proposed that where self-custody is adopted, the Fund Manager should



ensure that it has policies, procedures, and internal controls in place to ensure that the persons fulfilling the custodial function are functionally independent from the persons fulfilling the fund's management or administration functions.

Selection of custodian, custody agreement and monitoring of custody arrangements

42. The SFC proposes to enhance the relevant requirement in the FMCC to explicitly require a Fund Manager to exercise due skill, care and diligence in the selection, appointment and ongoing monitoring of the custodian where it is responsible for the overall operation of a fund (or has de facto control of the fund's oversight and operations). One argument often put forward is that, for funds structured in a corporate form, the custodian is legally appointed by the board of directors of the fund and not by the Fund Manager. However, it should be noted that very often, funds are structured by the Fund Manager itself in practice and the Fund Manager who is responsible for the overall operation (or has de facto control of the oversight and operation) should therefore be able to fulfil this requirement.
43. Further, the Fund Manager who is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) should ensure that a formal custody agreement is entered into with the custodian appointed for custody of the fund's assets. It should also ensure that the custody agreement includes provisions about the scope of the responsibility and liability of the custodian, and monitor the custody arrangements on an ongoing basis to ensure the custodian's compliance with the custody agreement.

Disclosure of custody arrangements

44. Given the importance of the safekeeping of fund assets, it is proposed that a Fund Manager responsible for the overall operation of a fund (or who has de facto control of the fund's oversight and operations) should ensure that the custody arrangements in respect of assets of the fund and any material risks associated with the arrangements (including additional safeguards to mitigate any potential conflicts of interest that have been put in place where self-custody is adopted) are properly disclosed to the fund's investors and that fund investors are updated about any significant changes.

Question:

7. Do you have any comments on the above proposals regarding custodian and safe custody of fund assets?

Liquidity risk management

Background

45. Since the global financial crisis, the issue of liquidity and the management of liquidity risks has been a major focus internationally. In the context of funds, a failure to properly manage a fund's liquidity risk could result in adverse outcomes for the fund and its investors, including the inability to meet redemptions or meeting redemptions in a manner unfair to the fund and its remaining investors. Redemption cycles may also exacerbate stress of the fund. Effective liquidity risk management is therefore important not merely because it can minimise the risk that redemption requests cannot be met, but also



because it can safeguard the interests and fair treatment of fund investors, and maintain the robustness of the funds' liquidity and market integrity.

46. In March 2013, to provide guiding principles on liquidity risk management for funds, IOSCO issued its *Principles of Liquidity Risk Management for Collective Investment Schemes* which sets out a framework of principles for managing liquidity risks of CIS, whether public or private. In this connection, for public funds authorized by the SFC, the SFC has recently issued a circular¹⁰ to provide guidance to the management companies of SFC-authorized funds on liquidity risk management. The SFC also proposes to adopt in the FMCC relevant IOSCO principles for Fund Managers of both public and private funds. However, the SFC is mindful that at the international level, discussions and requirements in relation to liquidity risk management are ongoing and evolving and as such the SFC will keep in view any regulatory developments and the need for any subsequent amendments to the current proposals.

Proposals

Liquidity management policy

47. The effective operation of a liquidity risk management process is a fundamental part of the risk management process of a fund. It is thus proposed that where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the fund's oversight and operations), the Fund Manager should maintain and implement effective liquidity management policies and procedures to monitor the liquidity risk of the fund, taking into account the investment strategy, liquidity profile, underlying obligations and redemption policy of the fund, and should ensure that the effectiveness of its liquidity management policies and procedures is periodically reviewed and updated as appropriate.
48. During soft consultations with various industry groups, the applicability of the liquidity risk management proposals was raised, as comments were made that the proposed IOSCO principles appeared to be more relevant to open-ended funds. It should be noted that although liquidity risk management is a particular concern for open-ended funds, some of the principles are relevant to private funds (sources of liquidity risk may include margin calls for derivatives and other financing obligations). Whilst recognising that the extent of the application of the proposed liquidity management principles will depend on the nature, liquidity profile and asset-liability management of the fund in question, it is expected that a Fund Manager of any type of fund should still consider the extent of the applicability of the requirements on liquidity risk management proposed to be adopted in the FMCC to the funds it manages and ensure that its activities are commensurate with the liquidity profile of the fund.

Stress testing

49. As part of the implementation of the liquidity risk management policies and procedures, appropriate assessments should be carried out by the Fund Manager (where it is responsible for the overall operation of a fund or has de facto control of the fund's oversight and operations) of the liquidity risk to the fund in normal and stressed scenarios (for example, atypical redemption requests). We thus propose that a Fund Manager

¹⁰ Circular to management companies of SFC-authorized funds on liquidity risk management issued by the SFC on 4 July 2016.



should conduct regular assessments of liquidity in different scenarios, including stressed situations, to assess and monitor the liquidity risk of the funds accordingly.

50. It was suggested during soft consultations that the SFC should give discretion to Fund Managers to decide which fund/account requires regular stress testing as not all types of funds/accounts need stress testing. Our view is that a Fund Manager should perform liquidity stress testing on its funds on an ongoing basis to assess the impact of plausible severe adverse changes in market conditions on the liquidity of the funds. The extent or frequency of the testing may however be varied depending on the nature and liquidity profile of each fund. The SFC expects that stress test results should be reviewed by a committee responsible for liquidity risk management and/or senior management to determine whether further actions are warranted. Even if it is decided that no immediate actions are warranted, the Fund Manager should have in place action plans regarding how it would meet the fund's liquidity needs should any of the stress scenarios materialise.

Tools and exceptional measures

51. Liquidity risk management tools are often effective means to protect fund investors' interests and to ensure a fair outcome for the fund and its investors as such tools can allow fund managers to process redemptions in an orderly manner and to mitigate first-mover advantage.
52. As such, we propose to incorporate into the FMCC a general principle that where the constitutive documents of a fund allow the use of specific tools or exceptional measures which could affect redemption rights, the Fund Manager should consider the appropriateness of using such specific tools and exceptional measures, taking into account the nature of assets held by the fund and its investor base.
53. In addition, we would like to highlight that in the use of liquidity risk management tools, investors' interest should take priority over a Fund Manager's own interest, such as reputational and competitive concerns.
54. As investors' redemption rights may potentially be affected by such tools and exceptional measures, and are limited when such tools and exceptional measures form part of the investment strategy of a fund, an explanation of any such tools and exceptional measures should be disclosed in the fund offering documents. Where side letters have been entered into, a Fund Manager should disclose such fact and the material terms in relation to redemption in the side letters to all potential and existing fund investors¹¹.

Questions:

8. Do you have any comments on the above proposals regarding liquidity risk management?
9. Do you have any suggestions on any particular liquidity management measures which a Fund Manager should put in place for effective liquidity management, for example, in terms of setting liquidity targets or stress testing?

¹¹ Circular to All Licensed Corporations Engaged in Hedge Funds Management Business issued by the SFC on 27 October 2008.



Disclosure of leverage

Background

55. At the international level, there has been increased scrutiny of the use of leverage by funds on the premise that such activities may contribute to the build-up of systemic risk or disorderly markets. Leverage within investment funds has been identified by the FSB as a potentially important structural vulnerability in the asset management sector and it has recommended that regulators should collect data on leverage in funds and monitor the use of leverage by funds, while IOSCO is developing measures of leverage in funds.¹²
56. Overseas jurisdictions have also placed more focus on leverage in funds. In the United States (US), the Securities and Exchange Commission (SEC) requires investment advisers to private funds to report various information relating to leverage to the SEC in its regulatory form, Form PF, primarily for use by the Financial Stability Oversight Council for systemic risk monitoring. Investment advisers with regulatory assets under management (AUM) attributable to private funds of at least US\$150 million are required to report such information once a year. Hedge fund advisers with regulatory AUM attributable to hedge funds of at least US\$1.5 billion are also required to report more detailed leverage information every quarter.
57. In Europe, under the Alternative Investment Fund Managers Directives (AIFMD), special requirements are applicable to Alternative Investment Fund Managers (AIFM) which employ leverage on a substantial basis at the Alternative Investment Fund (AIF) level. Such AIFMs are required to report to regulators information regarding the overall level of leverage employed, the leverage arising from borrowing of cash or securities and the leverage arising from positions held in derivatives, the extent of reuse of assets and the main sources of leverage in their AIF. In terms of disclosure to investors, AIFMs are required to make available to AIF investors the maximum level of leverage which the AIFM is entitled to employ on behalf of the AIF.

Proposal

Disclosure of maximum leverage to investors of the fund

58. For the purpose of enhancing disclosure and transparency to fund investors, it is proposed that a Fund Manager who is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) should disclose the maximum level of leverage which it may employ on behalf of each fund it manages.
59. We note that in the international arena, there is currently no general consensus on how leverage should be calculated. Hence, while the SFC does not propose to prescribe the method for calculating leverage at this stage, we propose that the Fund Manager should take into account financial leverage arising from borrowings and synthetic leverage arising from the use of derivatives in calculating leverage and disclose the basis of calculation it has adopted, which should be reasonable and prudent, having due regard to international best practices, in the fund's offering document. The SFC will continue to keep in view the international regulatory developments in this area, and review our regulations where appropriate.

¹² Consultative Document, *Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities* issued by the FSB on 22 June 2016.



60. As noted from our soft consultation discussions that information about leverage is one of the key pieces of information that investors of private funds require, the SFC believes that in practice there should not be any major difficulties in complying with this disclosure requirement by Fund Managers.

Questions:

10. Do you consider it appropriate for Fund Managers to disclose the maximum leverage of the fund it manages to fund investors?
11. Do you have any comments on how leverage should be calculated?

Section 2

Other amendments

Background

61. We also propose other amendments to update and modernise the FMCC. These amendments are mostly a codification of existing requirements and/or practices, updates, or housekeeping changes to improve clarity. Details of the amendments can be found in the indicative draft of the revised FMCC, which is set out at Appendix A. A summary of the major amendments are set out below.

Proposals

Fund portfolio valuation

62. The accurate valuation of fund assets is essential to the integrity of the running of a fund and investor protection. To update and modernise principles for CIS valuation and keep abreast of market developments, IOSCO published the *Principles for the Valuation of Collective Investment Schemes* in May 2013. While the FMCC currently includes requirements governing the valuation policies and procedures of Fund Managers, the SFC proposes to expressly codify existing requirements and industry practices with reference to relevant principles under these IOSCO principles. These include requirements with respect to the independent valuation of fund assets and periodic review of valuation policies and procedures and fund valuation processes. In this connection, it is generally considered that independence in the valuation process can be achieved by various means such as the appointment of a qualified independent third party to be involved in the valuation process or the separation of the valuation and/or pricing function from the investment function so as to ensure that the persons who are responsible for making investment decisions will not determine the valuations, although they may be able to provide input as appropriate.

Audited financial statements

63. To codify existing industry practice, the FMCC will explicitly require that where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should appoint an independent auditor to perform an audit of the financial statements of each of the funds it manages and make available an



annual report for each of the funds it manages, which is prepared in accordance with generally accepted accounting principles.

Risk management

64. The FMCC currently sets out key principles which require a Fund Manager to maintain sufficient human and technical resources and experience for proper performance of its duties. It also requires a Fund Manager to maintain satisfactory risk management governance structure and procedures commensurate with the size, complexity and risk profile of the firm and the investment strategy adopted by each of the funds under its management. In addition, certain suggested risk management control techniques and procedures are also set out in the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC (ICG) to give additional guidance on the topic to all SFC-licensed or registered persons, including Fund Managers.
65. In order to provide further guidance to Fund Managers on this important subject, we are proposing some enhancements and updates to the FMCC, both in respect of risk management of the Fund Manager and also risk management of the funds managed by the Fund Manager. These enhancements are mainly an elaboration of existing requirements.
66. We have also elaborated on the risk management requirements at the fund level. In particular, in order to make the FMCC a more comprehensive and tailored guidance to Fund Managers, we have introduced a new Appendix 2 to the FMCC setting out certain suggested risk management control techniques and procedures which a Fund Manager should take into account, where applicable, in monitoring the risks of the funds it manages. These suggested techniques and procedures are largely an elaboration of the existing suggested risk management control techniques and procedures set out in the ICG but tailored for application in the context of funds. We have also added certain specific suggestions in respect of business continuity and transition plan in line with the latest international regulations in this area. For the avoidance of doubt, the revised FMCC does not supersede the ICG and Fund Managers are still required to comply with the provisions in the ICG.

Side pockets

67. Some funds may set up side pockets where certain illiquid or hard-to-value investments of a fund as determined by the Fund Manager are segregated from other fund assets.
68. In order to make the FMCC a more comprehensive and tailored guidance to Fund Managers, we have added a new section on side pockets in the FMCC mainly reflecting the relevant requirements set out in the SFC Circular issued on 27 October 2008, "*Circular to All Licensed Corporations Engaged in Hedge Funds Management Business*".

