



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

## **Consultation Conclusions on the Proposed Regulatory Regime for Depositories of SFC-authorized Collective Investment Schemes**

**and**

## **Further Consultation on Proposed Amendments to Subsidiary Legislation and SFC Codes and Guidelines to Implement the Regulatory Regime for Depositories of SFC-authorized Collective Investment Schemes**

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**February 2022**

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## Foreword

On 27 September 2019, the Securities and Futures Commission (SFC) issued a Consultation Paper on the Proposed Regulatory Regime for Depositaries of SFC-authorized Collective Investment Schemes (2019 Consultation).

Part I of this paper summarises the comments received and provides the SFC's responses. Part II consults the public on proposed amendments to the relevant subsidiary legislation and SFC codes and guidelines to implement the regime.

The SFC invites market participants and interested parties to submit written comments no later than 30 April 2022 on the proposals in Part II and the draft amendments in Appendices A to C or on related matters which might have a significant impact upon the proposals. Any person wishing to comment on the proposals should provide details of any organisation whose views they represent.

**Please note that the names of the commentators and the contents of their submissions may be published, in whole or in part, 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, submission or both to be published by the SFC. If this is the case, please state that you wish your name, submission or both to be withheld from publication when you make your submission.**

Written comments may be submitted as follows:

By mail to:                   The Securities and Futures Commission  
54/F, One Island East,  
18 Westlands Road,  
Quarry Bay,  
Hong Kong

Re: Proposed Regulatory Regime for Depositaries of  
SFC-authorized Collective Investment Schemes - Further  
Consultation on Proposed Amendments to Subsidiary  
Legislation and SFC Codes and Guidelines

By fax to:                   (852) 2877 0318

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

By e-mail to:              ra13-consultation@sfc.hk

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

Securities and Futures Commission  
Hong Kong

February 2022

## 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 Data<sup>1</sup> 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 provisions<sup>2</sup> 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 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.

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<sup>1</sup> Personal Data means personal data as defined in the Personal Data (Privacy) Ordinance.

<sup>2</sup> 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 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:

Data Privacy Officer  
Securities and Futures Commission  
54/F, One Island East,  
18 Westlands Road,  
Quarry Bay,  
Hong Kong

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

## Executive summary

1. In September 2019, the Securities and Futures Commission (SFC) issued the Consultation Paper on the Proposed Regulatory Regime for Depositaries of SFC-authorized Collective Investment Schemes (2019 Consultation).
2. The 2019 Consultation proposed a framework for a new regulated activity, Type 13 (RA 13), to regulate top-level trustees and custodians (ie, the depositaries) of SFC-authorized collective investment schemes (CIS) under the Securities and Futures Ordinance (SFO) (relevant CIS). The proposal enhances the regulation of public funds and is part of the strategy to reinforce Hong Kong as an international, full-service asset management centre.
3. The consultation ended in December 2019. Nine written submissions were received, including from trustee companies, industry associations and law firms. A list of respondents (other than those who requested anonymity) is set out in Appendix D.
4. Respondents generally supported the proposals, agreeing that they are comparable with other leading international markets and would strengthen Hong Kong's position as a leading asset management centre. Key comments related to the scope of RA 13 and how it would apply to individuals who are staff of a depositary. Other comments sought clarification of various technical issues, in particular the requirements for depositaries in the proposed Schedule 11 to the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of Conduct). There were also comments seeking clarification of existing requirements.
5. Part I of this paper sets out the Consultation Conclusions on the Proposed Regulatory Regime for Depositaries of SFC-authorized Collective Investment Schemes. It summarises the key comments received and provides our responses.
6. Given the support for the RA 13 framework, the SFC will move the proposals forward, maintaining close dialogue with the industry and other stakeholders. The Consultation Paper on Proposed Amendments to Subsidiary Legislation and SFC Codes and Guidelines to Implement the Regulatory Regime for Depositaries of SFC-authorized Collective Investment Schemes is set out in Part II and Appendices A to C to this paper.
7. We would like to thank all respondents and the industry for their time and effort in providing us with their detailed comments on the proposals in the 2019 Consultation and those in Part II.
8. The 2019 Consultation, the responses (other than those requested to be withheld from publication) and this paper are available on the SFC website at [www.sfc.hk](http://www.sfc.hk).

## Part I – Consultation conclusions on the proposed regulatory regime for depositaries of SFC-authorized collective investment schemes

### Proposed scope

- Question 1:** Do you have any comments on the proposed scope of RA 13?
- Question 2:** Do you have any comments on the proposed exemption for trustees which only act for MPF products?
- Question 3:** Do you think any other exemptions are necessary? If so, what are they and why are they necessary?

### Proposed scope

#### *Public comments*

9. Most respondents agreed with the proposed scope of the regime covering top-level trustees and custodians. One respondent asked whether a depositary operating outside Hong Kong would fall within the scope of RA 13. Another respondent asked whether a company in Hong Kong which is delegated by an offshore depositary to perform the latter's depositary functions (in whole or in part) in Hong Kong would fall within the scope of RA 13.

#### *The SFC's response*

10. In general, offshore entities that do not carry on a business in a regulated activity (RA) in Hong Kong will not need to be licensed by or registered with the SFC.
11. As stated in the 2019 Consultation<sup>3</sup>, the SFC's policy intent is to capture only top-level trustees or custodians (ie, depositaries) which carry on a business in RA 13 in Hong Kong. A depositary's delegates (such as its sub-custodians) will not fall within the proposed scope of RA 13, regardless of whether such delegates operate within or outside Hong Kong.

### Exemptions

#### *Public comments*

12. While most respondents supported the proposal to exclude trustees of pure MPF products<sup>4</sup> from RA 13 to minimise regulatory duplication<sup>5</sup>, a few suggested that trustees of pooled retirement funds (PRFs) should also be exempted. There were also suggestions that approved pooled investment funds which are authorised for offering to the retail public (retail APIFs) should be exempted because trustees of retail APIFs are

<sup>3</sup> Paragraphs 15 and 16 of the 2019 Consultation.

<sup>4</sup> As explained in the 2019 Consultation, pure MPF products are approved by the MPFA and authorised by the SFC under section 104 of the SFO and pursuant to the SFC Code on MPF products. The Mandatory Provident Schemes (General) Regulation (Cap. 485A, Laws of Hong Kong) also requires pooled investment funds invested under MPF schemes to be authorised by the SFC.

<sup>5</sup> MPF-approved trustees are subject to the direct supervision of the Mandatory Provident Fund Schemes Authority (MPFA).

MPF-approved trustees regulated by the MPFA and a consistent approach should be adopted for retail APIFs and pure MPF products.

13. Two respondents also commented that the proposal would add significant compliance costs.

*The SFC's response*

14. PRFs are not pure MPF products as they do not generally fall within the MPFA's regulatory remit. Accordingly, it would not be appropriate to exempt PRF trustees.
15. The SFC maintains its view that retail APIFs should be distinguished from pure MPF products for the reasons stated in the 2019 Consultation<sup>6</sup>.
16. With regard to compliance costs, given that depositaries perform an important role with respect to public CIS, it is necessary for them to be regulated. Since a majority of the proposed requirements are based on existing Product Code<sup>7</sup> requirements, any additional compliance costs should not be substantial.

