

Consultation Paper  
on Investment Incidental Advice  
Provided by Solicitors and Accountants

**Hong Kong  
April 2000**

## FOREWARD

This Consultation Paper is published by the Securities and Futures Commission to solicit comments on its proposed practice note on incidental investment advice provided by solicitors and accountants. Comments are invited from all interested persons.

Comments should be addressed to the Licensing Department of the Securities and Futures Commission, 12<sup>th</sup> floor, Edinburgh Tower, 15 Queen's Road Central, The Landmark, Hong Kong and should be submitted **on or before 30 April 2000**.

This Consultation Paper can also be found on the SFC's website: [www.hksfc.org.hk](http://www.hksfc.org.hk). Comments can be submitted by e-mail to [licinad@hksfc.org.hk](mailto:licinad@hksfc.org.hk).

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## **Purpose**

1. Currently, solicitors and accountants, pursuant to the exemption contained in section 2(1) of the Securities Ordinance (“SO”), are not required to be registered as investment advisers when providing investment advice incidental to the practice of their professions (“incidental advice”).
2. This Practice Note sets out the Commission’s views on when advice given on securities by solicitors and accountants may properly be considered incidental advice.
3. This Practice Note does not have the force of law.

## **Statutory Basis of the Incidental Advice Exemption**

4. Under section 2(1) of the SO, subject to certain exceptions, “investment adviser” is defined to mean any person who –
  - (a) for remuneration carries on a business of advising other persons concerning securities;
  - (b) for remuneration as part of a regular business issues analyses or reports concerning securities; or
  - (c) for remuneration pursuant to a contract or arrangement with a client, undertakes on behalf of the client the management of a portfolio of securities, including the arranging of purchases, sales, or exchanges of securities through a dealer or exempt dealer.

and, in the case of a corporation which is an investment adviser, includes any director of the corporation who actively participates in, or is in any way directly responsible for the supervision of, the corporation's business as an investment adviser; but does not include –

- (i) a licensed bank;
- (ii) a solicitor or professional accountant whose carrying on business as an investment adviser is wholly incidental to the practice of his profession (“incidental advice exemption”);
- (iii) the proprietor or publisher of, any contributor to, a bona fide newspaper, magazine, journal, or other periodical publication that is generally available to the public, otherwise than on subscription, who, only in that bona fide newspaper, magazine, journal, or periodical publication, advises other persons concerning securities, or issues analyses or reports concerning securities, not being the proprietor or publisher of, or a contributor to, a newspaper, journal, magazine, or other periodical publication whose principal or only object is to advise others concerning securities or to issue analyses or reports concerning securities;
- (iv) a dealer or exempt dealer to the extent that his giving of investment advice is incidental to his carrying on business as a dealer or exempt dealer;
- (v) a trustee company registered under Part VIII of the Trustee Ordinance (Cap.29);
- (vi) an exempt investment adviser;
- (vii) a recognized clearing house.

5. The word “securities”, under section 2(1) of the SO, means any shares, stocks, debentures, loan stocks, funds, bonds or notes of, or issued by, any body, whether incorporated or unincorporated, or of any government or local government authority; and includes:
- (a) rights, options or interests (whether described as units or otherwise) in or in respect of any of the foregoing;
  - (b) certificate of interest or participation in, or temporary or interim certificates for, receipts for, or warrants to subscribe to or purchase, any of the foregoing;  
or
  - (c) any instruments commonly known as securities;

but does not include, among other things, any shares, or debentures of any company which is a private company within the meaning of section 29 of the Companies Ordinance.

### **Concern of the Commission**

6. The Commission is concerned that some solicitors and accountants, in rendering their respective professional services, recommend that their clients purchase or dispose of particular securities and give advice on matters/transactions falling within the Hong Kong Codes on Takeovers and Mergers and Share Repurchases on the pretext that these acts are incidental to the practice of their professions. In the Commission’s view, solicitors and accountants, in carrying out these acts, may have gone beyond what might reasonably be construed as wholly incidental to their professional services. For the avoidance of doubt, the Commission considers it necessary to clarify what constitutes activities wholly incidental to the practice of the professions by way of a practice note.