Reporting

69. To enable the SFC to be in a better position to monitor and detect risks arising from asset management activities such as securities lending and repos and employment of leverage as well as to fulfil the increasing international regulatory obligations mentioned above, the SFC would need to collect relevant information from Fund Managers from time to time or on an ad hoc basis.



70. The reporting requirements expected to be complied with by Fund Managers on an ongoing basis have been set out in more detail in the revised FMCC. The SFC will engage the industry on the items for data collection in due course.

House accounts

71. The FMCC currently provides that where a client order has been aggregated with another order, the client's order must take priority in any subsequent allocation for partially filled orders. Order aggregation may not always be in the best interests of a client as it can result in an order exceeding the range of normal market order sizes and lead to increased market impact costs. We have added a clarification under paragraph 3.10 (a) of the proposed FMCC that aggregation of house orders with client orders should only be made if it is in the best interests of clients. Since this clause is applicable to the aggregation of both buy and sell orders (ie, when a fund invests into or disposes of holdings respectively), we have simplified paragraph 3.10 (c) of the proposed FMCC by deleting the duplicated text to improve clarity, such that paragraph 3.10 (a) now addresses the requirements on order aggregation and client priority, and paragraph 3.10 (c) addresses the requirements against front running.

Miscellaneous amendments

72. In line with the key principles currently laid down in the FMCC and to provide further guidance to the industry, we have elaborated on the responsibilities of Fund Managers in respect of a number of areas. We have also revised the requirements in respect of transactions with connected persons.
73. To reflect the revised structure of the FMCC and to clarify the application of the FMCC in different business operation contexts, we have refined the definition or interpretation of a number of terms in the FMCC. Amendments are also proposed to clarify the intended scope of application of particular provisions in the corresponding business operation context.
74. As licensed persons engaging in electronic trading should comply with the Code of Conduct, the section on Electronic Trading in the existing FMCC has therefore been removed.

Questions:

12. Do you have any comments on the other amendments proposed to the FMCC?
13. Under the existing requirement, where a client's order has been aggregated with a house order, the client's order must take priority in any subsequent allocation of partially filled orders. Are there any circumstances where it is in the best interests of clients to aggregate their orders with house orders? What are those circumstances which justify that they are in the best interests of clients? Are there any circumstances in which an institutional professional investor should be able to request pro rata allocation of aggregated but partially filled orders, on the terms specified by such an investor? What are those circumstances? Does the investor who request pro rata allocation have concerns that the flexibility can be abused by the licensed manager?



14. Do you have any comments on the suggested risk-management control techniques and procedures as set out in Appendix 2?

Appendix 1 to the FMCC – Requirements for licensed or registered persons conducting discretionary accounts management

75. As mentioned above, the SFC is of the view that the requirements set out in the FMCC are generally applicable to licensed or registered persons that manage discretionary accounts (Discretionary Account Manager) which are operated in the following manner:-
- (a) The Discretionary Account Manager provides discretionary management services to a client, in the form of an investment mandate or a pre-defined model investment portfolio¹³; and
 - (b) The Discretionary Account Manager receives management fee and/or performance fee as remuneration for managing discretionary accounts for its clients.
76. The SFC does not intend to apply the requirements set out in the FMCC to those licensed or registered persons whose provision of discretionary account services is an ancillary part of brokerage services for clients. For example, where a client has opened a securities trading account with a securities brokerage firm and authorized an account executive to trade his account with discretion without establishing an investment mandate or pre-defined model investment portfolios and that the brokerage firm does not receive management fee and/or performance fee in addition to commission fees.
77. However, the SFC is aware that not all requirements in the FMCC are equally applicable to Discretionary Account Managers as they are to Fund Managers, while other requirements should only be applicable to Discretionary Account Managers (for example, minimum content of Discretionary Client Agreement). As such, Appendix 1 sets out the particular requirements in the FMCC which are not applicable to Discretionary Account Managers and additional requirements which are only applicable to Discretionary Account Managers.

Questions:

15. Do you have any comments on the requirements set out in Appendix 1?
16. Do you think a 6-month transition period following gazettal of the final form of the amendments to the FMCC is appropriate? If not, what do you think would be an appropriate transition period and please set out your reasons.

¹³ The investment mandate may set out, amongst others, the types, risks and allocation of investments after taking the client's investment objectives and strategies into account. In the case of a pre-defined model portfolio, it may specify the proportion of the asset classes and markets and the risk profile of the selected portfolio.



Part II Intermediaries conduct

Section 1

Key proposals in the Code of Conduct

Inducements / commissions

Background

78. After the global financial crisis, there have been a number of regulatory developments internationally which aim to address inherent conflicts of interest and introduce more transparency. One significant change relates to inducements and commissions received by financial advisers and distributors.
79. In the United Kingdom (UK), the Financial Conduct Authority implemented a set of rules, the Retail Distribution Review (RDR), in 2013, under which financial advisers are no longer permitted to earn commissions from fund companies in return for selling or recommending their investment products. Instead, investors have to agree fees with the adviser upfront which in essence is a “pay-for-advice” model. In addition, financial advisers in the UK now offer either “independent” or “restricted” advice and must explain the difference between the two – essentially making clear whether their recommendations are limited to certain products or product providers. In relation to securities products, Australia has also banned commissions, again, opting for a pay-for-advice model. Furthermore, the Canadian Securities Administrators (CSA) are considering to consult on discontinuing embedded commissions and transitioning to direct pay arrangements.
80. Whilst a pay-for-advice model may eliminate the inherent conflict of interest in receiving benefits from product providers in the sale of investment products to clients, it may have unintended consequences. For instance, an “advice gap” may have emerged in jurisdictions adopting a pay-for-advice model where investors who are without the resources to pay for or unwilling to pay for advice for any reason could be left with no or very limited access to investment products.
81. An alternative approach is adopted in the European Union under the Markets in Financial Instruments Directive II (MiFID II). Under MiFID II, if investment advice is provided on an independent basis, the investment firm is prohibited from accepting and retaining fees, commissions or any monetary or non-monetary benefits paid or provided by any third party. Similarly, in Singapore, the term “independent” can only be used if a financial adviser does not receive any commission for products provided which may create product bias.
82. In terms of enhancing transparency, various regulatory developments in major jurisdictions have sought to increase the information disclosed to investors in relation to costs and charges, for example, under MiFID II. From January 2018, MiFID II will require improved disclosure of all costs and charges in relevant products and services, including funds, by requiring disclosure of information relating to investment services, the cost of the financial instrument and how the client may pay for it, which also encompasses any third-party payments. In relation to third-party payments, they are to be identified separately (ie, it should be clear to the client which part of the costs paid are rebated to the investment firm providing the investment service).



83. The US SEC Investor Advisory Committee also recently reviewed various ways to improve mutual fund cost disclosures¹⁴. One of its recommendations was to require standardised disclosure of actual dollar amount costs on customer account statements.
84. In Hong Kong, intermediaries are currently required to disclose monetary and non-monetary benefits received or receivable by it in relation to distribution of an investment product. Such disclosure was introduced back in 2010 and became effective in 2011 as one of the key proposals to enhance protection for the investing public following the global financial crisis.
85. In relation to monetary benefits received or receivable by intermediaries that are not quantifiable prior to or at the point of entering into a transaction (eg, the ongoing commission payable by product issuers to intermediaries for distribution (in the context of funds, trailer fees)), the Code of Conduct currently requires the licensed or registered person to disclose the existence and nature of such monetary benefits. From our observations of the disclosure practices adopted by intermediaries, some intermediaries disclose a maximum percentage amount receivable, and others disclose only a description of the costs and fees with no indicative monetary amount or percentage. Such varied disclosure practices may not help investors compare costs and fees amongst different intermediaries.
86. We also note that a number of international jurisdictions are currently looking at improving transparency for cases where the intermediary does not explicitly receive monetary benefits for distributing an investment product (eg, where the investment product is issued by an associate of the distributor). In Hong Kong, the disclosure of such non-explicit remuneration arrangements is already covered under the Code of Conduct whereby the intermediary is required to disclose where it or any of its associates will benefit from the origination and distribution of the product. As such, and given this is still an evolving topic internationally and no consensus has yet been reached, we do not propose to change the existing requirement but will continue to keep in view developments overseas.

Policy considerations

87. In deliberating on the approach to be taken in Hong Kong, the SFC is mindful of the characteristics of the Hong Kong investment market and investor behaviour.
88. According to a global market survey conducted in 2015¹⁵, the results for Hong Kong show that only 11 percent of the persons surveyed would be willing to pay HK\$15,000 or more for financial planning services with the majority (55 percent) only willing to pay HK\$5,000 or less. Further, more than five in 10 (54 percent) consumers rely on friends and family for information about financial matters and planning, while only 29 percent rely on financial planners. It was noted that one of the top three barriers to financial planning is that Hong Kong consumers feel that the fees / costs charged for financial advice are not worth it. From a market landscape point of view, based on market research, it is noted that up to only three percent of the retail fund distribution in Hong Kong was done through the independent financial advisers channel¹⁶. Based on these survey results, the adoption of

¹⁴ *Recommendation of the Investor Advisory Committee Regarding Mutual Fund Cost Disclosure* issued by the SEC on 14 April 2016.

¹⁵ *The Value of Financial Planning and Awareness of CFP Certification: A Global Financial Planning Survey* issued by the Financial Planning Standards Board and GfK in 2015

¹⁶ *Risk-focused Industry Meeting Series: Asset Management: Looking Forward* issued by the SFC in January 2015.



a pay-for-advice model with a complete ban on receipt of commissions by intermediaries may not seem appropriate for Hong Kong.

89. To address the conflicts of interest arising from intermediaries receiving benefits from other parties including product providers in the sale of investment products to clients, it is proposed that a two-pronged approach be taken in:
- (1) governing the conduct of intermediaries when representing themselves as “independent” or as providing “independent advice”; and
 - (2) enhancing the disclosure of monetary benefits received or receivable that are not quantifiable prior to or at the point of entering into a transaction.
90. We believe that this would be a balanced approach more appropriate for Hong Kong’s market landscape and would avoid any potential unintended consequences associated with a pay-for-advice model. In particular, we have taken into consideration the various investor protection measures and requirements that already exist under the Code of Conduct and related guidance. For instance:
- (a) as a general principle, a licensed or registered person should act in the best interests of its clients when distributing investment products to them¹⁷;
 - (b) a licensed or registered person must not take commission rebates or other benefits receivable by them or their related companies as the primary basis for recommending particular investment products to clients¹⁸;
 - (c) a licensed or registered person is required to ensure that it takes into account available alternatives in its advice and recommendations to clients¹⁹;
 - (d) where a licensed or registered person distributes an investment product to a client, it should disclose its affiliation with a product issuer to the client prior to or at the point of entering into a transaction²⁰; and
 - (e) where a licensed or registered person only recommends investment products which are issued by its related companies, it should disclose this limited availability of investment products to each client²¹.
91. Subject to consultation feedback on the proposals, we will continue to keep in view the effectiveness of this two-pronged approach following its implementation.

Proposals

(1) Restriction on the use of the term “independence”

¹⁷ General principles (GP1) under the Code of Conduct.

¹⁸ Circular on “Questions and Answers on Compliance with Suitability Obligations” issued by the SFC on 8 May 2007, as updated from time to time.

¹⁹ Paragraph 3.4 of the Code of Conduct.

²⁰ Paragraph 8.3A(a)(ii) of the Code of Conduct.

²¹ Circular on “Questions and Answers on Compliance with Suitability Obligations” issued by the SFC on 8 May 2007, as updated from time to time.



92. Given that the receipt of monetary and/or non-monetary benefits from other parties in itself could undermine independence, we therefore propose, as the first limb, to restrict representation by an intermediary as being “independent” or using any other term(s) with similar inference (eg, “independent financial advisers”, “IFA”, “impartial”, “neutral”, “objective”, or “unbiased”) if monetary or non-monetary benefits from other parties including product issuers are received. In addition to the existing disclosure requirement for the monetary and non-monetary benefits receivable from other parties, including product issuers, the intermediary would also be required to provide clear disclosure²² to investors prior to or at the point of transaction on whether or not it is independent and the bases for such determination. At a minimum, a one-off disclosure is acceptable but intermediaries must inform clients of any changes.
93. In terms of what amounts to “independence”, it is proposed that when distributing an investment product, a licensed or registered person would generally not be regarded as independent if it receives fees, commissions, or any monetary or non-monetary benefits paid or provided (whether directly or indirectly) by any party in relation to such distribution of the investment product to clients or if it has any links or other legal or economic relationships with product issuers which are likely to impair its independence in respect of favouring a particular investment product, a class of investment products or a product issuer.
94. Hence, where an intermediary represents itself as being “independent”, or uses other terms with similar inference, it cannot receive fees, commissions, or any monetary or non-monetary benefits paid or provided (whether directly or indirectly) by any party in the distribution of an investment product to clients.

