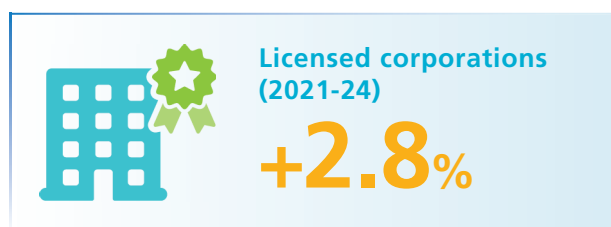


Intermediaries

We set standards and qualifying criteria for corporations and individuals licensed to operate in our markets under the Securities and Futures Ordinance (SFO). As part of our ongoing supervision, we conduct on-site inspections and off-site monitoring of licensed corporations¹ (LCs) and explain our regulatory focus and concerns to the industry. We closely monitor market and technological developments and adapt our regulatory approach to ensure our gatekeeping and supervisory functions remain effective.



Licensing corporations and individuals

As of 31 March 2024, the number of licensees and registrants totalled 47,851. With the continuous expansion of the financial landscape, there were 84 licensed firms carrying out regulated business in robo-advisory, virtual banking, virtual asset (VA) related activities and multi-family offices.



Mr Keith Choy, Interim Head of the Intermediaries Division, at the Hong Kong Web3 Festival 2023

The number of LCs in Hong Kong stood at around 3,250. Approximately 15% of the LCs were controlled by foreign financial groups, mainly from the US, UK, and the European Union. In addition, a number of overseas-based fund managers, which manage pension funds and private equity funds, have established their business activities in Hong Kong over the years. The number of licensed individuals stayed at around 45,000 during the period, about 35% of which were employed by foreign-controlled LCs.

Licensees

	Corporations [^]		Representatives		Responsible Officers		Total [^]		
	As at 31.3.2024	As at 31.3.2023	As at 31.3.2024	As at 31.3.2023	As at 31.3.2024	As at 31.3.2023	As at 31.3.2024	As at 31.3.2023	Change
Stock exchange participants	545	559	11,259	11,358	2,003	2,075	13,807	13,992	-1.3%
Futures exchange participants	86	91	373	737	113	143	572	971	-41.1%
Stock exchange and futures exchange participants	74	83	5,283	5,269	619	668	5,976	6,020	-0.7%
Non-stock/non-futures exchange participants	2,541	2,521	18,159	18,080	6,684	6,598	27,384	27,199	0.7%
Total	3,246	3,254	35,074	35,444	9,419	9,484	47,739	48,182	-0.9%

[^] These figures exclude 112 registered institutions as at 31 March 2024 and 31 March 2023.

¹ Broadly, LCs include securities and futures brokers, leveraged forex traders, fund managers, investment advisers, sponsors and credit rating agencies.



During the year, we received around 7,300 new licence applications, comprising more than 7,000 individuals and 220 corporations. It is noteworthy that the number of new corporate licence applications received in this financial year substantially increased by 22% as compared to last year.

We approved 164 new corporate licence applications and around 6,700 individual licence applications. The total number of applications increased by 5% from last year. Amongst the newly approved corporate applications, 85% of them applied for Type 9 (asset management) regulated activity (RA) and 63% applied for Type 4 (advising on securities) RA. As of 31 March 2024, the number of firms licensed for Type 9 RA increased by 2.6% to 2,140.

To support the industry, we have waived the annual licensing fees for all intermediaries and licensed individuals in Hong Kong for the 2024-25 financial year. This measure will help the industry save approximately HK\$250 million.

Enhancing our regulatory regime

Stepping up risk management for dealing in futures contracts

In August 2023, we concluded a public consultation on proposed guidelines which set out a comprehensive risk management framework to ensure licensed futures brokers' resilience in volatile markets.

Effective February 2024 after a transitional period of six months, the guidelines set out our requirements for commodity futures trading, client credit risk management, concessionary margining, safeguarding client assets and stress testing.

Consulting on guidelines for market soundings

In October 2023, we launched a consultation on proposed guidelines for market soundings to assist intermediaries in their compliance with the general principle to conduct their business activities honestly, fairly and in the best interests of their clients and market integrity during market soundings. The guidelines were based on a thematic review of market soundings we initiated in early 2022 to understand current industry practices and related controls, through surveys to buy-side and sell-side intermediaries and focus group discussions. In the guidelines, we also took into consideration local and overseas market practices and regulatory requirements as well as information and preliminary feedback from intermediaries during the thematic review. The consultation ended in December 2023 and we are analysing the responses.

