

Intermediaries

We set standards and qualifying criteria for corporations and individuals licensed to operate in our markets under the Securities and Futures Ordinance. As part of our ongoing supervision, we conduct on-site inspections and off-site monitoring of licensed corporations (LCs)¹ and explain our regulatory focus and concerns to the industry. We also closely monitor market and technological developments and adapt our approach accordingly.

Licensing

As of 31 March 2022, the number of licensees and registrants totalled 48,401, up 2.6% from last year, including the number of LCs which increased 2.3% to 3,231. During the year, we approved 171 new corporate licence applications. We received a total of 7,163 new licence applications, up 28.5% from the previous year.

Licensed individuals (2019-2022)

+3.3%

Competency framework

In June 2021, we concluded a consultation on updates to the competency framework for intermediaries and individual practitioners. The enhancements included recognising post-graduate diplomas and certificates in designated fields and accepting management experience acquired in the financial industry by responsible officer and executive officer applicants. We also raised the eligibility criteria for individuals advising on matters regulated by the Codes on Takeovers and Mergers and Share Buy-backs. In addition, environmental, social and governance (ESG) was included as a relevant topic for continuous professional training purposes.



Ms Julia Leung, Deputy Chief Executive Officer and Executive Director of Intermediaries, speaks at the Hong Kong Investment Funds Association Annual Conference 2021

The enhanced competency framework, including the revised Guidelines on Competence, Guidelines on Continuous Professional Training and Fit and Proper Guidelines, took effect on 1 January 2022.

Virtual assets

We issued a warning statement in July 2021 to caution against trading stock tokens on unregulated platforms. We also reminded investors of the risks of trading virtual assets on unregulated platforms. In January 2022, we issued a joint circular with the Hong Kong Monetary Authority (HKMA) to provide guidance to intermediaries on distributing virtual asset-related products and engaging in virtual asset dealing and advisory services.

Over-the-counter derivatives regime

In response to market feedback, we clarified the scope of regulated activities under the over-the-counter derivatives licensing regime and carved out activities which are not intended to be covered. The change was enacted in June 2021 under the Securities and Futures and Companies Legislation (Amendment) Ordinance 2021.

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

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Licensees

	Corporations [^]		Representatives		Responsible Officers		Total [^]		Change
	As at 31.3.2022	As at 31.3.2021	As at 31.3.2022	As at 31.3.2021	As at 31.3.2022	As at 31.3.2021	As at 31.3.2022	As at 31.3.2021	
Stock exchange participants	591	595	12,001	11,931	2,163	2,157	14,755	14,683	0.5%
Futures exchange participants	99	108	827	839	178	192	1,104	1,139	-3.1%
Stock exchange and futures exchange participants	93	88	5,101	4,912	680	669	5,874	5,669	3.6%
Non-stock/non-futures exchange participants	2,448	2,368	17,730	16,973	6,379	6,231	26,557	25,572	3.9%
Total	3,231	3,159	35,659	34,655	9,400	9,249	48,290	47,063	2.6%

[^] These figures exclude 111 registered institutions as at 31 March 2022 and 115 as at 31 March 2021.

Digitalised licensing platform

In January 2022, we launched the next generation licensing platform on WINGS² together with a companion mobile application, WINGS Mobile App. The fully digitalised platform provides a one-stop, comprehensive service for users to prepare, electronically sign and submit licensing forms, track the progress of applications, pay licensing fees and communicate directly with the SFC. Online submission of all licensing applications, notifications and regulatory filings via WINGS became mandatory from 1 April 2022.



Video introducing new licensing functions on WINGS

Number of licensing submissions processed via WINGS

38,000

Annual licensing fee waiver

In view of market conditions, we waived the annual licensing fees for over 48,000 intermediaries and licensed individuals for the 2022-23 financial year. This measure will help the industry save approximately \$240 million.

Prudential risks

Data standards for order life cycles

Starting 30 April 2021, brokers whose annual trading turnover on the Stock Exchange of Hong Kong reaches or exceeds 2% of that year's total market trading volume are required to comply with the data standards for order life cycles, which prescribe the minimum content and presentation format of trading-related data submitted by them to the SFC upon request. We are developing test cases and a platform for automating our analysis of trading data submitted by these brokers to alert us to irregular activities and potential non-compliance. Further guidance on the data standards will be provided to the industry based on our findings.

² WINGS is a web-based platform for SFC electronic forms and online submission services launched in January 2019.