(2) Enhancing disclosure

95. As the second limb, we also propose to enhance the disclosure requirement in relation to monetary benefits received or receivable that are not quantifiable prior to or at the point of entering into a transaction (for example, trailer fees) to enable investors to make a more informed decision. Increased transparency would make it easier for investors to identify the fees receivable by different intermediaries, thus making it easier to detect potential instances of conflicts. The proposal can also facilitate easy comparison of fees received by different intermediaries. We hope this increased transparency not only encourages investors to seek quality advice or services from intermediaries but also facilitates competition and drives down fees in the long run.
96. To enhance transparency, it is proposed that, in addition to disclosing the existence and nature of monetary benefits received or receivable that are not quantifiable prior to or at the point of entering into a transaction, an intermediary is required to disclose (i) the range of such monetary benefits receivable on an annualised basis and (ii) the maximum dollar amount of such monetary benefits receivable per year.
97. Set out below is a sample disclosure for proposal (i) and (ii) above using trailer fees as an example:

²² The disclosure should be made in the form of a statement as specified in the newly-added Schedule 9 to the Code of Conduct and contain the substance set out therein.



Name of Fund	Ongoing commission / monetary benefits from product issuer
Fund A	<p>We will receive from the fund manager as ongoing commission 40% - 60% of Fund A's annual management fees.</p> <p>This means that if you invest HK\$10,000 in Fund A, we will receive up to HK\$x* out of the annual management fees every year throughout the term of your investment.</p> <p>*HK\$x is based on the assumption that you remain invested in Fund A for a 12-month period, and that there is no change in the net asset value per unit of Fund A such that the value of your HK\$10,000 investment remains unchanged throughout the period.</p>

98. Under this proposal, the intermediary would be required to provide a range to give potential investors information on how much of the management fees are paid to the intermediary. In providing the range of such monetary benefits, intermediaries should ensure that the range reasonably reflects the terms of any agreement with the party providing such monetary benefits (eg, the range of trailer fees should be based on the range as agreed with the product issuer in the relevant distribution agreement). The intermediary would also be required to disclose a maximum dollar amount to give potential investors an idea of how much fees in dollar terms are paid to the intermediary per year. In the context of trailer fees in respect of funds, the maximum dollar amount would be calculated based on the simple assumption that the investor will remain invested in the fund for a 12-month period and that there will be no change in the net asset value (NAV) per unit in the fund throughout that period to remove any market impact. This can serve to standardise the calculation across the industry.
99. The obligation to disclose such information in respect of all applicable investment products lies with intermediaries prior to or at the point of entering into a transaction, and the disclosure is to be made on a transaction basis.
100. In formulating this proposal, we have considered various alternatives on how monetary benefits receivable by intermediaries, largely trailer fees in the context of funds, should be disclosed.
101. During our soft consultation process, many industry participants pointed out that the trailer fee calculation mechanism varies across different fund houses and different distributors and even across different fund types. The calculation is typically based on the total amount of assets managed by the fund manager for the intermediaries' clients during or at the end of the calculation period on a fund / fund house basis. The percentage of fees receivable may also vary depending on the type of funds involved. Hence, the calculation of trailer fees is complex and difficult. Many industry participants also expressed concerns about the commercial sensitivity involved in the disclosure of trailer fees. On balance, and taking into account the industry feedback, the SFC has come up with the current proposal.
102. We will work with the Investor Education Centre, the SFC's wholly-owned subsidiary, on additional educational materials to enhance investors' understanding of these disclosures and how to interpret these numbers.

**Questions:**

17. What is your view on a pay-for-advice model for Hong Kong? Do you have any comments on our suggested approach to addressing the inherent conflicts of interest arising from receipt of commissions by intermediaries from other parties including product issuers?
18. Do you have any comments on the proposed disclosure requirement in relation to independence set out above?
19. Do you have any comments on the enhanced disclosure proposed with regard to monetary benefits received or receivable by intermediaries that are not quantifiable prior to or at the point of entering into a transaction (and in particular, in relation to specific types of investment products)?
20. Do you have any comments on the suggested manner of disclosure of trailer fees (in the context of funds) set out in the sample disclosure above? Do you have any other suggestions to ensure the disclosure of non-quantifiable monetary benefits relating to other types of investment products will be clear, fair, meaningful and easily understood by investors?
21. Do you think a 6-month transition period following gazettal of the final form of the amendments to the Code of Conduct is appropriate? If not, what do you think would be an appropriate transition period and please set out your reasons.

Other amendments

103. In line with the policy objective of updating and enhancing our regulations on asset management to clarify our policy intent and better reflect the regulatory position in practice, amendments will be made to the Code of Conduct to make it clear that the Code of Conduct and its general principles will be applicable to all Fund Managers.

Section 2**Other matters considered but not included in our proposals**

104. We are conscious that there are developments overseas in other areas relating to asset management regulations which are not covered in the proposals put forward in this paper.
105. One such area is remuneration in the context of the alignment of incentives between fund managers and fund investors. We understand that there are various remuneration rules being put in place in Europe to ensure remuneration should not result in excessive risk taking and should not impair clients' interests. In this connection, we note that there are already general principles under the existing FMCC and Code of Conduct governing best execution and conflicts of interest as well as provisions in the ICG to ensure that funds are not taking on excessive risks and there is proper management of risks which should address any mis-alignment of incentives.
106. Another area is unbundling of research from broker commissions charged to fund managers, which is currently a big theme in Europe and an evolving issue in the



international arena. Under the FMCC and Code of Conduct, soft dollars are currently permissible provided that certain requirements which are designed to address potential conflicts of interest are met. These include the requirement that the types of goods and services received are of demonstrable benefit to the clients, transaction execution is consistent with best execution standards, client's consent has been obtained and requisite disclosure has been made. Further, there are already general principles under the existing FMCC and Code of Conduct governing best execution and conflicts of interest.

107. Given that our existing requirements applicable to these two areas meet the relevant IOSCO standards and it also appears that a consensus has not yet been reached in the international arena on these subjects, we will continue to keep in view FSB and IOSCO requirements and other global regulatory developments on these subjects.
108. In formulating the scope of the proposals covered in the present exercise, we are particularly mindful that different considerations may apply in different markets and there is no "one size fits all" approach. Local market characteristics, such as market structure and investors' characteristics and behaviour, must be taken into account when deliberating appropriate regulations.
109. The SFC will continue to keep in view international regulatory developments in these areas and review our regulations where appropriate.

Seeking comments

110. The SFC welcomes any comments from the public and the industry on the proposals made in this consultation paper and the indicative draft of the proposed amendments to the FMCC in Appendix A and the Code of Conduct in Appendix B to this consultation paper. Please submit comments to the SFC in writing no later than 22 February 2017.



Appendix A

Proposed amendments to the Fund Manager Code of Conduct



FUND MANAGER CODE OF CONDUCT

~~Second~~ Third Edition
pursuant to the Securities and Futures Ordinance (Cap. 571)

~~January 2014~~ [● 2017]

Securities and Futures Commission
Hong Kong



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FUND MANAGER CODE OF CONDUCT

HONG KONG

INTRODUCTION

Persons to whom this Code applies

This Code sets out conduct requirements for persons licensed by or registered with the Securities and Futures Commission (SFC) whose business involves the ~~discretionary~~ management of collective investment schemes (whether ~~authorised~~ authorized or ~~unauthorised~~ unauthorized) and/or discretionary accounts (in the form of an investment mandate or pre-defined model portfolio) (Fund Managers). The particular Code requirements that are not applicable to and additional requirements that are applicable to licensed or registered persons conducting discretionary accounts management are set out in Appendix 1.

~~These guidelines apply~~ This Code applies to all licensed or registered persons acting as Fund Managers, including, as appropriate, their representatives. To the extent that a Fund Manager is not responsible for the overall operation of a fund, or has no de facto control of the oversight or operation of the fund, certain requirements (as specifically set out in this Code) are not applicable.

For the avoidance of doubt, all licensed or registered persons should also comply with the requirements set out in other applicable codes and guidelines in force from time to time, including the Code of Conduct for Persons Licensed by or Registered with the SFC (Code of Conduct) and the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the SFC (Internal Control Guidelines). In particular, a Fund Manager managing SFC-authorized collective investment schemes is required to comply with the relevant requirements under the SFC Handbook for Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Products in force from time to time.

Interpretation

For the purposes of this Code, a registered person means a “registered institution” and, except where the context otherwise requires, includes a “relevant individual” as defined in section 20(10) of the Banking Ordinance (Cap. 155), and “registered” shall be construed accordingly. A reference in this Code to “representatives” has the same meaning as section 167 of the Securities and Futures Ordinance (Cap. 571) (SFO).

Unless specified otherwise, a reference to a “fund” or “client” in this Code¹ is a reference to a collective investment scheme (whether authorized or unauthorized) managed by a Fund Manager and “fund investors” refers to investors as a whole of a collective investment scheme (whether authorized or unauthorized) managed by the Fund Manager.

¹ Where the licensed or registered persons are conducting discretionary accounts management, the meaning of these terms are defined separately in Appendix 1.



Where a Fund Manager is a delegate of another fund manager for the management of a portfolio within a fund, a reference to its “client” in this Code is a reference to the delegating fund manager, and a reference to “fund” in this Code is a reference to the portfolio managed by the delegated Fund Manager.

Purpose of this Code

This Code aims, firstly, to supplement codes and guidelines applicable to all categories of licensed or registered person, including, for the avoidance of doubt, the Code of Conduct (including the General Principles set out therein), with guidance in respect of the minimum standards of conduct specifically applicable to Fund Managers. It does not replace any legislative provisions, codes or guidelines issued by the SFC. Secondly, it highlights certain existing requirements applicable to Fund Managers. Further reference should however be made to the legislation, other applicable codes and guidelines, and, in the case of any inconsistency, the more stringent applicable provision will be applied. This Code does not have the force of law and should not be interpreted in a way that would override the provisions of any law.

Effect of breach of this Code

Breach of any of the requirements of this Code will, in the absence of extenuating circumstances, reflect adversely on the fitness and properness of a Fund Manager and may result in disciplinary action. **When considering a person’s failure to comply with this Code, SFC staff will adopt a pragmatic approach taking into account all relevant circumstances, including the size of the ~~corporation~~ Fund Manager, and any compensatory measures implemented by its senior management.**



I. ORGANISATION AND STRUCTURE

1. Organisation and Management Structure

Incorporation and Registration

- 1.1 A Fund Manager should ensure that its business is properly incorporated and that any person it employs or appoints to conduct business is properly licensed or registered in accordance with all applicable statutory requirements.

Organisation and Resources

- 1.2 A Fund Manager should maintain:

- (a) financial resources in accordance with all applicable statutory requirements;
- (b) sufficient human and technical resources and experience for the proper performance of its duties. This would be expected to vary depending on the amount of assets under management by the ~~corporation~~ Fund Manager, and the type and nature of the assets and markets in which the ~~corporation invests funds managed by the Fund Manager invest~~. The functions of within the corporation Fund Manager, including fund management, operations, compliance, risk management, valuation and audit, should only be performed by qualified and experienced persons, who should receive appropriate training on an ongoing basis;
- (c) satisfactory internal controls and written compliance procedures which address all applicable legal and regulatory requirements;
- (d) satisfactory risk management governance structure and procedures commensurate with the size, complexity and risk profile of the firm and the investment strategy adopted by each of the funds under its business management; and
- (e) adequate professional indemnity insurance cover commensurate with its business.

Functional Separation

- 1.3 Where a Fund Manager is itself undertaking or is part of a group of companies which undertake other financial activities such as advising on corporate finance, banking or broking, it should ensure there is an effective system of functional barriers (Chinese Walls) in place to prevent the flow of information that may be confidential and/or price sensitive between the different areas of operations. There should be physical separation between the activities and the different persons it employs or appoints to conduct business unless this is impossible given the size of the ~~corporation~~ Fund Manager, together with written procedures to document the controls. If physical separation is impossible, the ~~corporation~~ Fund Manager should prohibit dealing in price sensitive or confidential information.