Other comments regarding the scope of RA 13

*Public comments*

17. A respondent suggested defining the business functions of an RA 13 depositary for better clarity. Another respondent commented that RA 13 should be defined by reference to an "activity" instead of a "role" for consistency with other types of RA.

*The SFC's response*

18. In view of the comments and subsequent discussions with the industry, we have revised our approach. RA 13 will be defined by reference to the activity of providing depositary services for a relevant CIS and propose to set out the core functions of a depositary in the definition. Our revised approach is discussed in paragraph 22 and Section 1 of Part II.

**Licensing and conduct requirements**

**Question 4: Do you have any comments on the proposed licensing scope applicable to staff members of RA 13 depositaries?**

**Question 5: Do you agree with the proposal to apply the existing licensing criteria to persons licensed or registered for RA 13? If not, please explain your views.**

<sup>6</sup> Paragraph 21 of the 2019 Consultation.

<sup>7</sup> As defined in paragraph 9 of the 2019 Consultation, the Product Codes collectively refer to the Code on Unit Trusts and Mutual Funds (UT Code), the Code on Pooled Retirement Funds (PRF Code), the Code on Real Estate Investment Trusts (REIT Code), and the Code on Open-Ended Fund Companies (OFC Code). Open-ended fund companies which are offered to the public in Hong Kong (ie, those which are registered and authorised under section 104 of the SFO) and their key operators (including the custodians) are required to comply with all applicable requirements under the UT Code as well as Section I of the OFC Code.



## Licensing requirements for individuals

### *Public comments*

19. The 2019 Consultation proposed that individuals performing a regulated function in relation to an intermediary's business of "acting as a depositary" should be licensed representatives (LRs) or relevant individuals for RA 13. Specifically, staff who perform more than a clerical role<sup>8</sup> in a business function directly relating to the depositary's discharge of its regulatory obligations set out in the Product Codes should be LRs or relevant individuals<sup>9</sup>.
20. Most respondents took the view that the proposed scope was too wide and the phrase "more than a clerical role" was unclear. There were also suggestions that only staff responsible for oversight functions should be required to be licensed or registered for RA 13, while staff who perform fund administration (such as fund accounting and fund valuation), transfer agency or registrar functions should not.
21. Some respondents asked whether individuals who are staff of an RA 13 depositary's delegates (but not staff of the depositary) and perform depositary functions on behalf of the delegate would be required to be licensed or registered for RA 13.

### *The SFC's response*

22. As mentioned in paragraph 18, we propose that RA 13 be defined as an activity of "providing depositary services for a relevant CIS" with reference to two core functions of a depositary, being (a) custody and safekeeping of scheme property and (b) oversight of the operation of the relevant CIS to ensure that it is operated in accordance with its constitutive documents.
23. As a result of these changes, the licensing scope applicable to individuals will be aligned with these two core functions as elaborated in paragraphs 24 and 25.
24. With respect to the custody and safekeeping of scheme property:
  - (a) where a depositary delegates this function to another entity (eg, a sub-custodian), staff of the depositary responsible for monitoring the performance of the delegate will need to be licensed or registered for RA 13; and
  - (b) where a depositary performs part or all of this function within the firm, staff of the depositary who are empowered to approve instructions or transactions for custody-related purposes (eg, approving payments or asset transfers, signing-off cash reconciliation) in respect of a relevant CIS and those who assume oversight duties over the performance of this function will need to be licensed or registered for RA 13; whereas staff who are engaged in custody operations without such approving powers or oversight duties will generally not be subject to the licensing obligations under the RA 13 regime.

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<sup>8</sup> A "clerical role" generally refers to the performance of routine tasks following established procedures which do not require staff to make business decisions.

<sup>9</sup> Paragraph 23 of the 2019 Consultation.

25. With respect to the oversight of scheme operations, staff of a depositary responsible for performing the duties of this function in respect of a relevant CIS should be licensed or registered for RA 13. Broadly speaking, oversight duties encompass the monitoring of various operations of the CIS including, amongst others, compliance with investment and borrowing restrictions, cash flow, fund accounting and valuation, as well as the issue, repurchase, redemption and cancellation of the units or shares of the CIS. Nevertheless, where a depositary also acts as the fund administrator, transfer agent or registrar for a relevant CIS, staff of the depositary who are engaged to provide such services are generally not required to be licensed or registered for RA 13, unless they also have an oversight responsibility in respect of these operations based on the particular business model and governance structure adopted by the depositary<sup>10</sup>.
26. Given the proposal to exclude delegates and sub-delegates from the RA 13 definition, it should be clear that individuals who are staff of these delegates will not be required to be licensed or registered.

#### Other comments on licensing requirements

##### *Public comments*

27. Two respondents asked for clarification of which Managers-in-Charge (MICs) need to be approved as responsible officers (ROs).
28. One respondent asked whether staff members in sales and marketing functions would be required to be licensed.
29. Another respondent sought guidance on whether an individual's overseas depositary experience which is not directly related to SFC-authorized CIS would be considered as relevant industry experience. Another asked whether there would be any exemptions from the local regulatory examination requirements.

##### *The SFC's response*

30. Under the current licensing regime, the MICs of the overall management oversight function and MICs of key business lines of a licensed corporation (LC) should be ROs. The MICs of other core functions<sup>11</sup> are generally not required to be licensed. The same expectation will apply to RA 13.
31. In view of the revised approach for defining RA 13 mentioned in paragraph 22, the marketing of a depositary's services by itself does not fall within the scope of "providing depositary services for a relevant CIS". Therefore, individuals who solely perform marketing activities for a depositary will not be subject to the licensing obligation under the RA 13 regime.
32. Relevant industry experience generally refers to hands-on working experience acquired through carrying on RAs in Hong Kong or similar regulated activities

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<sup>10</sup> Based on our discussions with the industry, we understand that depositaries currently adopt different business models and governance structures in performing their oversight function in respect of relevant CIS. While the SFC does not mandate a particular business model or governance structure, a depositary should ensure that its oversight function is carried out effectively by among other things, deploying sufficient staff (who are suitably qualified) to perform this function, having regard to its scale of operations including the number and the complexity of the relevant CIS under its oversight.

<sup>11</sup> Including operational control and review, risk management, finance and accounting, information technology, compliance and anti-money laundering and counter-terrorist financing.

elsewhere<sup>12</sup>. Accordingly, experience in providing depositary services, regardless of whether the experience was acquired in Hong Kong or overseas, will be recognised for licensing purposes in relation to RA 13.

33. As set out in the 2019 Consultation<sup>13</sup>, the SFC will provide a grandfathering arrangement (ie, attending training courses in lieu of passing local regulatory examinations) for practitioners when implementing the RA 13 regime. In addition, an individual may apply for an exemption from the recognised industry qualification and the local regulatory framework paper requirements if he or she satisfies the exemption criteria set out in the Guidelines on Competence<sup>14</sup>.

### Financial resources requirements

**Question 6: Do you agree with the amounts proposed for the financial resources requirements for RA 13 licensed corporations under the Financial Resources Rules<sup>15</sup>? If not, please explain your views.**

#### *Public comments*

34. There were no objections to the proposed requirement for an RA 13 LC to have a minimum paid up share capital of HK\$10,000,000 (which is similar to the current financial resources requirement under the Product Codes) and a minimum liquid capital of HK\$3,000,000.
35. One respondent who is not a depositary commented that the removal of the option currently available under the Product Codes for a trustee or custodian to rely on its parent company's standing commitment or undertaking to meet the financial resources requirements may be burdensome.