## **Guidelines for Relying on the Incidental Advice Exemption**

7. The Commission is of the view that a solicitor or an accountant can rely on the incidental advice exemption and will not be required to be licensed when all of the following requirements are satisfied:
  - (a) the advice given on securities forms a normal or a wholly incidental part to the overall services provided; and
  - (b) no discrete fee is charged for the wholly incidental advice given as a part of the general practice of the solicitor or accountant.

## **Normal or Wholly Incidental Part of the Overall Services**

8. The practitioners of the legal and accounting professions are in a better position than the Commission to determine what activities would form the bases of normal legal and accounting services. It is therefore inappropriate for the Commission to list out such activities. However, we feel it necessary to set forth our basic understanding of what incidental advice is.
9. Whether or not provision of advice on securities forms a wholly incidental part of the overall services offered by the solicitor or an accountant is a question of fact and is assessed in the light of individual circumstances. However, we are generally of the view that if a solicitor or accountant, in the course of providing his professional services, gives investment advice which is:
  - (a) subordinate to the main purpose for which those services are provided, and in that sense is incidental to the giving of legal or accounting advice;

- (b) general in nature in the sense that such advice would not result in the solicitor or accountant making specific recommendations to the client on a particular stock or investment product; and
- (c) given on an irregular and non-repetitive basis,

such advice will form a wholly incidental part to the overall services offered by the solicitor or accountant.

10. It is highly unlikely that any investment advice provided or held out as a separate or distinct service in the course of the solicitor's or accountant's profession at practise as such will form a normal or wholly incidental part of the overall services provided by him.
11. By way of example, if the solicitor or accountant states in his business cards, letterheads or promotional brochures, that the provision of advice on securities is a distinct service offered by him, such a service is unlikely to be wholly incidental to that solicitor's or accountant's practice.

### **No Discrete Fee**

12. In line with the above requirement, a solicitor or an accountant, in the Commission's opinion, should not charge any discrete fee in providing incidental advice. This means that there should not be any fees charged to the client for the wholly incidental advice either separately or included within the overall fees charged for the provision of normal professional services.

13. For example, if the incidental advice is given in the course of providing tax advice, the client should only be charged with fees for the tax advice and not be charged with a separate fee for the provision of incidental advice.
14. This requirement ensures that provision of incidental advice remains wholly incidental to the overall service provided to the client and does not constitute and is not held out as a discrete service provided to that client.

### **Practical Examples of Incidental Advice**

15. Solicitors and accountants provide a number of services in the course of their practice which are linked to the provision of incidental advice. The following paragraphs set out some of these services and discuss whether solicitors and accountants, in engaging in such activities, are caught by the licensing net and, if so, whether they can rely on the incidental advice exemption by meeting the guidelines contained in above paragraph 7.

### **Mere Referrals**

16. Where a solicitor or an accountant refers his clients to an investment adviser for a referral fee, he is not required to be licensed if he:
  - (a) does nothing more than merely introduce a potential investor to the investment adviser; and
  - (b) does this merely as an incidental part of his principal business.

It should be noted however that where a solicitor or accountant, in return for remuneration, refers his clients to a dealer, he is required to be licensed under section 3(1A) of the SO.

17. Since there is no direct or implicit recommendation made on securities in the course of the referral, the solicitor or accountant making the referral is not considered to be providing investment advice and is therefore not required to be licensed. Consequently, there is no need for him to rely on the incidental advice exemption.
18. However, if the referring solicitor or accountant provides any direct or indirect investment advice as a part of introducing his clients, for example, if he discusses, either in general or in particular, the merits of investing in securities, then he is prima facie providing investment advice and should be licensed unless he can demonstrate that the advice fall within the incidental advice exemption.
19. The fact that the referring solicitor or accountant, instead of receiving a discrete referral fee, is remunerated under a profit-sharing arrangement for making the referrals is not relevant. As long as the solicitor or accountant provides direct or indirect investment advice in the course of the referral and receives remuneration for the referral, he is prima facie required to be licensed.
20. Moreover, it is the Commission's view that a solicitor or an accountant is generally unable to rely on the incidental advice exemption when making referrals under a profit-sharing arrangement. This is because a solicitor or an accountant is usually required, under such an arrangement, to make regular referrals consistently, which is in direct contrast to one of the indicia of incidental service that they be provided on an irregular and non-repetitive basis.