Segregation of Duties

- 1.4 A Fund Manager should ensure that key duties and functions are appropriately segregated, unless this is impossible given the size of the ~~corporation~~ Fund Manager. In particular:
- (a) front office functions (which include making investment decisions, marketing and dealing in ~~collective investment schemes~~ funds, and placing orders to deal with brokers) should be physically segregated from back office functions (which include receiving broker confirmations, settling trades, accounting and reconciliation, ~~valuing client portfolios~~ valuation and reporting to clients funds and their investors) and should be carried out by different staff with separate reporting lines;
 - (b) compliance and audit functions should, if possible, be separated from each other, and have separate reporting lines from other functions; and
 - (c) the investment decision making process should be clearly delineated from the dealing process.

Note: A central dealing function is encouraged but is not mandatory.

Conflicts of interest

- 1.5 A Fund Manager should maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to identify, prevent, manage and monitor any actual or potential conflicts of interest, including conducting all transactions in good faith at arm's length and in the best interests of the fund on normal commercial terms. In particular, where such a conflict cannot be avoided, and provided that funds' interests can be sufficiently protected, the conflicts should be managed and minimised by appropriate safeguards and measures to ensure fair treatment of fund investors, and any material interest or conflict should properly be disclosed to fund investors.

Responsibilities of Management

"Senior management" means the Managing Director of a ~~corporation~~ Fund Manager or its Board of Directors, Chief Executive Officer or other senior operating management personnel in a position of authority over the ~~corporation's~~ Fund Manager's business decisions.

- 1.56 The senior management of a Fund Manager should:
- (a) be principally responsible for compliance by the Fund Manager with all relevant legal and regulatory requirements ~~under this Code~~, as well as the nurturing of a good compliance culture within the ~~corporation~~ Fund Manager;
 - (b) maintain clear reporting lines with supervisory and reporting responsibilities assigned to qualified and experienced persons;



- (c) ensure that all persons performing functions on behalf of the ~~corporation~~ Fund Manager are provided adequate and up-to-date information about the ~~corporation's~~ Fund Manager's policies and procedures applicable to them; and
- (d) ensure that the performance of Fund Managers in managing ~~client accounts funds (whether authorized or unauthorized)~~ is reviewed, on at least an annual basis annually.

Risk Management

- 1.7.1 The Fund Manager should establish and maintain effective policies and procedures as well as a designated risk management function to identify and quantify the risks, whether financial or otherwise, to which the Fund Manager and, if applicable, the funds are exposed. The Fund Manager should take appropriate and timely action to contain and otherwise adequately manage such risks.
- 1.7.2 The Fund Manager should refer to and comply with the relevant provisions under the Internal Control Guidelines.
- 1.7.3 A Fund Manager should review the risk management policies and procedures with appropriate frequency and enhance such policies and procedures whenever necessary.

Compliance

- 1.68.1 A Fund Manager should:
 - (a) maintain an effective compliance function, including a ~~Designated Compliance Officer~~ compliance officer, within the ~~corporation~~ Fund Manager to ensure that the ~~corporation~~ Fund Manager complies with its own internal policies and procedures, and with all applicable legal and regulatory requirements, including this Code; and
 - (b) ensure that the compliance function possesses the technical competence and experience necessary for the performance of its functions.
- 1.68.2 The compliance function and ~~Designated Compliance Officer~~ the compliance officer should be independent of other functions and report directly to the ~~corporation's~~ Fund Manager's senior management, unless this is impossible given the size of the ~~corporation~~ Fund Manager. Where there is no separation of functions, the ~~corporation's~~ Fund Manager's senior management should assume the role of ~~Designated Compliance Officer~~ compliance officer. Compliance activities may be delegated to an appropriately qualified professional, although the responsibility and obligations may not be delegated.
- 1.68.3 ~~The Designated Compliance Officer~~ There should maintain be sufficiently detailed compliance procedures to ~~give~~ enable senior management ~~reasonable assurance that the corporation complies~~ to comply with all applicable requirements at all times.



Audit

- 1.79 Where practicable, a Fund Manager should maintain an independent and objective audit function to report on the adequacy, effectiveness and efficiency of the ~~corporation's~~ Fund Manager's management, operations and internal controls. The audit function should:
- (a) where practicable, be free from operating responsibilities, with a direct line of communication to senior management or the audit committee, as applicable;
 - (b) follow clearly defined terms of reference (including monitoring the timeliness and accuracy of other functions) which set out the scope, objectives, approach and reporting requirements;
 - (c) adequately plan, control and record all audit work performed, and record the findings, conclusions and recommendations; and
 - (d) report to senior management on all matters highlighted in the audit report, which should be resolved satisfactorily and in a timely manner.

Where the size of the ~~corporation~~ Fund Manager does not justify a separate internal audit function, the relevant roles and responsibilities should be performed or reviewed by ~~the~~ external auditors.

Delegation

- 1.810 A Fund Manager should exercise due skill, care and diligence in the selection and appointment of third-party delegates. Where functions are delegated to third parties, there should be ongoing monitoring of the competence of delegates, to ensure that the principles of this Code are followed. Although the investment management role of the ~~corporation~~ Fund Manager may be sub-contracted, the responsibilities and obligations of the ~~corporation~~ Fund Manager to its clients the funds it manages may not be delegated.

Withdrawal from Business

- 1.911 A Fund Manager who withdraws from business should ensure that any affected clients are promptly notified and that proper arrangements remain in place for the safekeeping of client assets. Where a ~~corporation~~ Fund Manager is being wound up, it should comply with all the applicable statutory requirements.

2. Staff Ethics

Personal Account Dealing

Note: The following guidelines are intended to address the basic principles that persons engaged in fund management business, when transacting for themselves, must give ~~their clients~~ the funds managed by the Fund Manager priority and avoid conflicts of interest. In the context of these guidelines, "relevant persons" means any employees or



directors of a Fund Manager or persons accredited to a Fund Manager for conducting regulated activities:

- *who in their regular functions or duties make or participate in investment decisions, or obtain information, prior to buying or selling investments on behalf of a client fund; and/or*
- *whose functions relate to the making of any recommendations with respect to such buying or selling;*

or any persons over whom they exercise control and influence.

As a minimum, these guidelines cover trading in ~~shares~~ securities and derivatives. Beyond this, however, the scope of investments that should be covered is not defined, as this may vary depending on the business of the ~~corporation~~ Fund Manager and the underlying investments of the funds managed by the Fund Manager. A Fund Manager is expected to define the types of investment intended to be covered, and to respect the principles outlined here.

2.1.1 A Fund Manager should ensure that it has internal rules or provisions in its contracts of employment ~~for~~ or other agreements with the relevant persons as follows:

- (a) that relevant persons are required to disclose existing holdings upon joining a Fund Manager and at least semi-annually thereafter;
- (b) that relevant persons are required to obtain prior written permission for personal account dealing from the ~~Designated Compliance Officer~~ compliance officer or other person designated by senior management. The permission should be valid for no more than ~~5~~ five trading days, and be subject to the following constraints:
 - (i) that relevant persons may not buy or sell an investment on a day in which the Fund Manager has a pending “buy” or “sell” order in the same investment until that order is executed or withdrawn;
 - (ii) that relevant persons may not buy or sell an investment for their personal account within ~~4~~ one trading day before (if the relevant person is aware of a forthcoming client fund transaction) or after trading in that investment on behalf of a client fund;
 - (iii) that relevant persons may not buy or sell an investment for their personal account within ~~4~~ one trading day before (if the relevant person is aware of a forthcoming recommendation) or after a recommendation on that investment is made or proposed by the Fund Manager;

Note: Subject to rules being set down by the ~~Designated Compliance Officer~~ senior management, the restrictions in (ii) and (iii) above need not be applied where client fund orders have been fully executed and any conflicts of interest have been removed.



- (iv) that cross trades between relevant persons and ~~clients~~ funds be prohibited;
 - (v) that short-selling of any securities recommended by the Fund Manager for purchase be prohibited; and
 - (vi) that relevant persons should be prohibited from participating in initial public ~~offers~~ offering available to ~~clients of~~ funds managed by the Fund Manager or its connected persons, and should not use their positions to gain access to ~~IPO's~~ initial public offerings for themselves or any other person;
- (c) that relevant persons are required to hold all personal investments for at least 30 days, unless prior written approval of the ~~Designated Compliance Officer~~ compliance officer or other persons designated by senior management is given for an earlier disposal; and
- (d) that relevant persons are required, either:
- (i) to hold their personal accounts with the Fund Manager or a connected person and place all deals through that corporation; or
 - (ii) obtain approval from the ~~Designated Compliance Officer~~ compliance officer or other persons designated by senior management for outside broking accounts, and ensure that copies of records and statements of personal transactions entered into by them are submitted to the ~~Designated Compliance Officer~~ compliance officer or other persons designated by senior management within a defined timeframe.

2.1.2 A Fund Manager should maintain appropriate procedures to distinguish personal transactions for relevant persons from other transactions, and to ensure that such transactions are properly approved and there is an adequate audit trail of such approval and the transaction [see 5.1(a)].

2.1.3 A Fund Manager should not permit relevant persons to delay settlement of personal transactions beyond the normal settlement time for the relevant market.

2.1.4 A Fund Manager ~~who is a relevant person~~ should ~~comply~~ maintain appropriate procedures to ensure compliance with the provisions set out in 2.1.1 (a) to (d) above by all its relevant persons.

Receipt or Provision of Benefits

2.2 A Fund Manager:

- (a) should not offer or accept any inducement ~~in connection with the affairs or business of a client~~ which is likely to ~~significantly~~ materially conflict with the duties owed to clients;



- (b) in the case of a corporation, should maintain:
 - (i) written guidelines, including monetary limits, ~~about for the offer and acceptance by,~~ staff members and persons accredited to it for conducting regulated activities, of gifts, rebates or other benefits ~~received from clients or business contacts,~~ to give effect to (a); and
 - (ii) a register of benefits received above the specified limit.

II. FUND MANAGEMENT

3. Fund Management

Investment within ~~Client~~ Mandate

- 3.1 A Fund Manager should ensure that transactions carried out on behalf of ~~a client~~ each fund are in accordance with the ~~portfolio's~~ fund's stated investment strategy, objectives, investment restrictions and guidelines, whether in terms of asset class, geographical spread or risk profile, as set out in the respective constitutive and/or relevant documents of the funds managed by the Fund Manager. In this connection, a Fund Manager should have in place effective and properly-implemented procedures and controls.

Best Execution

- 3.2 A Fund Manager should ~~execute client~~ ensure that fund orders are executed on the best available terms, taking into account the relevant market at the time for transactions of the kind and size concerned.

Prohibition on Insider Dealing

- 3.3 A Fund Manager should establish and maintain policies and procedures to prohibit and prevent market misconduct, including, but not limited to, insider dealing and market manipulation. In particular, it should not effect or cause to be effected any transaction based on confidential price sensitive information or when otherwise prohibited from dealing by statutory restrictions on insider dealing, and should have procedures in place to ensure that staff are aware of such restrictions.

Order Allocation

- 3.4 A Fund Manager should:
 - (a) ensure that all client orders are allocated fairly;
 - (b) make a record of the intended basis of allocation before a transaction is effected; and
 - (c) ensure that an executed transaction is allocated promptly in accordance with the stated intention, except where the revised allocation does not disadvantage a client and the reasons for the re-allocation are clearly documented.



Fund Portfolio Turnover

- 3.5 A Fund Manager should ~~not trade excessively on behalf of the client portfolio, taking~~ take into account the ~~portfolio's~~ fund's stated objectives and not trade excessively on behalf of a fund.

Underwriting

- 3.6 Unless specifically permitted in the ~~Client Agreement or client~~ fund mandate, a Fund Manager should not participate in underwriting activities on behalf of a ~~client~~ fund. Where underwriting is undertaken on behalf of a ~~client~~ fund, all commissions and fees received under such contract should be credited to the ~~client~~ fund account.

Participation in Initial Public ~~Offers~~ Offerings

- 3.7 Where a Fund Manager participates in an initial public offering on behalf of ~~clients~~ funds managed by it, it should ensure that:
- (a) the allocation of stock received in the offering provides for a fair and equitable allocation amongst clients;
 - (b) preferential allocations are prohibited; and
 - (c) ~~the reasons for all allocations are documented~~ records of (i) the intended basis of allocation before a transaction is effected and (ii) the actual allocation after the transaction is effected, are made.

Transactions with Connected Persons

- 3.8.1 A Fund Manager should not carry out any transaction on behalf of a ~~client~~ fund with a ~~corporation~~ party which is a connected person unless such transaction is carried out on arm's length terms, consistent with best execution standards, and at a commission rate no higher than customary institutional rates. ~~In the case of an authorised collective investment scheme, total transactions with connected persons should not exceed 50% of the scheme's transactions in value in any one financial year of the scheme, except with the approval of the SFC.~~
- 3.98.2 A Fund Manager should not, on behalf of a fund, deposit funds with or borrow funds ~~on behalf of a client with~~ from a connected person unless:
- (a) in the case of a deposit, interest is received at a rate not lower than the prevailing commercial rate for a deposit of that size and term; and
 - (b) in the case of a loan, interest charged and fees levied in connection with the loan are no higher than the prevailing commercial rate for a similar loan.