#### *The SFC's response*

36. Given that no potential RA 13 depositaries indicated that they are unable to meet the proposed requirements, which are consistent with the requirements for other types of RAs, we will proceed with the proposal. Please see Part II and Appendix A.

### Professional indemnity insurance requirement

**Question 7: Do you agree with the proposed requirement for RA 13 depositaries to maintain a professional indemnity insurance policy with respect to their RA 13 business? If not, please explain your views.**

<sup>12</sup> Paragraph 4.1.8 of the Guidelines on Competence.

<sup>13</sup> Paragraph 47 of the 2019 Consultation.

<sup>14</sup> Paragraph 4.4 of the Guidelines on Competence.

<sup>15</sup> Securities and Futures (Financial Resources) Rules (Cap. 571N, Laws of Hong Kong) (FRR).

*Public comments*

37. One respondent asked if registered institutions (RIs) could be exempted from the professional indemnity insurance requirement. Another respondent sought clarification of whether a self-insurance programme provided at the group level for an RA 13 depository within a banking group would be adequate.

*The SFC's response*

38. A depository, regardless of whether it is a RI or a LC, should maintain professional indemnity insurance coverage commensurate with its business, in line with the requirements applicable to certain other intermediaries<sup>16</sup>. The insurance can be maintained at either group or entity level. We will proceed with the proposal to set out this requirement in the proposed Schedule 11. Please see Part II and Appendix B.

**Conduct and internal control requirements**

- Question 8: Do you agree with the proposal to rely on existing provisions in the Product Codes for the regulation of RA 13 depositories? If not, please explain your views.**
- Question 9: Do you agree with the proposals (i) to remove the requirement for the submission of annual internal control reports and (ii) for the provision of additional internal control requirements in the proposed Schedule 11 to the Code of Conduct? If not, please explain your views.**

*Public comments*

39. Respondents generally agreed with the proposal to rely on existing provisions in the Product Codes for the regulation of RA 13 depositories and, while there were some specific comments on the detailed provisions, the introduction of the proposed Schedule 11 to the Code of Conduct. Respondents also welcomed the proposal to remove the submission of annual internal control reports.

*The SFC's response*

40. Given the support received, the SFC will proceed with the proposal. Please see part II and Appendix C.

- Question 10: Do you have any comments on the proposed Schedule 11? For requirements which are oversight functions of the depository under the proposed Schedule 11, the term "relevant operator(s)" has been used to refer to the party or parties which should be subject to the depository's oversight. Do you have any comments on the use of this term? We would welcome any input regarding which specific party should appropriately be subject to the depository's oversight.**

<sup>16</sup> For example, paragraph 1.2(e) of the Fund Manager Code of Conduct.

41. There were extensive comments on the proposed Schedule 11. In view of some of the comments and subsequent discussions with the industry, we have revised Schedule 11 as set out in Part II and Appendix B to this paper for further consultation. The following summarises the main comments received and the SFC's responses.

### Scope of Schedule 11

#### *Public comments*

42. There were general comments that the scope of certain requirements under Schedule 11 were wider than Appendix G to the UT Code and suggestions that the language in Appendix G be adopted instead.
43. There were also comments that a depositary should not be required to assume primary responsibility for activities which are carried out by the depositary but are beyond the scope of RA 13 (eg, fund accounting and valuation).

#### *The SFC's response*

44. While every effort has been made to reflect the regulatory objectives of Appendix G in Schedule 11, it should be noted that Appendix G contains terms of reference for an audit, whereas Schedule 11 sets out specific regulatory obligations and is part of the Code of Conduct. As such, it is necessary for the obligations in Schedule 11 to be clear and aligned with other provisions of the Code of Conduct. We have reviewed the provisions which respondents suggested impose wider or new obligations compared to existing ones in the UT Code<sup>17</sup> and are satisfied that the revised proposed Schedule 11 reflects the obligations expected of RA 13 depositaries.
45. Under the proposed scope of RA 13, depositaries have oversight obligations over the operation of a CIS. Where a depositary carries out these operational functions itself (eg, by acting as the transfer agent or fund administrator), it would be held primarily responsible for them.

### Relevant operators

#### *Public comments*

46. A few respondents were of the view that the existing framework for open-ended fund companies (OFCs) does not require the custodian to oversee the board of directors and suggested removing the board of directors from the definition of "relevant operators". One respondent also asked whether "relevant operators" covers sub-custodians.

#### *The SFC's response*

47. Notwithstanding the specific oversight obligations in the Product Codes, a core function of a depositary is to have oversight of a relevant CIS to ensure that it is operated in accordance with the constitutive documents. This oversight obligation is the same regardless of the identity of the operator performing the activity. Under the UT Code<sup>18</sup>,

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<sup>17</sup> Examples of provisions in the proposed Schedule 11 which a respondent suggested may be new or wider than existing ones in the UT Code include: the requirements for depositaries to (a) report to the management company matters which may affect the depositary's ability to discharge its functions; (b) have in place policies and procedures to address actual or potential conflicts of interest (instead of only "conflicts of interest"); (c) safeguard all CIS property (instead of only physical assets).

<sup>18</sup> For example, obligations under 4.5 (b), (c), (e), (g) and (h) of the UT Code.

the oversight obligations of a depositary include, for example, oversight of the issue of units or shares of the relevant CIS. These activities may be carried out by the board of directors of an OFC, the management company or other operators. Hence, the board of directors is a “relevant operator” for the purposes of these requirements. On the other hand, sub-custodians are delegates of the depositaries and are not “relevant operators”.

### Communication with management company

#### *Public comments*

48. A majority of the respondents suggested adding an explicit requirement for management companies to provide relevant information to depositaries<sup>19</sup> to enable depositaries to discharge their functions and obligations.
49. A respondent commented that the management company should be the party to promptly report material breaches or issues to the depositary instead of the other way round. There was also a suggestion that a depositary’s reporting obligations be restricted to material breaches by itself or its delegates.
50. Two respondents suggested that communication with the management company with respect to a depositary’s business continuity plan (BCP) is necessary only if there would be an impact on the services provided to the relevant CIS or the management company.

#### *The SFC’s response*

51. Reporting obligations are existing requirements imposed on depositaries under the Product Codes. Given that a depositary has oversight of the operations of a CIS, it should be aware of reportable breaches regardless of which party the breach is attributed to. We are also of the view that management companies and depositaries should effectively communicate breaches or other material issues relating to the operation of the CIS to one another. They are also expected to coordinate to ensure that breaches or issues are reported to the SFC<sup>20</sup>. Consequential amendments to the UT Code and the REIT Code have been proposed.
52. Paragraph 5(b) of Schedule 11 has been revised so that the depositary will only need to notify the management company of material exceptions to its BCP which may have a material adverse impact on the operation of the CIS or the discharge of the depositary’s obligations.