Operation of bank accounts

In a June 2021 circular, we reminded LCs of the need to implement effective policies, procedures and internal controls for bank accounts operations, including our expectations regarding bank account signatory arrangements. The controls should ensure the proper safeguard of client money, prompt discharge of liabilities, availability of financial resources and compliance with the regulatory financial resources requirements.

Regulatory enhancements

Management and disclosure of climate-related risks

In August 2021, we released consultation conclusions on amendments to the Fund Manager Code of Conduct (FMCC) to require fund managers managing collective investment schemes (CIS) to take climate-related risks into consideration in their investment and risk management processes and provide investors with appropriate disclosures. We also issued a circular setting out the expected standards for compliance with the amended FMCC. The requirements will be implemented in phases starting from 20 August 2022.

Regulators join forces

To enhance the regulation of intermediaries, we worked together with the HKMA to carry out thematic reviews and surveys and jointly publish circulars and reports on a wide range of topics during the year.

Non-exchange traded investment products

In October 2021, we and the HKMA published the report of our first annual joint survey of the sale of non-exchange traded investment products.

A total of 308 LCs and 64 registered institutions reported selling investment products with an aggregate transaction amount of \$5,700 billion during 2020, with the participation of over 700,000 investors. Structured products accounted for the largest share of the aggregate transaction amount, followed by CIS and debt securities. The findings enable us to better understand market trends, identify risks and coordinate responses to address areas of common concern.



Spread charges

The SFC and the HKMA carried out a concurrent thematic review of intermediaries' spread charges and related practices as well as their disclosure of transaction-related information. In an October 2021 circular, we shared key observations noted from the review and set out expected standards of conduct for handling price improvements.

Virtual assets

A January 2022 joint circular provided guidance for intermediaries which wish to distribute virtual asset-related products and engage in virtual asset dealing and advisory services.

Conduct standards in capital market transactions

In October 2021, we concluded a consultation on conduct requirements for capital market transactions in Hong Kong to clarify the roles of intermediaries and set out the standards expected of them in bookbuilding, pricing, allocation and placing activities to enhance the transparency of the price discovery process and balance the interests of issuers and investors. The new requirements³ will take effect on 5 August 2022.

Anti-money laundering

We issued consultation conclusions in September 2021 on proposed amendments to our anti-money laundering and counter-financing of terrorism (AML/CFT) guidelines to align them with the Financial Action Task Force's standards and provide additional guidance for the implementation of risk-based measures. The revised guidelines came into effect on 30 September 2021, except for new requirements for cross-border correspondent relationships, which became effective on 30 March 2022.

Supervisory approach

We adopt a front-loaded, risk-based supervisory approach focusing on the greatest threats and the most significant or systemic risks. Our supervision of LCs focuses on financial risks and how they conduct business and we closely monitor their operations and risk management. The stress tests we conduct are particularly important in times of extreme market conditions, and we provide timely guidance to help intermediaries comply with 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 gauge their compliance with legal and regulatory requirements. During the year, we carried out 262 risk-based on-site inspections, including those conducted due to the pandemic, and noted more than 1,400 breaches of the SFC's rules.

883

on-site inspections in the past three years

This year's thematic inspections covered intermediary misconduct in listed markets, foreign exchange activities, remote booking, operational and data risk management and asset managers' liquidity risk management.

Off-site monitoring

We conduct off-site monitoring by analysing the information in regulatory filings and intelligence from other sources. We also maintain regular interaction to assess LCs' financial strength, internal controls and risk management practices.

Mainland property developers' credit events

Given the financial distress faced by some Mainland property developers during the year, we conducted stress tests to assess LCs' risk exposures to the sector and the potential financial impact. We also made enquiries to understand LCs' exposures to shares and bonds related to these developers and requested LCs under Mainland property developer groups to take risk mitigation measures. In a coordinated enquiry with the HKMA, we obtained information from intermediaries about their clients' outstanding positions in, and selling practices concerning, a major developer's bonds.

Business email compromise

In March 2022, we issued a circular to summarise our observations of control deficiencies in instances of business email compromise schemes⁴ and provide our expected standards. The circular highlighted the importance for LCs to verify clients' identities before acting on their instructions and establish procedures to identify and follow up on red flags.

³ Amendments to the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission and the Guideline to sponsors, underwriters and placing agents involved in the listing and placing of GEM stocks.

⁴ A type of cyber fraud where fraudsters posing as known business contacts dupe unwary staff into sending them money or sensitive information.