Cross Trades

For the avoidance of doubt, a reference to “client” in this sub-section also includes a reference to the investors of discretionary accounts managed by the same Fund Manager.

3.409.1 A Fund Manager should only undertake sale and purchase transactions between client accounts (cross trades) where:

- (a) the sale and purchase decisions are in the best interests of both clients and fall within the investment objective, restrictions and policies of both clients;
- (b) the trades are executed on arm’s length terms at current market value;
- (c) the reasons for such trades is are documented prior to execution; and
- (d) such ~~activity is~~ activities are disclosed to ~~the~~ both clients.

3.409.2 Cross trades between house accounts and client accounts should only be permitted with the prior written consent of the client, to whom any actual or potential conflicts of interest should be disclosed. Cross trades between staff personal accounts and client accounts should be prohibited.

House Accounts

“House account” means an account owned by a Fund Manager or any of its connected persons over which it can exercise control and influence.

For the avoidance of doubt, a reference to “client” in this sub-section also includes a reference to the investors of discretionary accounts managed by the same Fund Manager.

3.4110 When dealing for a house account, a Fund Manager should:

- (a) give priority to satisfying a client order. Where a client order has been aggregated with another order, the client’s order must take priority in any subsequent allocation if all orders cannot be filled. Aggregation of house orders with client orders should only be made if it is in the best interests of clients;
- (b) not deal in accordance with a recommendation, research or analysis to be published to clients until the clients have had a reasonable opportunity to act on the information; and
- (c) except with the prior written consent of the ~~Designated Compliance Officer~~ compliance officer or other persons designated by senior management, not deal ahead of any transaction to be carried out on behalf of a client, ~~or, where the house account and a client have invested in the same investment, only dispose of its holdings following, or together with, the disposal of holdings on behalf of a client fund.~~ The ~~Designated Compliance Officer~~ compliance officer or other



persons designated by senior management should properly document the reasons for any consents given.

Note: For the avoidance of doubt, a reference to “dealing” in this sub-section includes any acquisition or disposal of securities.

Risk Management

3.11.1 For risk management at the fund level, a Fund Manager should implement adequate risk management procedures (including risk measurements and reporting methodologies) in order to identify, measure, manage and monitor appropriately all risks:

- (a) relevant to each investment strategy; and
- (b) to which each fund is or may be exposed, such as market, liquidity and counterparty risks, and other risks, including operational risks, which may be material for each fund it manages taking into account the nature, scale and complexity of its business and of the investment strategy of each of the funds it manages.

Note:

Where appropriate, measures to manage risks of a fund may include:

- (a) identifying and managing potential risks of a fund throughout the fund life cycle;
- (b) ensuring that the risk profile of the fund is consistent with the nature, size, portfolio structure and investment strategies, restrictions and objectives of the fund as provided and represented to fund investors in the constitutive and/or relevant documents; and
- (c) ensuring ongoing and proper identification, measurement, management and monitoring of risks associated with each investment of the fund and their overall effects on the fund’s portfolio (including via the use of suitable stress testing procedures).

3.11.2 A Fund Manager should take into account, where applicable, the suggested risk-management control techniques and procedures for funds set out in Appendix 2 to this Code in monitoring such risks.

Leverage

3.12 Where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should disclose (i) the maximum level of leverage which it may employ on behalf of each fund it manages and (ii) the basis of calculation of leverage which should be reasonable and prudent, having due regard to international best practices. At a minimum, such information should be disclosed in the fund’s offering document.



Securities Lending

Paragraphs 3.13.1 to 3.13.8 (inclusive) of this sub-section are applicable to Fund Managers that engage in securities lending, repurchase agreements (repos) and similar over-the-counter transactions on behalf of the funds managed by them.

3.13.1 The Fund Manager should put in place a collateral valuation and management policy and a cash collateral reinvestment policy governing securities lending, repo or similar over-the-counter transactions and any cash collateral reinvestments in respect of collateral received by the funds managed by the Fund Manager.

3.13.2 The collateral valuation and management policy should require that:

- (a) collateral and lent securities are marked to market daily wherever and whenever practicable; and
- (b) variation margin is collected at least daily where amounts exceed a minimum acceptable threshold appropriate to the counterparty risk posed as determined by the Fund Manager.

Note: As part of its collateral valuation and management policy, a Fund Manager is generally expected to accept collateral types that it is able, following a counterparty failure, to:

- (a) hold for a period without breaching applicable laws or regulations or the relevant mandate;
- (b) value; and
- (c) risk manage appropriately.

The collateral valuation and management policy should include contingency plans to cover how collateral should be managed following default situations (in particular, the default of the largest market counterparty to securities lending, repo and similar over-the-counter transactions of a fund) and the capabilities to liquidate collateral in an orderly way.

3.13.3 A Fund Manager should have in place an eligible collateral and haircut policy in determining the types of acceptable collateral and their corresponding haircut in connection with non-centrally cleared over-the-counter and securities financing transactions (such as securities lending, repo and similar over-the-counter transactions).

3.13.4 A Fund Manager should also have in place a properly designed methodology to calculate haircuts on the collateral received in connection with securities lending, repo and similar over-the-counter transactions of its funds. The Fund Manager should establish appropriate policies, procedures, and internal controls to ensure that haircuts are set in accordance with the methodology and are consistently applied when conducting such transactions on behalf of a fund.



3.13.5 The cash collateral reinvestment policy should ensure that assets held in the cash collateral reinvestment portfolio are sufficiently liquid with transparent pricing and low risk to meet reasonably foreseeable recalls of cash collateral, and measures are in place to manage the associated liquidity risk. A Fund Manager who reinvests cash collateral received by the funds should formally document and regularly review the cash collateral reinvestment policy and communicate such policy to fund investors.

Note: In designing its cash collateral reinvestment policy, a Fund Manager should consider setting specific requirements for the cash collateral reinvestment portfolio and/or liquidity pool maintained to meet cash collateral recalls, including:

(a) requiring a minimum portion of the cash collateral to be kept in short-term deposits, held in highly liquid short-term assets, or invested in short tenor transactions; and

(b) setting specific limits for the weighted average maturity and/or weighted average life.

3.13.6 A Fund Manager of a fund which is the securities lender should stress test the ability of a cash collateral reinvestment portfolio to meet foreseeable and unexpected calls for the return of cash collateral on an ongoing basis. Stress tests should include an assessment of the ability to liquidate part of the entire reinvestment portfolio under a range of stressed market scenarios.

3.13.7 A Fund Manager should provide information on a fund's securities lending, repo and similar over-the-counter transactions to clients (and, where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the fund's oversight and operations), to fund investors) at least on an annual basis and upon request.

3.13.8 Where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should disclose a summary of the securities lending, repo and similar over-the-counter transactions policy and the risk management policy in the fund's offering document.

Liquidity Management

Paragraphs 3.14.1 to 3.14.3 (inclusive) of this sub-section, except for 3.14.1(b) and 3.14.1(c), are applicable to a Fund Manager that is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund).

3.14.1 A Fund Manager should:

- (a) maintain and implement effective liquidity management policies and procedures to monitor the liquidity risk of the fund, taking into account the investment strategy, liquidity profile, underlying obligations, and redemption policy of the fund;
- (b) integrate liquidity management in investment decisions;
- (c) regularly assess the liquidity of the assets of a fund;



- (d) regularly conduct assessments of liquidity in different scenarios, including stressed situations, to assess and monitor the liquidity risk of the funds accordingly; and
- (e) disclose in the fund's offering document the liquidity risks involved in investing in the fund, and explanation of any tools or exceptional measure that could affect redemption rights.

Note: The extent of application of these liquidity management principles will depend on the nature, liquidity profile and asset-liability management of the fund. A Fund Manager should consider which principles are relevant to the fund it manages. The obligation to assess and make disclosure regarding the liability side of a fund applies only to the Fund Manager in charge of overall operation of the fund (or has de facto control of the oversight or operation of the fund).

3.14.2 Where the constitutive documents of a fund allow the use of specific tools or exceptional measures which could affect redemption rights, a Fund Manager should consider the appropriateness of using such tools and exceptional measures, taking into account the nature of assets held by the fund and its investor base.

Note:

Protecting the interests of fund investors should be the primary consideration in the use of liquidity risk management tools. A Fund Manager should also ensure that the investment strategy and portfolio profile of a fund are consistently maintained as much as possible when using these tools.

Where side letters have been entered into, a Fund Manager should disclose such fact and the material terms in relation to redemption in the side letters to all potential and existing fund investors.

3.14.3 A Fund Manager should conduct periodic reviews of the effectiveness of its liquidity management policies and procedures and such policies and procedures should be updated as appropriate.

Compliance

3.15 A Fund Manager should ensure that all material non-compliance matters are identified, rectified and reported to the SFC and any other relevant regulators on a timely basis, where appropriate.

Termination

Paragraphs 3.16.1 to 3.16.2 (inclusive) of this sub-section are applicable to a Fund Manager that is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund).

3.16.1 A Fund Manager's decision to terminate a fund should take due account of the best interests of investors in the fund. A Fund Manager should ensure that the termination process of a fund is carried out, and fund investors are treated fairly.



3.16.2 A Fund Manager should make adequate disclosure of all relevant material information in relation to the termination of the fund to all fund investors in an appropriate and timely manner.

Note: Such information should include without limitation termination decisions, implementation plans and material change of circumstances arising during the termination process.

4. Custody

Safety of ~~Client~~ Fund Assets

4.1.1 A Fund Manager should ensure that the fund assets entrusted to it are properly safeguarded. If the Fund Manager is responsible for making custody arrangements this means: In this connection, a Fund Manager should ensure that fund assets are segregated from the assets of the Fund Manager, and, unless held in an omnibus client account, assets of its affiliates and other clients.

Note: Where fund assets are held in an omnibus client account, the Fund Manager should ensure that adequate safeguards are put in place such that fund assets belonging to each client are appropriately recorded with frequent and appropriate reconciliations being performed.

4.1.2 Where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should arrange for the appointment of, and entrust the fund assets to, a custodian that is functionally independent from it. Where self-custody is adopted, the Fund Manager should ensure that it has policies, procedures, and internal controls in place to ensure that the persons fulfilling the custodial function are functionally independent from the persons fulfilling the fund's management or administration functions.

Note: In the case of self-custody, the Fund Manager should comply with, where applicable, all relevant requirements under the SFO, including the Securities and Futures (Client Money) Rules and the Securities and Futures (Client Securities) Rules.

Appointment of Custodian

(a) ~~if permitted by the terms of its license, it may retain the responsibility for safekeeping in a segregated trust account; or~~

(b) ~~it should arrange for the appointment of a custodian (see below), taking~~

4.2.1 Where the Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), a Fund Manager should exercise due skill, care and diligence in the selection, appointment and ongoing monitoring of the custodian and take all reasonable steps to ensure that the custodian is properly qualified for the performance of its functions. On an ongoing basis, a Fund Manager should satisfy itself as to the continued suitability and financial standing of any appointed custodian.



Note: In considering whether a custodian is properly qualified for the performance of its functions, the Fund Manager should consider the following as part of the selection process for custodians:

- (a) whether the custodian has appropriate segregation arrangements in place such that the fund assets are segregated from
 - (i) the assets of the custodian / sub-custodian throughout the custody chain; and
 - (ii) the assets of other funds and other clients of the custodian throughout the custody chain (unless the fund assets are held in an omnibus client account, in which case the principles set out in the note to paragraph 4.1.1 should apply);
- (b) the custodian's legal and regulatory status (i.e. authorization to undertake custody business);
- (c) the custodian's financial resources (i.e. the custodian's financial capacity to safekeep the fund assets and the custodian's credit worthiness);
- (d) the custodian's management of potential conflicts of interest;
- (e) the custodian's organisational capabilities; and
- (f) where appointment of sub-custodians is allowed, the custodian would use due skill, care and diligence in the selection and monitoring of its sub-custodians.

Appointment of Custodian

4.2.2 A custodian appointed by a Fund Manager should be ~~either~~ any of the following:

- (a) a registered trust company;
- (b) an ~~authorised~~ authorized financial institution (including a licensed bank, deposit-taking company or restricted-license bank) or the subsidiary of a licensed bank;
- (c) a banking institution or trust company outside Hong Kong that is subject to prudential supervision; or
- (d) any other appropriately qualified institution appointed with the prior written consent of the client.