### Delegation

#### *Public comments*

53. A few respondents suggested that a depositary’s obligations regarding the selection and ongoing monitoring of its own delegates should be distinguished from the oversight of the management company’s delegates. It was suggested that Schedule 11 should be clarified to require a management company to have primary responsibility for the

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<sup>19</sup> Such as material breaches.

<sup>20</sup> Please refer to the existing requirements under 4.5(k) and Note 2 of 5.10(d) of the UT Code (which also apply to the PRF Code), and paragraphs 8A(2)(ii)&(iii), 8A(6) and 8A(7)(ii) of Appendix G to the UT Code. Please also refer to paragraph 6 of Section V (Compliance) of the Internal Control Guidelines.

delegates and third parties that it appoints and that the depositary's responsibilities for these delegates and third parties should be confined accordingly.

*The SFC's response*

54. Depositaries are required to have oversight of the relevant CIS to ensure that it is operated in accordance with the constitutive documents of the CIS. In order to discharge this oversight function, depositaries are responsible for monitoring the relevant operational activities, whether they are carried out by delegates appointed by the depositary itself, or third parties appointed by other operators (including but not limited to the management company). A note to paragraph 6 of Schedule 11 has been added to clarify this expectation.

Pricing error or exception reporting

*Public comments*

55. Two respondents commented that it is the management company's obligation to report pricing errors and exceptions and not the depositary's. They suggested that a depositary should only report these to the SFC if the management company has not done so.

*The SFC's response*

56. There is no inconsistency between the proposed requirements and the respondents' comments. As explained in paragraph 51 above, we expect the depositary to maintain effective communication with the management company, particularly in relation to pricing errors or exceptions which would need to be reported under the regulatory requirements or may adversely impact the operations of the CIS, the orderliness of the market or investors' interests.

Cash flow monitoring

*Public comments*

57. A respondent said that the requirement to seek prior written consent from the depositary regarding cash placed with others<sup>21</sup> should be part of the controls to address conflicts of interest and it is unnecessary for a depositary to grant prior written consent to itself. The respondent also suggested that a depositary should not be required to identify all cash flows which are inconsistent with the operations of the relevant CIS, but only those cash flows which are "significant".

*The SFC's response*

58. In view of the comments, we have revised the proposals<sup>22</sup> so that a depositary must ensure relevant operators have effective controls in place for obtaining all necessary prior written consent from the depositary for connected party transactions. The requirement regarding connected party transactions is now in paragraph 15 of Schedule 11.

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<sup>21</sup> Paragraph 13(b) in the draft Schedule 11 in the 2019 Consultation (now paragraph 15(c)(ii)).

<sup>22</sup> Paragraphs 13(b) and (c) in the draft Schedule 11 in the 2019 Consultation are combined and moved to under paragraph 15 (Connected party transactions entered into by or on behalf of the relevant CIS) in the revised draft Schedule 11. Please refer to Appendix B.



59. We are of the view that all cash flows which are inconsistent with the operations of the relevant CIS should be identified, even if they are insignificant.

### Investment monitoring

#### *Public comments*

60. In response to the proposal<sup>23</sup>, a respondent commented that ensuring the accuracy of investment records is the management company's responsibility; depositaries maintain and reconcile asset records to enable the management companies to do so. Other respondents suggested that a depositary should have oversight of the management company's policies and procedures relating to investment records.

#### *The SFC's response*

61. The proposed requirement has been revised to clarify that a depositary should provide the management company with its reconciled records of relevant CIS property and transactions executed on behalf of the relevant CIS to facilitate the management company's verification of the accuracy of its investment records. This aligns with the policy intent of the existing requirements<sup>24</sup> which is to ensure the accuracy of investment records.

### Custody and safekeeping of relevant CIS property

#### *Public comments*

62. One respondent commented that Appendix G does not include the proposed requirement<sup>25</sup> for a payment or asset transfer on behalf of a relevant CIS to be authorised by the depositary and the depositary's obligation to ensure that the management company has properly authorised or obtained authorisation for the payment or asset transfer. Another respondent commented that a depositary should monitor rather than manage custody risks. Two respondents sought clarification that a depositary should properly safeguard only physical assets.

#### *The SFC's response*

63. The authorisation requirement is based on the principle that all payments and asset transfers, or other dealings on behalf of a relevant CIS, should be properly authorised in accordance with the constitutive documents of the relevant CIS. We have revised the proposal<sup>26</sup> to clarify our expectations by setting out guidance on the depositary's oversight obligation where a payment or asset transfer need not be authorised by the depositary.
64. More importantly, custody risks need to be managed and not just monitored in order for the depositary to discharge its obligations. In addition, a depositary should safeguard all assets and not only physical assets.

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<sup>23</sup> Paragraph 14(c) of the draft Schedule 11 in the 2019 Consultation.

<sup>24</sup> Under 8A(13)(iii) of Appendix G to the UT Code.

<sup>25</sup> Paragraph 15(h) in the draft Schedule 11 in the 2019 Consultation.

<sup>26</sup> Paragraph 14(j) and note to paragraph 14(j).



## Key operators

### *Public comments*

65. A respondent commented that it is unnecessary to impose specific management company oversight obligations on the depository in Schedule 11 given that the management company is also regulated by the SFC.

### *The SFC's response*

66. A critical role of a depository is to perform independent oversight of the relevant CIS to ensure that it is operated in accordance with the constitutive documents and regulatory requirements. Paragraph 8 of Schedule 11 has been revised accordingly.
67. The management company and the depository each perform important functions in relation to a relevant CIS. In this regard, the existing system of checks and balances between the management company and depository ensures that the relevant CIS is operated in accordance with the constitutive documents and regulatory requirements<sup>27</sup>.

## Schedule 11 requirements regarding REITs

### *Public comments*

68. A respondent commented that the requirements in relation to subscription and redemption<sup>28</sup> should not be applicable to depositories of REITs since REITs are close-ended listed CIS.
69. The same respondent also suggested that the proposed requirements<sup>29</sup> for valuation/price/net asset value (NAV) calculation monitoring and distribution payment should be disapplied to depositories of REITs on the basis that NAV and distribution calculations are subject to an auditor's independent review; and under current requirements a REIT trustee is only required to take reasonable care to ensure that the NAV of a REIT is calculated by the valuer and published in the REIT's annual report<sup>30</sup>.
70. The respondent further suggested carving out REIT depositories from the proposed requirements relating to mark-to-market of collateral<sup>31</sup> since there will never be non-cash collateral. The respondent also requested that the proposed requirement<sup>32</sup> regarding the custody and safekeeping of property be replaced by requirements in Part II of Schedule 11. The respondent also commented that there would be practical difficulties in meeting the proposed daily cash reconciliation requirement<sup>33</sup> in view of the abundance of special purpose vehicles and large volume of cash transactions in REIT's daily property management operations.

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<sup>27</sup> See also paragraph 41 of the 2019 Consultation.

<sup>28</sup> Paragraph 10 of the draft Schedule 11 in the 2019 Consultation.

<sup>29</sup> Paragraphs 11 and 12(a) of the draft Schedule 11 in the 2019 Consultation.

<sup>30</sup> Under 4.2(m) of the REIT Code.

<sup>31</sup> Paragraph 14(g) of the draft Schedule 11 in the 2019 Consultation.