## **Portfolio Management**

21. A client may frequently ask his accountant to review the combinations of various components of an investment portfolio. That may be proper and necessary, for example, to provide tax advice. If the advice given by the accountant goes beyond a very general recommendation relating to securities and identifies any specific securities for the client to hold or dispose of in the portfolio, he is in effect providing a portfolio management service for his client. The accountant is required to be licensed before he can provide such a service.
22. However, if the advice on securities is provided as part of a review of, say, the taxation consequences of the portfolio, the accountant may be able to rely on the incidental advice exemption and be exempt from the licensing requirements.
23. In similar vein, a client may ask his solicitor to review the investments in the portfolio from the perspective of their relative strength in terms of legal enforceability. The legal advice may include direct or indirect recommendations to hold or dispose of some securities in the portfolio. In this case, a solicitor will generally be able to rely on the incidental advice exemption to exempt himself from the licensing net.

## **Corporate Finance Advisory**

24. Corporate finance advisory activities may include:
  - (a) implementing or advising on takeovers, mergers, amalgamations, acquisitions, disposals, demutualisations, project financing, management buyouts, corporate restructurings, initial public offerings, rights issues, placements and other fund raising exercises;

- (b) giving advice on compliance with or in respect of relevant financial legislation and regulations including the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and the Hong Kong Codes on Takeovers and Mergers and Share Repurchases; and
  - (c) any other activities or business commonly accepted in the market as corporate finance.
25. The Commission considers that when a solicitor or an accountant provides professional services on corporate finance, certain of these services can reasonably be expected to be provided by the solicitor or accountant in the ordinary course of practising his profession. Such services may include but are not limited to:
- (a) drafting and advising on relevant contractual documentation, circulars, announcements, due diligence, advising on market and other practice; and
  - (b) dealing with regulatory bodies and providing general strategic advice in the context of legal, practical and market requirements.

In our view, the provider of these services will not normally fall within the licensing requirements if the performance of such activities is a normal part of his professional practice. To the extent that the advice is provided on securities as part of the provision of the above services, the solicitor or accountant may be able to rely on the incidental advice exemption.

26. The Commission however is of the view that advice given on public takeovers, mergers and the like is primarily in relation to securities and would fall within the scope of the activities of an adviser. In respect of advising an offeror on initial public offerings, and other securities issues on offer, the solicitor or accountant might be considered to be dealing in securities if his acts amount to inducing his clients to enter into securities transactions. Depending on the circumstances involved, a solicitor or an accountant who gives such advice in the course of his profession might be required to be licensed unless he can justify his exclusion from the licensing net by relying on the incidental advice exemption.

### **Advice on Underlying Securities in a Collective Investment Scheme Including Mandatory Provident Fund Schemes**

27. A solicitor or an accountant, engaged in a business of providing advice to potential investors on the relative merits, from an investment perspective, of collective investment schemes including Mandatory Provident Fund Schemes (“MPF Schemes”), may require a licence if the advice is provided in relation to comparing advantages and disadvantages of investing in different underlying products, and in so doing, the solicitor or accountant makes reference to specific securities; or comments on their performance, merits and demerits, etc. Therefore, unless the advice on the schemes can satisfy the guidelines set out in above paragraph 7, the solicitor or accountant must be licensed before he can provide such a service.
28. On the other hand, a licence is generally not required in situations where advice is simply given on the structure of MPF Schemes or other collective investment schemes or where generic advice is given on the constituent funds without advising on the underlying products that are securities.