Custody Agreement

Paragraphs 4.3.1 to 4.3.3 (inclusive) of this sub-section are applicable to a Fund Manager that is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund).



4.3.1 The Fund Manager should ensure that a formal custody agreement is entered into with the custodian appointed for custody of a fund's assets.

4.3.2 The Fund Manager should formulate custody arrangements with due skill, care and diligence and clarify the duties and responsibilities of the various parties to the custodial arrangements. In particular, the Fund Manager should ensure that the custody agreement contains provisions to specify the scope of the responsibility and liability of the custodian.

4.3.3 The Fund Manager should monitor custody arrangements on an ongoing basis to ensure the custodian's compliance with the terms of the custody agreement.

Disclosure of Custody Arrangements

4.4.1 Where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should ensure that the custody arrangements in respect of assets of the fund and any material risks associated with the arrangements are properly disclosed to the fund investors and that fund investors are updated about any significant changes.

4.4.2 Where the Fund Manager retains custody of fund assets, the Fund Manager should also specifically disclose the existence of such an arrangement and the additional safeguards that have been put in place to mitigate any potential conflicts of interest.

5. Operations

Records Required to be Kept Record Keeping

- 5.1 A Fund Manager should keep its accounts and records properly and in line with all applicable statutory requirements. Proper record keeping includes:
- (a) maintaining an audit trail of all transactions effected by the Fund Manager, all information relating to client accounts produced by third parties and all relevant internal reports, by keeping all transaction records such as contract notes from third party brokers, client registers, accounting/securities ledgers, registers of securities, and records of investment processes adopted;
 - (b) maintaining appropriate procedures for the safekeeping, retrieval and storage of documents and records; and
 - (c) complying with provisions of the Securities and Futures (Keeping of Records) Rules.

Auditors and Audited Accounts

5.2.1 A Fund Manager should appoint ~~a firm of auditors~~ an independent auditor to perform an audit of the financial statements of the ~~corporation~~ on at least an annual basis Fund Manager. The audited accounts of the Fund Manager should be filed in accordance with



the applicable statutory requirements and be made available to clients the fund upon request.

5.2.2 Where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), the Fund Manager should ensure that an independent auditor is appointed to perform an audit of the financial statements of each of the funds it manages (whether by appointing the independent auditor or procuring the relevant fund to appoint the independent auditor) in order to make available, at a minimum, an annual report for each of the funds it manages. The annual report for each of the funds should also be made available to fund investors of the relevant funds upon request.

5.2.3 The accounting information given in the annual report for each of the funds should be prepared in accordance with generally accepted accounting principles and with the accounting rules set out in the constitutive documents of the fund.

Fund Portfolio Valuation

5.3.1 Where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) or has been delegated responsibility for fund valuation, it should ensure that, in respect of each fund it manages, appropriate policies and procedures are established so that a proper and independent valuation of the fund assets can be performed and valuation methodologies are consistently applied to the valuation of the assets across all funds managed by the Fund Manager.

5.3.2 The valuation policies and procedures should also describe the process for handling situations where the value of an asset determined in accordance with methodologies of the Fund Manager's valuation policies and procedures may not be appropriate.

Note: The valuation policies and procedures should include, and describe clearly, the process for handling exceptions, including:

- (a) requiring the Fund Manager to document the reason for any price override or deviation;*
- (b) ensuring an appropriate review of the price override or deviation by a functionally independent party; and*
- (c) describing the method for determining the appropriate price.*

5.3.3 A Fund Manager should review the valuation policies and procedures on a periodic basis to ensure their continued appropriateness and effective implementation.

5.3.4 Where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) and appoints a third party to perform valuation services, the Fund Manager should exercise due skill, care and diligence in the selection and appointment of the third party and should ensure that the third party's activities are periodically reviewed.



5.3.5 All fund assets held managed by a Fund Manager ~~on behalf of clients~~ should be valued on a regular basis ~~and the~~. The frequency of such valuations should be appropriate to the fund assets and the dealing frequency of the fund. Where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should also disclose the frequency of valuation and dealing and basis of valuation disclosed to clients fund investors.

5.3.6 Unless otherwise ~~agreed with a client~~ or specified in a ~~collective investment scheme's~~ fund's constitutive documents, a Fund Manager should have regard to applicable generally accepted accounting principles as well as best industry standards and practices in valuing fund assets and valuation should be made in accordance with the following general principles:

- (a) ~~listed securities~~ which are listed or actively traded on a market should be consistently valued at a price representative of either the ~~daily opening, mid,~~ closing price or ~~average last known market~~ price for that security at the stock exchange or market on which that security is listed or traded as indicated by an automatic price feed or other independent pricing source;
- (b) the value of unlisted or unquoted securities that are not actively traded should be ~~valued at cost price subject to adjustment~~ based on their fair value by reference to:
 - (i) comparable recent third-party transactions in ~~the same~~ similar investments, ~~taking into consideration~~ exercising professional judgement and prudence in selecting appropriate comparable transactions and in assessing the cost reasonableness of the investments resulting valuation;
 - (ii) any appraisals of the relevant investments or issuer of the investments undertaken by qualified accountants, ~~or appraisers or credit rating agencies~~. Where necessary, the Fund Manager should seek independent confirmation of the valuation from a suitably qualified person; and
 - (iii) any information generally about the relevant investments or issuer of the investments that is or becomes known to the Fund Manager from independent sources;
- (c) units or shares in collective investment schemes should be consistently valued by reference to the latest quoted price;
- (d) any listed securities which are not actively traded or have been suspended from trading (including securities which are listed or traded on a market where the market price is unrepresentative or not available) should be identified and the price at which that security is valued should be monitored. In this case, a Fund Manager should maintain procedures to:
 - (i) demonstrate that it will actively seek independent confirmation of the appropriate price for the security from suitable brokers or market makers;



- (ii) identify when such a security will be written down or written off in the valuation of a client fund account; ~~or~~ and
 - (iii) ascertain whether it will in appropriate situations transfer the security to its own account and, if so, at what price the client fund account will be compensated for the transfer; and
- (e) the value of other relevant fund assets managed by the Fund Manager should be based on their fair value by reference to the factors set out under (b) above.

5.3.7 The valuation policies and procedures and the valuation process should be periodically reviewed (at least annually) by a competent and functionally-independent party. Such party should also test the valuation procedures by which fund assets are valued. In selecting the competent and functionally-independent party, the Fund Manager should exercise due skill, care and diligence.

Side Pockets

5.4.1 Before any side pocket is introduced in a fund (i.e. where certain illiquid or hard-to-value investments of a fund as determined by the Fund Manager are segregated from other fund assets), a Fund Manager who is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) should disclose to the fund investors:

- (a) the limit to total assets to be put in the side pocket;
- (b) the overall fee structure and charging mechanism (in respect of, among others, any management and performance fees);
- (c) that the redemption lock-up period for a side pocket would be different from that of the ordinary units/shares of the fund;
- (d) how the Fund Manager defines and categorises investment products which are to be put into the side pocket and the policies and rationale for transferring investments in and out of side pockets; and
- (e) where the assets in side pockets are allowed to be transferred to another investment vehicle, the circumstances under which transfers are allowed and the pricing mechanism for such transfers.

Such Fund Manager should also disclose to the fund investors the actual amount of fees charged in relation to side-pocketed assets from time to time.

5.4.2. In setting up and managing side pockets in respect of fund assets managed by the Fund Manager, a Fund Manager should ensure that:

- (a) it has the risk management competency in managing side pockets;
- (b) it has a valuation policy covering side-pocketed assets; and



- (c) it has operational checks and controls for transferring investments in and out of side pockets;

5.4.3 Where a Fund Manager decides to side pocket any fund asset, it should arrange clear disclosure to fund investors of:

- (a) the creation of the side pocket;
- (b) the asset which has been side-pocketed; and
- (c) how the asset has been valued at the time of side pocketing and the ongoing valuation of the asset.

Net Asset Value Calculation and Pricing

Paragraphs 5.5.1 to 5.5.2 (inclusive) of this sub-section are applicable to a Fund Manager that is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund) or has been delegated responsibility for fund valuation.

5.45.1 In connection with a collective investment scheme, a Fund Manager should ensure that a valuation A Fund Manager should ensure that the net asset value calculation of different unit/share classes is carried out, in accordance with the terms set out in the constitutive documents of the scheme, to calculate accurately the net asset value of the scheme fund and the valuation policies and procedures established by the Fund Manager.

5.5.2 A Fund Manager should ensure the valuation policies and procedures in respect of each fund it manages should seek to detect, prevent and correct pricing errors and to compensate fund investors in respect of any material error. Action should also be taken to avoid further error.

Reconciliations

5.56 A Fund Manager should arrange to carry out reconciliations of the corporation's Fund Manager's internal records against those issued by third parties, e.g. clearing houses, banks, custodians, counterparties and executing brokers, to identify and rectify any errors, omissions or misplacement of assets, as follows: Reconciliations should be performed regularly (and, in any event, at least monthly) having regard to the nature of the fund assets.

- (a) reconciliations should be performed at least monthly;
- (b) reconciliations should be prepared from an asset register that is maintained and used to update client asset ledger accounts.

Disclosure of Interests

5.67 A Fund Manager should disclose all interests in securities as required by all applicable statutory requirements and have procedures in place to ensure that staff are aware of such requirements.



III. DEALING WITH CLIENTS THE FUND AND FUND INVESTORS

6. Dealing with Clients the Fund and Fund Investors

Providing Provision of Information About the Corporation

6.1 A Fund Manager should:

- (a) provide ~~clients~~ the fund and fund investors with adequate information about the ~~corporation~~ Fund Manager, including its business address, relevant conditions or restrictions under which its business is conducted, and the identity and status of persons acting on its behalf with whom the ~~client~~ fund or fund investors may have contact; and
- (b) disclose the financial condition of its business to a ~~client~~ fund upon request.

6.2 Where a Fund Manager is responsible for the overall operation of a fund (or has de facto control of the oversight or operation of the fund), it should make adequate disclosure of information (as well as any material changes to the information) on the fund which is necessary for fund investors to be able to make an informed judgment about their investment into the fund.

Confidentiality

6.2.3 A Fund Manager should maintain proper procedures to ensure confidentiality of ~~client~~ information in respect of the fund or fund investors.

Account Opening Procedures/Information About Clients

~~6.3~~ A Fund Manager should:

- ~~(a)~~ take all reasonable steps to establish:
 - ~~(i)~~ the client's full and true identity, including the identity of the actual beneficiaries, where appropriate, and verify that identification where required;
 - ~~(ii)~~ where appropriate, the client's financial situation, investment experience, and investment objectives; and
- ~~(b)~~ maintain written procedures to comply with all relevant legal and regulatory requirements against money laundering, including the SFC's Guidelines on Money Laundering.

~~Client Agreements (Discretionary Services)~~

~~6.4.1~~ A Fund Manager should ensure that a written agreement (Client Agreement) is entered into with a client before any services are provided to or transactions made on behalf of



that client. A Client Agreement should contain at least such information set out in **Appendix 1** and be provided in a language understood by the client.

6.4.2 Notwithstanding the above, in the case of a collective investment scheme:

- (a) where a Fund Manager is providing services to a collective investment scheme, a written management agreement in accordance with the rules of the collective investment scheme may be regarded as a Client Agreement;
- (b) where a Fund Manager is acting as distributor of a collective investment scheme on a non-discretionary basis, an authorised offering document and application form in accordance with the Code on Unit Trusts and Mutual Funds may be regarded as a Client Agreement.

Reporting: Periodic Statements

6.5 A Fund Manager should adhere to all relevant legal and regulatory requirements in respect of reporting, including the Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules.

Valuations and Performance Reviews

6.6 Except as agreed otherwise in writing by the client or where the portfolio is a collective investment scheme, a Fund Manager should:

- (a) review the performance of each client's account against any previously agreed benchmark, either in writing to the client or by way of meeting, at least twice a year;
- (b) provide written portfolio valuations to the client at least as regularly as provided in the Client Agreement. The report should, as a minimum, include the following:
 - (i) the date at which the report is made;
 - (ii) the contents and value of the client portfolio at that date including income received;
 - (iii) movements in the value of the client portfolio;
 - (iv) any open positions in relation to derivative transactions.

Complaints

6.74 A Fund Manager should maintain:

- (a) procedures to ensure that:



- (i) complaints from ~~clients~~ a fund or fund investors relating to ~~its business~~ the management of any fund managed by it are handled in a timely and appropriate manner;
 - (ii) steps are taken to investigate and respond promptly to a complaint by a person designated by senior management other than an individual directly concerned with the subject of the complaint; or by the ~~Designated Compliance Officer~~ compliance officer; and
 - (iii) if a complaint is not remedied promptly, the ~~client~~ fund or fund investor is advised of any further steps which may be available to the ~~client~~ fund or fund investor under the regulatory system; and
- (b) a register of complaints to give effect to (a) above. This should be reviewed by senior management on a regular basis.