<sup>32</sup> Paragraph 15 of the draft Schedule 11 in the 2019 Consultation.

<sup>33</sup> Paragraph 15(b) of the draft Schedule 11 in the 2019 Consultation.

### *The SFC's response*

71. We disagree with the comment that the proposed requirements for subscription and redemption should not apply to REITs. Units of REITs may be issued or bought back subsequent to listing. For example, units may be issued to the manager as payment of management fees; there can be secondary offerings of new units and the issue of consideration units for asset acquisitions. In addition, the REIT Code currently requires REIT trustees to have oversight to ensure that the sale, issue, repurchase and cancellation of units effected by a scheme are carried out in accordance with the provisions of the constitutive documents<sup>34</sup>. Trustees are also currently required to take all reasonable care to ensure that unit certificates are not issued until subscription monies have been paid<sup>35</sup>.
72. The depositary of a REIT has fiduciary duties with respect to the REIT property. Although we recognise that a REIT depositary may not have the expertise to carry out certain activities — for example, real estate valuation, where it may rely on professional advisers such as the principal valuer — and that an auditor is appointed to audit the REIT as a whole, the depositary should still have effective oversight of the REIT's operations. On this basis, the requirements under paragraph 10 of Schedule 11 should generally be applicable to REIT depositaries. However, we agree that the requirements relating to pricing error in paragraph 10(d) would not typically be relevant to REITs as they are traded at the prevailing prices on the Stock Exchange of Hong Kong (SEHK). Where there is no issue of new REIT units based on the REIT's net asset value, the requirement under paragraph 10(d) will not be triggered. A new paragraph 19(a) has been added to Part II of Schedule 11 to clarify this.
73. The proposed mark-to-market collateral requirements will not be applicable if no non-cash collateral is held for the REIT so there is no need to explicitly disapply the requirement. On custody and safekeeping, paragraph 20(b) (now 19(c)) forms part of the requirement under paragraph 14 and the two should be read together. Paragraph 19(c) explains what a REIT depositary should do to comply with the requirements under paragraph 14.
74. With respect to the requirement to carry out daily cash reconciliation, we have taken into account the differences in the structures and operations of REITs as compared to other types of CIS and have revised the requirements in Schedule 11 accordingly.
75. Where appropriate, revisions have been made to Schedule 11 to address public comments as discussed above. Please see Part II and Appendix B.

### **Consequential changes to SFC codes and guidelines**

**Question 11: Do you agree with the proposed consequential amendments to the Product Codes? Are there additional amendments you believe to be appropriate? Please explain your views.**

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<sup>34</sup> 4.3(b) of the REIT Code.

<sup>35</sup> 4.2(j) of the REIT Code.

*Public comments*

76. Respondents generally had no objections to the high-level amendments to the Product Codes proposed in the 2019 Consultation.
77. A respondent sought clarification of whether a depositary's responsibility to exercise reasonable care, skill and diligence in the selection and monitoring of delegates should stop at the level of immediate delegates.
78. One respondent suggested that a list of acceptable jurisdictions for overseas depositaries for the purposes of section 4.2(d)<sup>36</sup> of the UT Code be issued.

*The SFC's response*

79. Given the general support received, we will proceed with the proposal. Please see Part II and Section 1 of Appendix C.
80. In terms of the responsibility over delegates, please see paragraph 54 above.
81. Given that there is no change to the position of overseas depositaries under 4.2(d) of the UT Code, we do not believe it necessary to promulgate a list of acceptable jurisdictions for overseas depositaries.

**Consequential amendments to subsidiary legislation**

**Question 12: Do you agree with the list of subsidiary legislation which may be subject to amendment? Would amendments be necessary to any other subsidiary legislation in order for RA 13 to be introduced? Please explain your views.**

*Public comments*

82. The following comments on specific rules were received –
- (a) Securities and Futures (Keeping of Records) Rules<sup>37</sup> (KRR) – A respondent suggested defining “records” as an RA 13 depositary's oversight records so that records kept at service providers (such as a fund administrator) would not be caught.
- (b) Securities and Futures (Client Securities) Rules<sup>38</sup> (CSR) and Securities and Futures (Client Money) Rules<sup>39</sup> (CMR) – A respondent proposed that the CSR and CMR be amended to allow client securities to be deposited in safe custody in segregated accounts established and maintained in Hong Kong by an RA 13 depositary and client money accounts to be established and maintained by an RA 13 depositary.

<sup>36</sup> 4.2(d) of the UT Code provides that one of the eligibility requirements to act as trustee/custodian of a SFC-authorized CIS is to be an overseas prudentially regulated and supervised bank or entity in a jurisdiction that is acceptable to the SFC.

<sup>37</sup> Cap. 571O, Laws of Hong Kong.

<sup>38</sup> Cap. 571H, Laws of Hong Kong.

<sup>39</sup> Cap. 571I, Laws of Hong Kong.

83. One respondent sought clarification of how a depository which is also a trust or company service provider (TCSP) licensed with the Companies Registry<sup>40</sup> should comply with the Guideline on Anti-Money Laundering and Counter-Financing of Terrorism (For Licensed Corporations) (AML/CFT Guideline). The respondent suggested that additional SFC guidance be provided on how a depository should determine the customer to whom customer due diligence (CDD) should apply<sup>41</sup>.
84. Two respondents commented that any over-the-counter derivative (OTCD) transactions would be originated by the management company, and therefore RA 13 depositaries should not be subject to the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules<sup>42</sup> (OTCD Reporting Rules) because the management company should remain the party responsible for the reporting and clearing obligations.

#### *The SFC's response*

85. Having considered the comments received and subsequent discussions with the industry, proposed amendments to subsidiary legislation are set out in Part II and Appendix A.
86. Regarding the comments on the CSR and CMR, securities held on behalf of a relevant CIS should only be deposited in accounts established and maintained with entities under section 5 of the CSR (ie, banks, LCs licensed for Type 1 RA, the Hong Kong Securities Clearing Company Limited<sup>43</sup> and the Hong Kong Monetary Authority (HKMA)<sup>44</sup>). We do not see a need to extend the scope of entities which can hold securities on behalf of a relevant CIS. Money held on behalf of a relevant CIS must be deposited in accounts established and maintained with authorised financial institutions.
87. All RA 13 LCs are required to comply with the AML/CFT Guideline<sup>45</sup>, regardless of whether the corporations are also licensed with the Companies Registry.
88. While an RA 13 depository is generally expected to carry out CDD on the relevant CIS to which the depository services are provided as the customer<sup>46</sup>, the depository may instead carry out CDD measures on the management company of the CIS if the following conditions are met:
- (a) the management company is a LC or RI;

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<sup>40</sup> Currently, a trustee of SFC-authorized CIS should obtain a TCSP licence from the Companies Registry unless it is exempted from the TCSP licensing requirement, such as an authorised institution, a licensed corporation that operates a trust or company service business in Hong Kong that is ancillary to the corporation's principal business, or an accounting or legal professional. Upon RA 13 coming into effect, such a trustee would become dually licensed by the Companies Registry and the SFC and subject to supervision by both the Companies Registry and the SFC for compliance with customer due diligence and record-keeping requirements prescribed under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (AMLO) (Cap. 615, Laws of Hong Kong).

