

23 December 2016

Circular to Intermediaries

Frequently Asked Questions on Triggering of Suitability Obligations

The purpose of this circular is to clarify the scope of application of the suitability obligations under the Code of Conduct¹ and to provide guidance and illustrations on whether and when the suitability obligations would be triggered under certain scenarios.

Under paragraph 5.2 of the Code of Conduct², a licensed or registered person should, when making a recommendation or solicitation, ensure the suitability of the recommendation or solicitation for the client is reasonable in all the circumstances, having regard to information about the client of which the licensed or registered person is or should be aware through the exercise of due diligence. The suitability obligations are applicable to all recommendations or solicitations concerning any investment products, whether or not the products involved are traded on an exchange.

Solicitations may cover a wide range of acts on the part of licensed or registered persons. Whether a licensed or registered person has made a solicitation is a question of fact which should be assessed against the circumstances of each case.

For example, in determining whether the posting of an advertisement for an investment product or the provision to clients of research reports and other product-specific materials such as stock commentaries (Research and Marketing Materials) has actually triggered the suitability obligations, the assessment should be made at the point of sale or advice. The assessment would focus on the communications between the client and the licensed or registered person leading up to and including the point of sale or advice, taking into account the content and context of any Research and Marketing Materials³ and the extent to which they created an environment in which the client was induced or recommended to enter into the transaction.

This means that posting of Research and Marketing Materials may or may not trigger suitability obligations, depending on whether they are relevant to the selling or advisory process, ie the direct communications with the client. In the absence of direct communications with the client, suitability obligations are unlikely to be triggered by the mere posting of an advertisement for an investment product in newspapers, magazines or television programmes, or by the wide dissemination of research reports.

The SFC has also issued Frequently Asked Questions (FAQs) with a view to providing guidance to licensed and registered persons on whether the suitability obligations under the

¹ Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission

² As supplemented by relevant FAQs and circulars, etc. issued by the SFC from time to time

³ Licensed or registered persons are required to comply with relevant legal and regulatory requirements when issuing Research and Marketing Materials. For example, they should ensure that advertisements do not contain information that is false, disparaging, misleading or deceptive under paragraph 2.3 of the Code of Conduct and that they should have a reasonable basis for investment recommendations under paragraph 16.



Code of Conduct will be triggered where:

- (i) licensed or registered persons have interactive communications with their clients on investment products; and
- (ii) licensed or registered persons provide discretionary account services to their clients.

A copy of the FAQs is attached to this circular for your information. The e-version of the FAQs is available for download on the SFC website at www.sfc.hk under the sections “Regulatory functions – Intermediaries – Supervision – FAQs – Triggering of Suitability Obligations”. The FAQs will be updated from time to time and you are advised to check our website for new information.

Licensed or registered persons should consider their own circumstances, review their existing systems and practices and enhance their own systems and controls, where necessary, having regard to this circular. Licensed or registered persons should also make reference to other relevant guidance, including the Frequently Asked Questions on Compliance with Suitability Obligations, issued by the SFC from time to time.

Should you have any queries regarding the contents of this circular, please contact Ms Pauline Chan at 2231 1952.

Intermediaries Supervision Department
Intermediaries Division
Securities and Futures Commission

Enclosure

End

SFO/IS/045/2016