² For granting an approval in principle; the change is on a year-on-year basis. Electronic submission via WINGS became mandatory from 1 April 2022.

Financial position of the Hong Kong securities industry^a

	As at 31.12.2023	As at 31.12.2022	As at 31.12.2021
Securities dealers and securities margin financiers	1,406	1,439	1,433
Active clients ^b	4,757,112	4,650,024	4,159,100
Balance sheet	(\$ million)	(\$ million)	(\$ million)
Total assets	1,331,829	1,452,449	1,658,553
Total liabilities	850,453	969,051	1,130,341
Total shareholders' funds	481,376	483,398	528,212
(\$ million)	12 months to 31.12.2023	12 months to 31.12.2022	12 months to 31.12.2021
Profit and loss			
Total value of transactions ^c	107,897,497	126,014,719	160,931,088
Net securities commission income	17,113	20,210	31,329
Total operating income	197,239	187,385	217,469
Total overheads and interest expense	172,046	170,730	173,978
Total operating profit	25,193	16,655	43,491
Net profit proprietary trading	3,307	6,211	21,397
Net profit	28,500	22,866	64,888

^a Data were extracted from the monthly financial returns submitted under the Securities and Futures (Financial Resources) Rules by corporations licensed for dealing in securities or securities margin financing.

^b Active clients are clients for whom the LC is required to prepare and deliver monthly statements of account in respect of the relevant reporting month under the Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules.

^c The total value of transactions includes trading in equities, bonds and other securities in Hong Kong and overseas.

Note: Also see Table 8 in Operational Data on page 213 for more details.

Supervising licensed firms

As of 31 March 2024, 3,246 LCs were subject to our supervision. We adopt a front-loaded, risk-based approach to supervising LCs and focus on the greatest threats and the most significant or systemic risks. We closely monitor LCs' operations and risk management, focusing on their business conduct and financial soundness, and carry out stress tests to ensure their resilience, particularly in extreme market conditions. We also provide timely guidance to help intermediaries comply with our regulatory requirements.



On-site reviews

On-site reviews are a key supervisory tool for us to understand LCs' business operations, risk management and internal controls, and to gauge their compliance with legal and regulatory requirements.

During the year, we carried out 234 risk-based on-site inspections. We noted LCs' breaches of our rules and regulations³, mainly the Code of Conduct⁴, Fund Manager Code of Conduct and Anti-Money Laundering Guidelines as well as internal control weaknesses.

This year's thematic inspections covered LCs' selling practices, anti-money laundering and counter-financing of terrorism (AML/CFT) measures and cybersecurity.

Off-site monitoring

We conduct off-site monitoring of LCs' operations by analysing their regulatory filings and intelligence from other sources. We also interact regularly with LCs to assess their financial strength, internal controls and risk management practices.

Breaches noted during on-site inspections³

	2023/24	2022/23	2021/22
Internal control weaknesses ^a	465	430	427
Breach of Code of Conduct ^b	332	243	265
Non-compliance with anti-money laundering guidelines	269	214	301
Failure to safekeep client money	45	26	35
Failure to safekeep client securities	41	27	23
Others	340	290	365
Total	1,492	1,230	1,416

^a Comprised deficiencies in management review and supervision, operational controls over the handling of client accounts, segregation of duties, information management and adequacy of audit trail for internal control purposes, among other weaknesses.

^b Commonly related to risk management, client agreements, safeguarding of client assets and information for or about clients.

³ Please refer to Table 2 of Operational Data on page 208 for details.

⁴ Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

Assessing prudential and conduct risks

Protecting client assets at non-compliant brokers

During the year, we issued restriction notices to three brokers that breached our regulatory requirements in relation to the protection of client assets, which seriously jeopardised the interests of the investing public. In one instance, we obtained a court order to appoint administrators to assume control of a broker suspected of misappropriating client money, review its books and records, and facilitate the orderly return of client assets.

Surveying the sale of non-exchange traded investment products

In September 2023, we and the Hong Kong Monetary Authority (HKMA) published a report on our annual joint survey on the sale of non-exchange traded investment products. The survey results help both regulators better understand market trends, identify risks and strengthen our supervisory work to protect investors.

Our survey found that 371 LCs and registered institutions engaged in the sales of investment products in 2022, with an aggregate transaction amount of \$3,799 billion. Around 35% of those firms recorded an increase in their transaction amount. Money market funds were the top-selling collective investment schemes (CIS), accounting for 61% of the total top five CIS by transaction amount in 2022, up from 33% a year earlier. Bond funds and equity funds followed, accounting for 14% and 7% of the total.