<sup>41</sup> This refers to guidance similar to the Companies Registry's guidance provided in Q6 of the Frequently Asked Questions (FAQs) for Trust Companies which explains that a TCSP licensee acting as trustee of a CIS in trust form is expected to carry out CDD on the CIS as customer, but is also allowed to carry out CDD on the CIS manager as customer in lieu of the CIS when certain prescribed conditions are met.

<sup>42</sup> Cap. 571AL, Laws of Hong Kong.

<sup>43</sup> Hong Kong Securities Clearing Company Limited is the operator of the Central Clearing and Settlement System.

<sup>44</sup> HKMA is the operator of the Central Moneymarkets Unit.

<sup>45</sup> RIs, ie, authorised institutions registered with the SFC to conduct securities intermediary activities, are required to comply with the HKMA's Guideline on Anti-Money Laundering and Counter-Financing of Terrorism (For Authorised Institutions) and have regard to, amongst other requirements, paragraph 4.1.6 of the AML/CFT Guideline.

<sup>46</sup> Paragraph 4.1.6 of the AML/CFT Guideline.

- (b) the underlying investors of the relevant CIS have no control over the management of the scheme's property; and
  - (c) the management company has put in place measures to carry out CDD (either by itself, or through an institution appointed by the relevant CIS or the management company) on all the investors of the relevant CIS in accordance with requirements similar to those set out in Schedule 2 to the AMLO<sup>47</sup>.
89. In addition, if the relevant conditions in section 4 of Schedule 2 to the AMLO are met, the depositary may apply simplified customer due diligence (SDD) measures<sup>48</sup> to the CIS, or the management company, as the case may be.
90. The above approach is in line with the Companies Registry's guidance and AML/CFT requirements in other major jurisdictions such as Singapore<sup>49</sup>. The SFC also understands that it is not uncommon for an SFC-licensed management company to put in place arrangements to ensure that CDD is conducted on all the investors of an SFC-authorized CIS which it manages.
91. The SFC will issue FAQs to provide the guidance described above when the RA 13 regime becomes effective.
92. For the avoidance of doubt, an RA 13 depositary must conduct ongoing monitoring<sup>50</sup> of the business relationship with the relevant CIS or the management company in accordance with Chapter 5 of the AML/CFT Guideline.
93. To address the comments on the OTCD Reporting Rules, the HKMA and the SFC which jointly administer the OTC derivative reporting regime, propose to exempt certain RA 13 depositaries from the OTCD reporting requirements under specific circumstances. Proposed amendments to the OTCD Reporting Rules are set out in Part II and Appendix A.

### Proposed implementation and transitional arrangements

**Question 13: Do you agree with the proposed transitional arrangements? If not, please explain your views.**

<sup>47</sup> In ascertaining whether the condition under this paragraph (c) is met, a depositary may, for example, obtain information from the management company by way of a due diligence questionnaire, or obtain the service level agreement with the appointed institution or operational procedures to facilitate its assessment.

<sup>48</sup> Where SDD measure can be applied, the RA 13 depositary will not be required to identify and take reasonable measures to verify the identity of the beneficial owners of the customer that is the relevant CIS (including any underlying investors who own or control more than 25% interest of the CIS) or the management company.

<sup>49</sup> In Singapore, a trustee of a public CIS is allowed to treat the management company of the CIS as the customer for CDD purposes when the manager is subject to the Singapore AML/CFT regulations and responsible for conducting CDD on the investors of the CIS it manages.

<sup>50</sup> The ongoing monitoring should include (i) periodic and trigger event-driven reviews of the customer's CDD records to ensure the documents, data and information are up-to-date and relevant (including information obtained for the purposes of ascertaining whether the conditions for treating the management company as customer for CDD purposes are still met), and (ii) monitoring transactions carried out for the customer, including the handling of scheme property of the relevant CIS associated with trade settlement and the subscription and redemption of the CIS units or shares, to detect any unusual or suspicious transactions.

### *Public comments*

94. There were requests to:
- (a) extend the proposed transitional period from around 12 to 18 months (from the gazettal date) to 24 months due to the complexity of the proposed licensing regime and the additional obligations;
  - (b) extend the proposed two-month deadline for submitting licence or registration applications<sup>51</sup> to six months because of the need to become familiar with the licensing regime, assess the application needs and comply with the documentation requirements; and
  - (c) with respect to the proposed “grandfathering” arrangement<sup>52</sup> for existing staff of depositaries, remove the one-off requirement to attend a five-hour course (which was proposed as an alternative to passing related licensing examinations) when these individuals seek to be licensed or registered for RA 13 during the transitional period.

### *The SFC’s response*

95. The SFC takes the view that a transitional period of 18 months will be sufficient, given the extended discussions and continuous engagement with market participants.
96. However, the SFC will extend the application submission deadline to four months from the gazettal date<sup>53</sup>. If a depositary foresees that it may not be able to meet this general expectation due to exceptional circumstances, it should approach the SFC or the HKMA to discuss the specifics as soon as practicable.
97. The SFC considers that the proposed five-hour training course (in lieu of examination) applicable to existing practitioners under the grandfathering arrangement is essential for the licensed individuals or relevant individuals to demonstrate that they possess the required regulatory knowledge in respect of RA 13. This is part of the fit and proper requirements which they need to satisfy for licensing purposes. We will therefore maintain this arrangement as an alternative to sitting examinations during the transitional period.

### **Conclusion and way forward**

98. In view of the general support for the proposed regulatory framework of RA 13, the SFC has engaged in continuous discussions with the depositary industry to formulate the details to implement the regime. The proposals in Part II have taken these discussions into account.

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<sup>51</sup> This refers to the proposed requirement in paragraph 45 of the 2019 Consultation – prospective applicants (including firms and individuals) are expected to submit their applications to the SFC, or to the HKMA as the case may be, together with supporting documents within two months from the date of gazettal of the notice published by the Financial Secretary to amend Schedule 5 to the SFO.

<sup>52</sup> Paragraph 47 of the 2019 Consultation.

<sup>53</sup> The gazettal date refers to the date of gazettal of the notice published by the Financial Secretary to amend Schedule 5 of the SFO.

## Part II – Further consultation on proposed amendments to subsidiary legislation and SFC codes and guidelines to implement the regulatory regime for depositaries of SFC-authorized collective investment schemes

### Section 1 – Proposed approach for defining RA 13

99. In view of the comments<sup>54</sup> received, we propose RA 13 to be an activity of providing depositary services for a *relevant CIS*, ie, –

- (a) custody and safekeeping of *relevant CIS property*; and
- (b) oversight of the relevant CIS to ensure that it is operated in accordance with the provisions of its constitutive documents,

whereby the person providing these services –

- (i) in the case of a relevant CIS that is constituted in the form of a trust, is the person appointed as a trustee pursuant to the trust deed which constitutes or governs the relevant CIS; or
- (ii) in the case of a relevant CIS that is constituted in a form other than a trust, is the person appointed as the custodian (by whatever name called), the appointment of which is pursuant to a written agreement entered into by the person with or in respect of the relevant CIS,

but does not include the provision of such services by a delegate or sub-delegate of that person, whether or not such delegate or sub-delegate is appointed by the person.