Breaches noted during on-site inspections

	2021/22	2020/21	2019/20
Internal control weaknesses ^a	427	515	451
Breach of Code of Conduct ^b	265	262	273
Non-compliance with anti-money laundering guidelines	301	208	331
Failure to safekeep client money	35	35	42
Failure to safekeep client securities	23	28	31
Others	365	302	361
Total	1,416	1,350	1,489

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.

Note: See Table 2 in Breakdown of SFC activity data on page 167 for more details.

Foreign exchange activities

We and the Australian Securities and Investments Commission issued a joint circular in January 2022 on our collaborative thematic review of the foreign exchange (FX) business and operations, including governance and controls, of global financial institutions in Hong Kong and Australia. The circular provided an overview of the FX market landscape in Australia and Hong Kong and shared observations and industry practices noted from the review.

Hedge funds

We conducted a survey of hedge fund managers in conjunction with an initiative of the International Organization of Securities Commissions (IOSCO) to collect data on investment funds. Our data was integrated into the *IOSCO Investment Fund Statistics Report* published in January 2022. More than 640 SFC-licensed hedge fund managers responded to the survey, providing us with an updated profile of the hedge fund industry in Hong Kong.

Industry guidance

We maintain close communication with the industry and regularly provide guidance through circulars. We hold seminars to explain and clarify our policies and expectations when introducing significant measures and regulatory enhancements.

Asset managers' climate-related risks management and disclosure

To help LCs comply with the new climate-related risks management and disclosure requirements in the FMCC, we issued a circular in August 2021 which provides sample industry practices for climate-related risks management and a decision flowchart for determining the applicability of the requirements. We also conducted two Facebook live training sessions to introduce the new requirements to the industry.



Facebook live training sessions on management and disclosure of climate-related risks by fund managers

Intermediaries

Anti-money laundering

In December 2021, we organised an AML/CFT webinar jointly with the Joint Financial Intelligence Unit to update 1,600 management and compliance personnel from LCs on major AML/CFT regulatory developments, share our inspection findings and other supervisory observations and provide feedback on suspicious transaction reporting.

We updated the frequently asked questions in September and October 2021 to elaborate some provisions in the AML/CFT guidelines to facilitate firms' compliance with the new requirements. In addition, the AML/CFT self-assessment checklist, which provides a structured framework for LCs and associated entities to assess their compliance with the key requirements, was updated in January 2022 to reflect the latest AML/CFT guidelines.

Financial distress and unavailability of key staff

To help the industry better prepare for contingent events caused by financial distress and the unavailability of key staff, we issued a circular in March 2022 to provide guidance on our regulatory approach and expected standards for LCs to mitigate the associated risks and the impact on investors and, if necessary, secure an orderly closure of business.

Complaint handling

In March 2022, we issued a circular to remind LCs about our regulatory requirements for complaint handling and provide suggested controls and examples of good practices to assist their compliance with the requirements.

COVID-19 response

We closely monitor the COVID-19 situation and take proactive steps to ensure our markets operate in an orderly manner when conditions change.

To help intermediaries maintain a high degree of operational resilience in the face of the pandemic and other disruptions, we issued a circular and a report in October 2021 to set out regulatory standards and measures for preventing and responding to operational disruptions and managing the risks of remote working.

Another circular strongly encouraged LCs to consider vaccination as a critical part of operational risk management. We urged LCs to review their business continuity plans, identify functions which are critical to their business operations and client interests and encourage staff performing these functions to get vaccinated. Amidst the acute situation of the fifth wave of COVID-19 infections in March 2022, we again reminded LCs to review and update their

business continuity plans. Specifically, LCs should critically assess the impact of sudden disruptions such as temporary staff shortages or reductions in services provided by essential vendors or other providers.

Following the suspension of the Hong Kong Securities and Investment Institute's in-person regulatory examinations, we announced that extensions would be allowed for individuals to take the exams and to fulfil continuous professional training requirements.



Statistical information and financial position of the Hong Kong securities industry

	As at 31.12.2021	As at 31.12.2020	As at 31.12.2019
Securities dealers and securities margin financiers	1,433	1,391	1,379
Active clients	4,159,100	3,207,677	2,024,849
Total assets (\$ million)	1,658,553	1,812,475	1,322,911

(\$ million)	12 months to 31.12.2021	12 months to 31.12.2020	12 months to 31.12.2019
Total value of transactions [^]	160,931,088	129,651,195	85,831,384
Total operating profit	43,491	30,904	11,962

[^] 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. Figures reported by an overseas incorporated licensed corporation which carries out its principal business activities outside Hong Kong and operates in Hong Kong as a branch office were excluded.

Note: Also see Table 8 in Breakdown of SFC activity data on page 172 for more details.