Conducting circularisation exercise and internal control review

As a regular exercise to examine brokers' internal controls over client asset protection, we engaged an independent accounting firm to conduct a circularisation exercise to ascertain the account balances of selected brokers' clients and review the brokers' internal control systems. We notified the industry of the exercise in a January 2024 circular and will share key findings from the exercise where appropriate.

Managing risks in providing IPO subscription services

In November 2023, we published a circular to remind LCs to exercise prudent risk management and controls when providing initial public offering (IPO) subscription and financing services to clients after the launch of FINI⁵. The circular sets out our expected control measures relating to credit risk management, liquidity risk management, safeguarding of client subscription deposits and financial risk management.

Distributing SFC-authorized funds

In October 2023, we issued a circular on our observations of LCs' practices in offering and promoting SFC-authorized funds. The circular also highlighted the legal and regulatory requirements for distributors that offer additional returns or other incentives in promoting such funds.

⁵ The Fast Interface for New Issuance (FINI) platform was launched by Hong Kong Securities Clearing Company for Hong Kong's IPO settlement process in November 2023.

Guidance to the industry

Dealing with sophisticated professional investors

Our July 2023 joint circular with the HKMA guided intermediaries on a streamlined approach to comply with suitability obligations when dealing with sophisticated professional investors. The approach seeks to front-load intermediaries' know-your-client measures when onboarding clients or during regular reviews to ascertain a client's financial situation, investment experience, investment objectives and risk tolerance. For clients who exhibit the degree of sophistication, loss-absorption ability and risk profile of a sophisticated professional investor, they would be allowed to specify the product type and amount they wish to trade without going through their intermediaries' routine assessment and disclosure processes.

This streamlined approach makes it more flexible and efficient for these investors to invest within acceptable parameters. To provide sufficient investor protection, intermediaries are required to establish and maintain effective systems and controls to ensure the streamlined approach operates properly, and the Code of Conduct continues to apply in full force.

Addressing anti-money laundering and terrorist financing risks

Effective June 2023, our amendments to the AML/CFT guidelines provided updated guidance to the industry on the revised statutory provisions under the Anti-

Money Laundering and Counter-Terrorist Financing Ordinance⁶. We also incorporated a new chapter to help the industry address money laundering and terrorist financing risks arising from the distinct characteristics of VAs when engaging in related businesses so as to meet statutory and regulatory requirements. In addition, we updated the AML/CFT self-assessment checklist in November to provide a structured framework for the industry to assess their compliance with key AML/CFT requirements.

Also in November, we hosted two AML/CFT webinars for close to 1,800 management and compliance personnel from LCs to provide updates on major regulatory developments and recent supervisory observations. External speakers⁷ shared the latest scam trends and provided feedback on suspicious transaction reporting as well as an overview of the proliferation financing risk situation in Hong Kong.

Preparing industry for increased connectivity in the Greater Bay Area

In January 2024, we issued a set of guidance and frequently asked questions (FAQs) for LCs which wish to participate in the cross-boundary Wealth Management Connect Pilot Scheme⁸ in the Guangdong-Hong Kong-Macao Greater Bay Area. The guidance and FAQs cover the eligibility criteria for participating LCs and investors, scope of eligible investment products, account opening arrangements, investor quota management, cross-boundary closed-loop fund flow arrangements as well as promotion and sales arrangements.

⁶ Including politically exposed persons, beneficial owner of a trust and the use of a recognised digital identification system for customer due diligence.

⁷ Including speakers from the Commerce and Economic Development Bureau and the Hong Kong Police Force.

⁸ See Products on pages 58-65.

Issuing quick reference guides to help industry understanding

We actively collaborate with the industry to improve their understanding of our licensing regime. The quick reference guides on licensing requirements we issued in March 2023 were well received by the industry.



Quick reference guides on licensing requirements.

The guides set out our requirements in a clear and accessible manner, making it easier for the industry and the public to grasp the key concepts.

Throughout the year, we engaged with stakeholders to promote transparency in our licensing process. At an event hosted by the Hong Kong Securities and Investment Institute in June 2023, we explained our gatekeeping functions, licence approval process and the application of technology such as artificial intelligence in the financial industry. In a seminar hosted by the Hong Kong Investment Funds Association in December 2023, we provided a refresher session to its members covering topics including overseas practitioners visiting Hong Kong to perform RAs, incidental RAs for fund managers and our digitalised licensing process.