100. To exclude depositaries of pure MPF products, we further propose that:

a *relevant CIS* would be a collective investment scheme which is authorised under section 104 of the SFO other than –

- (a) a registered scheme or its constituent fund as each is defined in section 2(1) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485); or
- (b) an approved pooled investment fund as defined in section 2 of the Mandatory Provident Fund Schemes (General) Regulation (Cap. 485 sub. leg. A) which is offered only to:
  - (i) professional investors;
  - (ii) employers as defined in section 2(1) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485);
  - (iii) registered schemes or their constituent funds as defined in section 2(1) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485);

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<sup>54</sup> Paragraphs 19 to 26 of Part I.



- (iv) occupational retirement schemes as defined in section 2(1) of the Occupational Retirement Schemes Ordinance (Cap. 426);
- (v) pooling agreements as defined in section 2(4) of the Occupational Retirement Schemes Ordinance (Cap. 426); or
- (vi) other approved pooled investment funds.

101. We also propose definitions for the following terms:

(a) *Relevant CIS property*—

- (i) in relation to a relevant CIS constituted in the form of a trust (other than a real estate investment trust), any property held upon or subject to trust pursuant to any trust deed which constitutes or governs the relevant CIS;
- (ii) in relation to a relevant CIS which is a real estate investment trust—
  - (A) any property held upon or subject to trust pursuant to any trust deed which constitutes or governs the relevant CIS; and
  - (B) any property owned, controlled or held by any special purpose vehicle that is owned or controlled under the relevant CIS in accordance with the Code on Real Estate Investment Trusts published by the Commission under section 399 of the Ordinance;
- (iii) in relation to a relevant CIS constituted in any other form, any property of the relevant CIS.

(b) *Constitutive documents*, in relation to a relevant CIS, means the documents that govern the formation or constitute the relevant CIS and documents pursuant to which obligations relating to the custody and safekeeping of any relevant CIS property or oversight of the operations of the relevant CIS are imposed.

**Question 1: Do you have any comments on the proposed approach for the definition of RA 13?**

## Section 2 – Proposed amendments to subsidiary legislation

102. The following summarises proposed amendments to subsidiary legislation which will need to be amended for the implementation of RA 13.



The Securities and Futures (Client Securities) Rules (CSR)<sup>55</sup> and the Securities and Futures (Client Money) Rules (CMR)<sup>56</sup>

103. The CSR and the CMR respectively set out requirements to ensure the proper handling of (i) client securities and securities collateral which are either listed or traded on SEHK or are interests in SFC-authorized CIS and (ii) client money, which is received or held in Hong Kong by or on behalf of an intermediary<sup>57</sup> (or its associated entity) in the course of (or in relation to) the conduct of any RA for which the intermediary is licensed or registered.
104. The manner in which a depositary holds assets, including money and securities and its obligations in relation to these assets are strictly governed by documents under which the relevant CIS is constituted, the relevant Product Codes and other regulatory requirements.
105. To better cater for the operations of an RA 13 depositary, we propose to add new parts in the CSR (Part 2A) and CMR (Part 3), as well as consequential amendments that are specifically applicable to RA 13, so that the obligations apply in respect of scheme securities<sup>58</sup> and scheme money received or held in Hong Kong by the RA 13 depositaries and their associated entities in the course of the conduct of RA 13.
106. Sections 1 and 2 of Appendix A set out indicative drafts of the proposed amendments to the CSR and CMR.

The Securities and Futures (Keeping of Records) Rules (KRR)

107. The KRR<sup>59</sup> specify the records that intermediaries and their associated entities are required to keep in relation to the RAs and client assets.
108. Amendments to the KRR are proposed so that record keeping obligations apply to RA 13 intermediaries and their associated entities.
109. Section 3 of Appendix A sets out an indicative draft of the proposed amendments to the KRR.

Other subsidiary legislation

110. The following consequential or non-substantive amendments are proposed:
  - (a) Securities and Futures (Financial Resources) Rules (FRR) – as proposed in the 2019 Consultation, amendments will be made to require an RA 13 LC to have a minimum paid-up share capital of HK\$10,000,000 and a minimum required liquid capital of HK\$3,000,000. In addition, where any amount of scheme money and certain other money including subscription and redemption proceeds received or held by an RA 13 LC has not been paid into a segregated

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<sup>55</sup> Made under section 148 of the SFO.

<sup>56</sup> Made under section 149 of the SFO.

<sup>57</sup> The CMR applies to licensed corporations and their associated entities.

<sup>58</sup> Securities either listed or traded on SEHK or interests in SFC-authorized CIS in Hong Kong which constitute relevant CIS property.

<sup>59</sup> Made under section 151 of the SFO.

bank account, the RA 13 LC will be required to treat that non-segregated amount of money as its ranking liabilities under a new section 37A.

- (b) Securities and Futures (Insurance) Rules<sup>60</sup> (Insurance Rules) – to specify an insured amount of “nil” for RA13 in Part 2 of Schedule 2.
- (c) Securities and Futures (Accounts and Audit) Rules<sup>61</sup> (Accounts and Audit Rules) – to make consequential amendments so that auditors of an RA 13 LC or its associated entity shall form opinions in relation to the new provisions in the CSR, CMR and KRR which are applicable to RA 13 LCs or their associated entities.
- (d) Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules<sup>62</sup> (Contract Notes Rules) – to disapply the Contract Notes Rules to RA 13 intermediaries and their associated entities. Since management companies should retain records of investment transactions executed for the relevant CIS and the movement of the relevant CIS property under their management, depositaries should not be required to provide similar information to the management companies. Therefore, we propose that RA 13 depositaries be exempted from the Contract Notes Rules. A similar approach is currently adopted for management companies.

111. Indicative drafts of the proposed amendments are set out in Section 4 of Appendix A.

#### Part IIIA of the SFO – the OTC derivative reporting and clearing regime

112. Under the current OTC derivative reporting regime, trustees are generally not subject to the mandatory reporting requirements<sup>63</sup> under the OTCD Reporting Rules which apply to, among others, LCs and authorised financial institutions (AFIs)<sup>64</sup>. Once the RA 13 regime commences, unless exempted, RA 13 depositaries would be subject to the mandatory reporting requirements which are triggered if a LC or RI is a counterparty to a specified OTC derivative transaction or has conducted the transaction in Hong Kong<sup>65</sup>.
113. To preserve the existing policy of the OTC derivative reporting regime, the HKMA and SFC propose that an RA 13 depositary which is a counterparty to an OTC derivative transaction in its capacity as a trustee of a relevant CIS will be carved out from the reporting obligation<sup>66</sup>. Transactions entered into by the RA 13 depositary in other capacities will not be exempted from the mandatory reporting requirements. Hence we

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<sup>60</sup> Cap. 571AI, Laws of Hong Kong.

<sup>61</sup> Cap. 571P, Laws of Hong Kong.

<sup>62</sup> Cap. 571Q, Laws of Hong Kong.

<sup>63</sup> Although trustees may be counterparties to OTCD transactions, they are currently not subject to the reporting obligations as most of them are not LCs. Currently, the reporting obligations only apply to those trustees which are AFIs.

<sup>64</sup> Under section 101B of the SFO, a “prescribed person” (which is defined to include an AFI or an LC) must report to the HKMA specified OTCD transactions in certain circumstances.