7. Marketing Activities

Representations by the Fund Manager or its Representatives

- 7.1 A Fund Manager should ensure that any representations made ~~and~~ or information supplied by it to a ~~client~~ are fund or any fund investor is accurate and or not misleading.

Issue of Marketing Materials

- 7.2 A Fund Manager should ensure that all advertisements and marketing materials are ~~authorised~~ authorized as required by the SFC before issue. ~~Where such materials are not required to be authorised, a Fund Manager should nonetheless~~ and, in any event, ensure that the marketing materials:
- (a) are ~~accurate and~~ not false, biased, misleading or deceptive;
 - (b) are clear, fair and present a balanced picture of the fund with adequate risk disclosures;
 - (c) contain information that is timely and consistent with the fund's offering document; and
 - (d) ~~and that any~~ only contain performance claims that can be verified.

Offers of Investments

- 7.3 A Fund Manager should comply with all applicable statutory requirements regarding the offer of investments.

8. Fees and Expenses

Disclosure of Charges



- 8.1 A Fund Manager should disclose to ~~the client~~ a fund and fund investors the basis and amount of its fees and charges.

Fair and Reasonable Charges

- 8.2 All charges, fees and mark-ups affecting a ~~client~~ fund and fund investors should be fair and reasonable in the circumstances, and be ~~characterized~~ characterised by good faith. In connection with mark-ups levied on transactions on behalf of a ~~client~~ fund, where the Fund Manager is:

- (a) acting as agent, such mark-ups are prohibited; and
- (b) acting as principal, the circumstances should be disclosed ~~in~~ to the ~~Client Agreement~~ fund and fund investors and transactions be reported in periodic statements.

Rebates and Soft Commission

- 8.3 In connection with an ~~authorised~~ authorized collective investment scheme, a Fund Manager should comply with ~~40.12~~ the relevant requirements of the Code on Unit Trusts and Mutual Funds in force from time to time, and, in connection with other ~~clients~~ funds, comply with ~~13.1 to 13.4~~ the relevant requirements of the Code of Conduct for ~~Persons Licensed by or Registered with the SFC~~ in force from time to time.

IV. ELECTRONIC TRADING REPORTING

9. Electronic Trading Reporting Obligations to the SFC

- ~~9.1 This paragraph applies a Fund Manager who conducts electronic trading of securities and futures contracts that are listed or traded on an exchange on behalf of collective investment schemes managed by it. The definition of "electronic trading" provided in paragraph 18.2 of the Code of Conduct for Persons Licensed by or Registered with the SFC (**Code of Conduct**) should be interpreted accordingly.~~

- ~~9.2 A Fund Manager should comply with the following principles and requirements when conducting electronic trading on behalf of collective investment schemes managed by it:~~

- ~~(a) Paragraphs 18.3 to 18.6 and 18.9 to 18.11 of the Code of Conduct; and~~
- ~~(b) Paragraphs 1.1 to 1.3 and 3.1 to 3.4 of Schedule 7 to the Code of Conduct.~~

- 9.1.1 Fund Managers should provide appropriate information to the SFC on an ongoing basis upon request.

Note: For example, such information may include:

- (a) *leverage;*
- (b) *assets and, where available, liability information (including illiquid assets);and*



(c) information on each fund's securities lending, repo and similar over-the-counter transactions.

Where necessary, for the effective monitoring of systemic risk, a Fund Manager may be required to provide other information on a periodic as well as on an ad hoc basis as the SFC may require from time to time.

9.1.2 A Fund Manager should respond to requests and enquiries from the SFC promptly in an open and co-operative manner.

9.1.3 A Fund Manager should ensure that all information provided to the SFC is in all material respects accurate, complete and not misleading. If it becomes aware that the information provided does not meet this requirement, the Fund Manager should inform the SFC promptly.



APPENDIX 1

Requirements for licensed or registered persons conducting discretionary accounts management

Introduction

Where applicable, those licensed or registered persons that are involved in the management of discretionary accounts which are operated in the following manner should observe the requirements of this Code as well as any additional requirements set out in this Appendix:

- (a) where a licensed or registered person provides discretionary management services to a client, in the form of an investment mandate or a pre-defined model investment portfolio; and

Note: The investment mandate may set out, among others, the types, risks and allocation of investments after taking into account the client's investment objectives and strategies. In the case of a pre-defined model portfolio, it may specify the proportion of the asset classes and markets and the risk profile of the selected portfolio.

- (b) the licensed or registered person receives management fee and/or performance fee as remuneration for managing the discretionary accounts for its clients.

For the avoidance of doubt, this Appendix applies to all licensed or registered persons acting as managers of discretionary accounts, including, as appropriate, their representatives. Where a person is involved in the management of both collective investment schemes and discretionary accounts, this Appendix only applies to the extent that that person is involved in the management of discretionary accounts.

Note: In relation to certain principles and requirements (as specifically set out in this Code) that are only applicable to a Fund Manager who is responsible for the overall operation of a fund, and has de facto control of the oversight or operation of the fund, discretionary account managers should also observe these principles and requirements, where applicable, and to the extent relevant to the functions and powers of the discretionary account manager.

Interpretation

Where requirements of this Code are applicable to discretionary accounts, terminologies that are specific to collective investments schemes/funds in the Code should be read as modified below:

- any reference to “fund” or “client” in this Code refers to “Discretionary Account”;
- any reference to “fund investors” in this Code refers to “Discretionary Account Clients”;
- any reference to “Fund Manager” in this Code refers to “Discretionary Account Manager”;
- any reference to “constitutive documents”, “offering documents” in this Code refers to “Investment Management Agreement” or “Discretionary Client Agreement”; and
- any reference to “redemption” in this Code refers to “capital withdrawal”.



Particular requirements in the Code which are not applicable to Discretionary Account Managers

The following requirements do not apply to a Discretionary Account Manager:

(a) Liquidity management

The requirements in relation to the use of specific tools or exceptional measures which could affect redemption rights and corresponding explanation in the offering documents are not applicable to a Discretionary Account Manager. (Paragraphs 3.14.1(e) and 3.14.2 of this Code)

Note: The extent of application of other liquidity management principles will depend on the capital withdrawal policy set out in the Discretionary Client Agreement.

(b) Termination

The requirements in relation to the termination process is not applicable to a Discretionary Account Manager. (Paragraphs 3.16.1 and 3.16.2 of this Code)

Note: A Discretionary Account Manager should observe the relevant termination provisions set out in the Discretionary Client Agreement.

(c) Side pockets

The requirements in relation to side pocket arrangements are not applicable to a Discretionary Account Manager. (Paragraphs 5.4.1 to 5.4.3)

(d) Auditors and audited accounts

The requirement in relation to the audit requirement of the financial statements of each of the funds under management is not applicable to a Discretionary Account Manager. (Paragraph 5.2.2 of this Code)

(e) Valuation frequency

The requirements in relation to the valuation frequency to be appropriate for the dealing frequency of the fund and related disclosure are not applicable to a Discretionary Account Manager. (Paragraph 5.3.5)

Note: Where applicable, a Discretionary Account should observe the relevant requirements set out in paragraphs 5.3.1 to 5.3.7 (save for the appropriateness to the dealing frequency and related disclosure set out in paragraph 5.3.5) and the relevant valuation provisions set out in the Discretionary Client Agreement.

(f) Net Asset Value Calculation and Pricing

The requirements in relation to net asset value calculation of different unit/share classes are not applicable to a Discretionary Account Manager. (Paragraphs 5.5.1 and 5.5.2 of this Code)



Note: Where applicable, a Discretionary Account Manager should observe the requirements in relation to overall net asset value calculation of the Discretionary Account.

(g) Offer of Investments

The requirement in relation to compliance with all applicable statutory requirements regarding the offer of investments is not applicable to a Discretionary Account Manager. (Paragraph 7.3 of this Code)

Additional requirements applicable to Discretionary Account Managers

In addition to the requirements set out in this Appendix, the requirements set out in the following paragraphs are also generally applicable to a Discretionary Account Manager:

Client Agreements

1. A Discretionary Account Manager should ensure that a written agreement (Discretionary Client Agreement) is entered into with a client before any services are provided to or transactions made on behalf of that client. A Discretionary Client Agreement should set out the precise terms and conditions under which discretion will be exercised and contain at least such information set out in the section “Minimum Content of Discretionary Client Agreement” and be provided in a language understood by the client. These minimum requirements do not apply to Institutional Professional Investors or Corporate Professional Investors as defined in paragraph 15.2 of the Code of Conduct and in the case of Corporate Professional Investors, the Discretionary Account Manager has also complied with paragraphs 15.3A and 15.3B of the Code of Conduct.

Performance Review and Valuation Reports

2. Except as agreed otherwise in writing by the client, a Discretionary Account Manager should:
 - (a) review the performance of each Discretionary Account against any previously agreed benchmark, either in writing to the client or by way of meeting, at least twice a year; and
 - (b) provide valuation reports to the client on a monthly basis or at such shorter intervals as provided in the Discretionary Client Agreement. The report should, as a minimum, include the following:
 - (i) the date on which the report is made;
 - (ii) the cash and investment holdings and value of the Discretionary Account on that date including all income received and charges levied against that account;
 - (iii) movements in the value of the Discretionary Account; and
 - (iv) any open positions in relation to derivative transactions.

Minimum Content of Discretionary Client Agreement

- (a) Full name and address of client;



- ~~(b) Full name and address of Fund Manager business, including its licensing or registration status;~~
- ~~(c) Undertakings to notify the other in the event of material changes;~~
- ~~(d) Authorisation for discretionary management;~~

In addition to the minimum content of client agreement set out in paragraph 6.2 of the Code of Conduct, a Discretionary Client Agreement should contain at least provisions to the following effect:

- ~~(a) appointment of the licensed or registered person as the Discretionary Account Manager;~~
- ~~(e) (b) Statement statement of the client's investment policy and objectives, including asset classes, geographical spread, performance benchmark, risk profile of the target portfolio and any limitations or prohibitions on asset classes and markets or instruments (e.g. use of derivatives) or geographical spread, performance benchmark and/or attitude to risk;~~

In the case where the client has selected a pre-defined model portfolio, the Discretionary Client Agreement should also specify the proportion of the asset classes, markets, and corresponding risk profile of the selected pre-defined model portfolios;

- ~~(f) (c) The the amount of all fees to be paid by the client, whether to the Fund Discretionary Account Manager or to a connected person with respect to the account, and a description of fees to be paid by the client to third parties, where applicable;~~
- ~~(g) Any necessary consents in relation to cash rebates and soft commissions, if applicable;~~
- ~~(h) Risk disclosure statement as required by the Code of Conduct for Persons Licensed by or Registered with the SFC;~~
- ~~(d) any consent from the client where the Discretionary Account Manager intends to receive soft commission or retain cash rebates;~~
- ~~(i) (e) Details details of custody arrangements if the Discretionary Account Manager provides custody arrangement by itself or through its associated entity; and~~
- ~~(j) (f) Details details of periodic reporting to be made to client.~~



APPENDIX 2

Suggested risk-management control techniques and procedures for funds

A. Risk management

- 1. A Fund Manager should establish and maintain effective risk management policies and reporting methodologies.**
- 2. The fund's risk policies and measurements and reporting methodologies should be subject to regular review, particularly when there are significant changes to the fund or relevant market conditions, legislation, rules or regulations that might impact the fund's risk exposure.**
- 3. The risk management policy for each fund should provide, for each fund, a system of limits concerning the measures used to monitor and to control the relevant risks.**

B. Market risk

- 1. A Fund Manager should establish and maintain effective risk management measures to quantify the impact on the fund (especially if the fund deals in derivative financial products) and, if applicable, the impact from changing market conditions. These measures should cover all risk elements associated with the fund. Matters to be covered in such risk measures may include:**
 - (a) unspecified adverse market movements - using an appropriate value-at-risk or other methodology to estimate potential losses;**
 - (b) individual market factors - measuring the sensitivity of the fund's risk exposure to specific market risk factors e.g. shifts in the interest rate yield curve and changes in market volatility; and**
 - (c) stress testing - determining the effect of abnormal and significant changes in market conditions on the fund using various quantitative and qualitative variable assumptions.**

C. Liquidity risk

- 1. A Fund Manager should set and enforce concentration limits with respect to the funds' investments, collateral, markets and business counterparties, taking into account the respective liquidity profile and the fund's approved liquidity risk policies.**
- 2. A Fund Manager should establish and regularly monitor measures of maturity mismatches between the funds' underlying investments and their redemption obligations.**
- 3. A Fund Manager should establish appropriate arrears and default procedures to alert staff member(s) responsible for liquidity management to potential problems and to provide them with adequate time to take appropriate action to minimise the impact of fund counterparty liquidity problems.**



4. In assessing the liquidity of the assets of a fund, a Fund Manager should consider the following, where applicable:

- (a) obligations to creditors, counterparties and third parties;
- (b) the time to liquidate assets;
- (c) the price at which liquidation could be effected;
- (d) financial settlement lag time; and
- (e) the dependence of these considerations on other market risks and factors.