Revamping the SFC Public Register

To enable easier access to information about intermediaries' business activities, we introduced a new search function in our Public Register of Licensed Persons and Registered Institutions by corporations' business activities, including VA-related activities, operation of online trading platforms, corporate finance-related activities and the management of public real estate investment trusts.

Embracing innovation with investor safeguards

To promote responsible innovation, we have addressed VA-related activities with proactive and comprehensive policy responses over the years to provide regulatory clarity and consistency. Adhering to the principle of “same business, same risks, same rules”, our regulatory framework aims to capture all dimensions of the public’s interface with VAs to ensure investor protection and tackle the prudential risks to financial institutions.

Regulation

To provide clarity on our expected standards for the new regime for virtual asset trading platform (VATP) operators, we concluded our consultation on the regulatory requirements for licensed VATP operators and the corresponding Guidelines for VATP Operators in May 2023. The new regime under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (AMLO) began in June 2023.

We extended retail access to VAs via SFC-regulated intermediaries partnering with SFC-licensed VATPs in October 2023. This is in line with our policy of allowing retail investors to trade VAs on SFC-licensed VATPs.

In December, we set out the latest requirements for distributing products with exposure to VAs in our updated joint circular^a with the HKMA, including the distribution of related investment products and the provision of dealing, asset management and advisory services in respect of VAs.

We also issued a circular in the same month on requirements applicable to SFC-authorized funds with exposure to VAs of more than 10% of their net asset value, including SFC-authorized VA spot exchange-traded funds (ETFs). These requirements cover the types of eligible VA, platforms for conducting VA transactions, entities responsible for VA custody and the custody standards.

Licensing

As of 31 March 2024, we had approved two licensed VATPs^b under the SFO to provide their services to Hong Kong investors. Their licensing

conditions were modified in August 2023 to allow retail access to their services. During the reporting period, we received 23 VATP applications under the new AMLO regime, four of which were from VATP licence applicants under the SFO, whilst the remainder were new applications.

Protecting investors^c

In February 2024, we published a press release reminding investors to check the regulatory status of VATPs, as VATP operators which had not submitted a licence application to us by 29 February must close down their businesses in Hong Kong by 31 May. The SFC issued another press release on 1 March to remind industry participants and investors of the above key dates, and urged investors to trade VAs only on SFC-licensed VATPs.

Publishing more guidance

To help the industry better understand our requirements and apply for a licence, we issued a wide range of publications, including a Licensing Handbook for VATP Operators, circulars on the implementation of and transitional arrangements for the new regime as well as FAQs on licensing and conduct matters. We introduced fully digitalised licensing application forms to enable potential applicants to apply for a licence online, and we consolidated all relevant materials on a new dedicated webpage for VAs on our website.

Going forward, to promote a vibrant VA ecosystem in Hong Kong, we will keep abreast of market developments in the Fintech space and put in place the necessary regulatory guardrails.



^a We issued joint circulars on intermediaries’ VA-related activities on 20 October 2023 and 28 January 2022. The December 2023 circular supersedes previous versions of this circular.

^b OSL Digital Securities Limited and Hash Blockchain Limited.

^c For more on our VA-related investor protection publicity, see Communications and Education on pages 89-97.

Broadening product variety

We observed financial institutions' growing interest in tokenising traditional financial instruments in global financial markets, with an increasing number of intermediaries exploring the tokenisation^a of securities and distribution of tokenised securities to their clients.

Tokenisation may bring potential benefits to financial markets, particularly in enhancing efficiency and transparency, reducing settlement time and lowering operational costs for traditional finance. Nevertheless, we are also aware of new risks arising from the use of this technology not typically associated with traditional securities, especially ownership and technology risks.

We consider it necessary to provide more guidance on tokenised securities-related activities to help clarify our regulatory expectations for intermediaries engaging in these activities. This also provides more regulatory certainty to support continued innovation with appropriate investor safeguards.



To this end, we issued two circulars to give guidance on tokenised securities-related activities and the tokenisation of SFC-authorized investment products, whilst highlighting how traditional financial institutions should address and manage the risks arising from this new tokenisation technology.

Following our guidance issued in November 2023, the first tokenised SFC-registered private OFC was launched in December, and the first tokenised retail gold product was authorised by us in March 2024.

^a This refers to the creation of blockchain-based tokens that represent, or aim to represent, ownership in certain assets or rights.