<sup>65</sup> The reporting obligation is triggered if circumstances under either the “counterparty” limb or the “conducted in Hong Kong” limb are met. Please refer to the Frequently Asked Questions on the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules (latest version dated 23 November 2021) ([https://www.sfc.hk/-/media/EN/files/SOM/OTC/FAQs\\_Phase-2-Reporting\\_20211123.pdf](https://www.sfc.hk/-/media/EN/files/SOM/OTC/FAQs_Phase-2-Reporting_20211123.pdf)) for details.

<sup>66</sup> Depositaries acting in the capacity of global custodians should not be caught under either limb of the reporting obligations in rules 10, 11 and 12 of the OTCD Reporting Rules. Therefore, they do not need to be exempted.

do not propose to provide an exemption from the reporting obligation which arises from the “conducted in Hong Kong” limb<sup>67</sup>.

114. It is further noted that, like other exempt persons under the OTCD Reporting Rules, an RA 13 depository will still be subject to the relevant record keeping requirements, including the requirement to keep records which are sufficient to demonstrate that it is a counterparty to the transaction in its capacity as a trustee of a relevant CIS.
115. An indicative draft of the proposed amendments to the OTCD Reporting Rules is set out in Section 5 of Appendix A.
116. Separately, upon the implementation of the RA 13 regime, an RA 13 depository that is currently not a prescribed person<sup>68</sup> will also be subject to the Securities and Futures (OTC Derivative Transactions – Clearing and Record Keeping Obligations and Designation of Central Counterparties) Rules<sup>69</sup> (OTCD Clearing Rules).
117. However, the clearing obligation will only be triggered in respect of a prescribed person when the specified conditions are met, including when the person’s applicable total position in relevant OTC derivative transactions reaches a prescribed threshold (Clearing Threshold), which currently stands at US\$20 billion. Based on an assessment of relevant factors, including the operations of the OTC derivative clearing regime since commencement, the HKMA and SFC propose that no change be made to the OTCD Clearing Rules pursuant to the implementation of the RA 13 regime.

**Question 2: Do you have any comments on the proposed amendments to the CMR?**

**Question 3: Do you have any comments on the proposed amendments to the CSR?**

**Question 4: Do you have any comments on the proposed amendments to the KRR?**

**Question 5: Do you have any comments on the proposed amendments to the FRR, Insurance Rules, Accounts and Audit Rules and Contract Notes Rules?**

**Question 6: Do you have any comments on the proposed amendments to the OTCD Reporting Rules?**

**Question 7: Do you think the proposed carve-out under the OTCD Reporting Rules is sufficient? If not, please give justifications and details.**

<sup>67</sup> As it is not anticipated that an RA13 depository would be conducting OTC derivative transactions in its capacity as a trustee of a relevant CIS, an exemption is considered unnecessary.

<sup>68</sup> As specified in paragraph (b) of the definition of “prescribed person” under section 101A of the SFO, in relation to the clearing obligation, a prescribed person includes an authorised institution and an approved money broker as defined under the Banking Ordinance, and a licensed corporation as defined under the SFO.

<sup>69</sup> Cap. 571AN, Laws of Hong Kong.

## Section 3 – Proposed amendments to SFC codes and guidelines

### Proposed Schedule 11 to the Code of Conduct

118. In addition to the changes summarised in Part I of this paper, amendments have also been proposed to Schedule 11 to address matters which are more appropriate to be dealt with in non-statutory regulations to ensure that all the relevant aspects of CIS operations are taken care of for better investor protection. These relate mainly to the handling of money and other property of the relevant CIS which may not fall under the proposed scope of the CSR and CMR for RA 13<sup>70</sup>.

**Question 8: Do you have any comments on the proposed amendments to the revised draft Schedule 11?**

### Product Codes and Fund Manager Code of Conduct (FMCC)

119. Consequential amendments to the UT Code, PRF Code and REIT Code are necessary to reflect the implementation of RA 13 and to address comments from the 2019 Consultation<sup>71</sup>.
120. Minor consequential amendments are also proposed to be made to the FMCC to reflect the introduction of RA 13.
121. Section 1 of Appendix C sets out the proposed amendments to the UT Code, PRF Code, REIT Code and FMCC.

**Question 9: Do you have any comments on the proposed amendments to the product codes and FMCC?**

### Guidelines on Competence

122. The Guidelines on Competence set out matters which the SFC will normally consider in assessing whether a corporation or an individual is competent to carry on any RA. The existing general principles and key elements of the competence requirements for corporations<sup>72</sup> are applicable to all intermediaries, regardless of which type(s) of RA they carry on. We therefore propose that the same requirements will also apply to corporations which carry on RA 13.
123. In considering whether individuals are competent to carry on RA 13, unless they are grandfathered under transitional arrangements (please see paragraph 97 above), they will be required to satisfy the relevant competence requirements under the Guidelines on Competence, including, among other things, passing the related licensing examinations, where applicable. The SFC is in discussions with the Hong Kong

<sup>70</sup> For example, money and property of the relevant CIS held overseas.

<sup>71</sup> No amendments are necessary to the OFC Code as custodians of public OFCs must comply with requirements in the SFC Products Handbook, including the UT Code.

<sup>72</sup> Paragraphs 3.1 and 3.2 of the Guidelines on Competence.

Securities and Investment Institute on the development of new examination papers and modification of the existing examination papers to cover industry and regulatory knowledge in relation to RA 13. We propose that the Guidelines on Competence be amended to provide for the relevant Recognised Industry Qualifications and Local Regulatory Framework Papers in relation to RA 13.

124. Section 2 of Appendix C sets out the proposed amendments to the Guidelines on Competence.

**Question 10: Do you have any comments on the proposed amendments to the Guidelines on Competence?**

### Seeking comments

125. The proposals in Part II of this paper have taken into account extensive discussions with the depositary industry.
126. The SFC welcomes comments from the public and the industry on the proposals in Part II of this paper. The feedback received will help finalise the amendments to the subsidiary legislation and SFC codes and guidelines for the introduction of RA 13. Please submit comments to the SFC in writing by no later than 30 April 2022.

## Proposed amendments to subsidiary legislation

Section 1 – Indicative draft of proposed amendments to the CSR

Section 2 – Indicative draft of proposed amendments to the CMR

Section 3 – Indicative draft of proposed amendments to the KRR

Section 4 – Indicative drafts of proposed amendments to the FRR, Insurance Rules, Accounts and Audit Rules and Contract Notes Rules

Section 5 – Indicative draft of the proposed amendments to the OTCD Reporting Rules



## Appendix B

Revised draft of Schedule 11 to the Code of Conduct for Persons  
Licensed by or Registered with the Securities and Futures Commission



## Appendix C

### Proposed amendments to SFC codes and guidelines

Section 1 – Proposed amendments to the UT Code, PRF Code, REIT Code and FMCC

Section 2 – Proposed amendments to the Guidelines on Competence



## List of respondents

**(In alphabetical order)**

- 1. Baker McKenzie**
- 2. Clifford Chance**
- 3. Eversheds Sutherland**
- 4. Hong Kong Trustees' Association**
- 5. State Street Corporation**
- 6. Submission of one respondent is published on a “no-name” basis**
- 7. Submission of three respondents are withheld from publication**