D. Issuer and counterparty credit risk

1. A Fund Manager should establish and maintain an effective credit rating system to evaluate the creditworthiness of the funds' counterparties and the credit risk of the fund's investments (or, if applicable, the relevant issuers).

E. Operational risk

1. In designing the policies, procedures, and internal controls to reduce operational risk, a Fund Manager should consider, amongst other considerations, physical and functional segregation of incompatible duties, maintenance and timely production of proper and adequate accounting and other records, the security and reliability of accounting and other information, staffing adequacy and prompt reconciliation of trading information.

2. A Fund Manager should establish, implement and maintain a business continuity and transition plan. The plan should include policies and procedures that ensure, in the case of a business disruption or an interruption to the Fund Manager's operations, the following matters are addressed:

- (a) the preservation of essential data and functions, and the maintenance of services and activities, or, where that is not possible, the timely recovery of such data and functions and the timely resumption of its services and activities;
- (b) continuity of effective communications with clients, employees, service providers and regulators;
- (c) identification, assessment and maintenance of third-party services critical to the operation of the Fund Manager; and
- (d) appropriate transitioning arrangements that account for the possible winding down of the Fund Manager's business or the transition of the Fund Manager's business to others in the event the Fund Manager is unable to continue providing its services.

Note:



Business disruptions, whether temporary or permanent, include, without limitation, natural disasters, cyber-attacks, technology failures, key personnel departures and other similar events.

3. The business continuity and transition plan, including the adequacy of the plan and the effectiveness of its implementation, should be reviewed at least annually. Records of such reviews should be maintained.



Proposed amendments to the Code of Conduct

Paragraph 1

Interpretation and application

1.4 ~~Persons to which the Code does not apply~~ [deleted]

~~To the extent that a licensed or registered person acts in the capacity of a management company in relation to the discretionary management of collective investment schemes (whether authorised or unauthorised), the Code does not apply to such activity. In relation to such activities, such licensed or registered persons are subject to the Fund Manager Code of Conduct issued by the Commission.~~

Paragraph 8

Information for clients

8.3 Disclosure of monetary and non-monetary benefits

Part A

Disclosure of monetary benefits

Where the monetary benefits received or receivable are quantifiable prior to or at the point of entering into a transaction

(a) Specific disclosure

Explicit remuneration arrangement

- (i) Where a licensed or registered person and/or any of its associates explicitly receives monetary benefits from a product issuer (directly or indirectly) for distributing an investment product, the licensed or registered person should disclose the monetary benefits that are receivable by it and/or any of its associates as a percentage ceiling of the investment amount or the dollar equivalent.

Trading profit made from a back-to-back transaction

- (ii) Where a licensed or registered person enters into a back-to-back transaction concerning an investment product, the licensed or registered person should disclose to the client the trading profit to be made. The trading profit should be disclosed as a percentage ceiling of the investment amount or the dollar equivalent.

Notes

For the avoidance of doubt, the specific disclosure should be made on a transaction basis.



As a minimum, a licensed or registered person should disclose the monetary benefits that are receivable by it and/or any of its associates or the trading profit in the form of a percentage ceiling of the investment amount rounded up to the nearest whole percentage point or the dollar equivalent. However, having regard to its own circumstances, the licensed or registered person may disclose a specific percentage or the dollar equivalent instead.

Back-to-back transactions refer to those transactions where a licensed or registered person, after receiving –

- (a) a purchase order from an investor, purchases an investment product from a third party and then sells the same investment product to the investor; or
- (b) a sell order from an investor, purchases an investment product from the investor and then sells the same investment product to a third party,

and no market risk is taken by the licensed or registered person.

(b) Generic and other disclosure

Non-explicit remuneration arrangement

- (i) Where a licensed or registered person does not explicitly receive monetary benefits for distributing an investment product which is issued by it or any of its associates, the licensed or registered person should disclose that it or any of its associates will benefit from the origination and distribution of this product.

Where the monetary benefits received or receivable are not quantifiable prior to or at the point of entering into a transaction

- (ii) Where the monetary benefits received or receivable by a licensed or registered person and/or any of its associates are not quantifiable prior to or at the point of entering into a transaction, the licensed or registered person should disclose the existence and nature of such monetary benefits, the range of such monetary benefits receivable on an annualised basis, and the dollar equivalent of the maximum amount of such monetary benefits receivable per year.

Notes

For the avoidance of doubt, the disclosure in respect of this paragraph 8.3(b)(ii) of the Code should be made on a transaction basis.

The maximum amount of monetary benefits receivable per year should be determined on the assumption that the client will remain invested in the relevant investment product for a 12-month period and the value of the client's invested amount in the investment product will remain unchanged throughout that period.

Part B

Disclosure of non-monetary benefits

- (a) Where a licensed or registered person and/or any of its associates receives from a product issuer non-monetary benefits for distributing an investment product, the



licensed or registered person should disclose the existence and nature of such non-monetary benefits.

8.3A Disclosure of transaction related information

- (a) Where a licensed or registered person distributes an investment product to a client (including where it sells an investment product to or buys such product from the client), the licensed or registered person should deliver the following information to the client prior to or at the point of entering into the transaction:
- (i) The capacity (principal or agent) in which a licensed or registered person is acting;
 - (ii) Affiliation of the licensed or registered person with the product issuer;
 - (iii) Whether or not the licensed or registered person is independent (with reference to the requirements set out in paragraph 10.2 of the Code) and the bases for such determination;
 - ~~(iii)~~(iv) Disclosure of monetary and non-monetary benefits (*Please please refer to paragraph 8.3 of the Code*); and
 - ~~(iv)~~(v) Terms and conditions in generic terms under which client may receive a discount of fees and charges from a licensed or registered person.
- (b) The disclosure must be made in writing, electronically or otherwise. In respect of the disclosure to be made under paragraph 8.3A(a)(iii), the disclosure should be made in the form of a statement as specified in Schedule 9 to the Code. The licensed or registered person should have adequate measures in place to ensure that the above information is provided to the client prior to or at the point of entering into the transaction. In respect of the disclosure to be made under paragraph 8.3A(a)(i), (ii), (iii), and (v) above, a one-off disclosure (“One-off Disclosure”) is acceptable. Where there are changes to the One-off Disclosure, either (1) an updated One-off Disclosure, or (2) individual disclosure for each transaction where the information for which deviates from the information in the One-off Disclosure, must be provided to the client prior to or at the point of entering into a transaction.
- (c) In circumstances where provision of information in written form is not possible before a transaction is concluded, the licensed or registered person should make a verbal disclosure and provide such information in writing to the client as soon as practicable after the conclusion of the transaction.
- (d) The information disclosed in written form should be in Chinese or English according to the language preference of the client.

Notes

The licensed or registered person should ensure that the disclosure in writing is prominent, is presented in a clear and concise manner and is easy for average clients to understand.



Paragraph 10

Conflicts of interest

10.1 Disclosure and fair treatment

Where a licensed or registered person has a material interest in a transaction with or for a client or a relationship which gives rise to an actual or potential conflict of interest in relation to the transaction, it should neither advise, nor deal in relation to the transaction, unless it has disclosed that material interest or conflict to the client and has taken all reasonable steps to ensure fair treatment of the client.

10.2 Independence

Where a licensed or registered person represents itself as being independent, or uses any other term(s) with similar inference, when distributing an investment product:

- (a) it should not receive fees, commissions, or any monetary or non-monetary benefits, paid or provided (whether directly or indirectly) by any party in relation to such distribution of investment product to clients; and
- (b) it should not have any links or other legal or economic relationships with product issuers which are likely to impair its independence in respect of favouring a particular investment product, a class of investment products or a product issuer.



Schedule 9 Disclosure statement in respect of an intermediary's independent status

Under paragraph 8.3A(a)(iii) of the Code, where a licensed or registered person distributes an investment product to a client (including where it sells an investment product to or buys such product from the client), the licensed or registered person should inform the client, prior to or at the point of entering into the transaction, whether or not the licensed or registered person is independent (with reference to the requirements set out in paragraph 10.2 of the Code) and the bases for such determination.

Such disclosure should be made by the licensed or registered person to the client containing the substance set out in the following disclosure statements.

Where the licensed or registered person is independent:

"We are an independent intermediary because:

1. we do not receive fees, commissions, or any other monetary or non-monetary benefits, provided by any party in relation to our distribution of any investment product to you; and
2. we do not have any links or other legal or economic relationships with product issuers which are likely to impair our independence in respect of favouring any particular investment product, any class of investment products or any product issuer."

Where the licensed or registered person is NOT independent:

"We are **NOT** an independent intermediary because:

1. we have links or other legal or economic relationships with issuers of products that we may distribute to you;

Note: in addition to making the disclosure in the paragraph above, it is optional for a licensed or registered person to further provide a description of the links or other legal or economic relationships with product issuers which are likely to impair the intermediaries' independence in respect of favouring any particular investment product, any class of investment products or any product issuer.

and/or

2. we receive fees, commissions, or other monetary or non-monetary benefits, from other parties (which may include product issuers) in relation to our distribution of investment products to you. For details, you should refer to our disclosure on monetary and non-monetary benefits which we are required to deliver to you prior to or at the point of entering into any transaction in investment products."



Appendix C

Further information on proposed securities lending and repurchase agreements requirements

Design of haircut methodologies

As discussed in paragraph 28 of this consultation paper, the SFC proposes that the design of a haircut methodology to be put in place by a Fund Manager should reflect the standards set by the FSB in its recommendations. In particular, Fund Managers should note the following FSB recommendations in this connection:

- (a) The haircut methodology of a Fund Manager should be designed on the basis that haircuts are set to cover the maximum expected decline in the market price of the collateral asset (over a conservative liquidation horizon) before a transaction can be closed out.
- (b) The maximum price decline used to determine the applicable haircut should be calculated using a long time series of price data that covers at least one stress period. If such historical data is either unavailable or unreliable, then stress simulations or data for other similar asset types as a proxy (including at least one stress period and with prudent adjustments made as appropriate) should be used. The assumed liquidation horizon should be conservative, reflect the expected liquidity or illiquidity of the asset in stressed market conditions, and depend on the relevant market characteristics (such as trading volumes and market depth) and other special characteristics of the collateral.
- (c) Haircuts should cover different risk considerations where relevant, including market risk, counterparty credit risk and foreign exchange risk. Additional factors to be considered in setting the appropriate haircut should include:
 - (i) specific characteristics of the collateral; and
 - (ii) the correlation between securities accepted as collateral and the lent securities.

Disclosure requirements relating to securities lending, repos and similar OTC transactions

As discussed in paragraph 33 of this consultation paper, a Fund Manager should disclose, at least on an annual basis and upon request, information relating to securities lending, repos and similar OTC transactions. As a minimum, the following information should be disclosed:

- (a) Global data:
 - (i) the amount of securities on loan as a proportion of total lendable assets and of the fund's assets under management; and
 - (ii) the absolute amount of assets engaged in securities lending, repos and similar OTC transactions.
- (b) Concentration data:
 - (i) top 10 collateral securities received by issuer; and
 - (ii) top 10 counterparties of securities lending, repos and similar OTC transactions.
- (c) Aggregate transaction data:
 - (i) by type of collateral received;



- (ii) by currency;
 - (iii) by maturity tenor;
 - (iv) by geography (counterparty);
 - (v) cash versus non-cash collateral;
 - (vi) maturity of collateral; and
 - (vii) settlement and clearing (tri-party, central counterparty, bilateral).
- (d) Reinvestment and re-hypothecation data:
- (i) share of collateral received that is re-invested or re-hypothecated, compared to the maximum authorized amount if any;
 - (ii) information on any restrictions on type of collateral received; and
 - (iii) aggregate transaction data for collateral re-invested or re-hypothecated by product type
- (e) Return data on collateral, including the split between the return from securities lending, repos and similar OTC transactions and the return from cash collateral reinvestment.
- (f) Number of custodians and the amount of collateral assets held by each of the custodians.
- (g) The proportion of collateral posted by funds which are held in segregated accounts, pooled accounts, or in any other accounts.

The SFC will keep in view any additional disclosure requirements relating to securities lending, repos and similar OTC transactions that may be issued by the FSB in future and the need for any subsequent amendments.