

29 September 2017

## Circular to announce the SFC Regulatory Sandbox

The SFC recognises that firms utilising innovative technologies and demonstrating a genuine and serious commitment to carry on regulated activities through the use of financial technology (“**Fintech**”) may increase the range and quality of products and services for investors and benefit the Hong Kong financial services industry. Accordingly, the SFC today launched the SFC Regulatory Sandbox (“**Sandbox**”) to provide a confined regulatory environment for qualified firms<sup>1</sup> to operate regulated activities under the Securities and Futures Ordinance (“**SFO**”) before Fintech is used on a fuller scale.

As the technology at the core of the regulated activity may be novel, for the sake of market integrity and better investor protection, the reliability of the delivery of such financial services as well as the firms’ internal control systems would need to be examined and monitored in a confined regulatory environment at the initial stage before the services can be expanded and provided to the wider public in Hong Kong. The Sandbox would enable qualified firms, through close dialogue with and supervision by the SFC under the licensing regime, to readily identify and address any risks or concerns relevant to their regulated activities.

The Sandbox should not be viewed as a means to circumvent the applicable legal and regulatory requirements. The SFC emphasises the paramount importance of the integrity of the market and investors’ interests, and will not compromise regulatory requirements which are key to investor protection. For instance, a qualified firm operating in the Sandbox must be fit and proper and must comply with the applicable financial resources requirements (“**FRR**”). These requirements are not onerous and, in practice, the required financial resources are necessary for operating a credible business.

The salient features of the Sandbox are as follows:

(1) Eligibility:

The Sandbox is available to both licensed corporations and start-up firms that intend to carry on a regulated activity under the SFO. The qualified firm must be fit and proper, utilise innovative technologies and be able to demonstrate a genuine and serious commitment to carry on regulated activities through the use of Fintech. The establishment or activities of these firms should also increase the range and quality of products and services for investors and benefit the Hong Kong financial services industry (“**qualified firms**”).

Under the SFO, no person shall carry on a business in a regulated activity unless the person is licensed by the SFC to conduct such regulated activity. Accordingly, a qualified firm must be licensed (in the case of a start-up, it will need to apply for and

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<sup>1</sup> As defined in the “Eligibility” section.



obtain the appropriate licence) and comply with the applicable requirements (including FRR).

(2) Licensing conditions:

In order to minimise risks to investors during the period when a qualified firm operates in the Sandbox, the SFC may impose licensing conditions.

Such licensing conditions may include limiting the types of clients which the firm may serve or the maximum exposure of each client, so as to limit the scope and boundary of the firm's business in regulated activities. Licensing conditions may in some cases require the firm to put in place appropriate compensation schemes for investors, or to submit to periodic supervisory audits by the SFC (as discussed below).

(3) Closer monitoring and supervision by the SFC:

Qualified firms may be placed under closer monitoring and supervision by the SFC when they operate in the Sandbox. In such cases, the SFC may engage in more intensive dialogue with firms and may highlight compliance areas where they can further improve their internal controls and risk management.

This will benefit qualified firms and the investing public by enabling such firms to refine their business models and address any risks or concerns arising from the conduct of the regulated activities at the initial stage.

(4) Investor protection measures:

Qualified firms are expected to have adequate investor protection measures in place to address actual or potential risks or concerns identified when they operate in the Sandbox. For instance, qualified firms should notify their clients that they are operating in the Sandbox and provide full disclosure of the potential risks and any available compensation arrangements.

(5) Exit:

Once a qualified firm has demonstrated that its technology is reliable and fit for purpose, and its internal control procedures have adequately addressed the risks identified, the firm may apply to the SFC for removal or variation of some or all of the licensing conditions imposed, so that it may conduct regulated activities and be subject to supervision by the SFC on the same basis as licensed corporations which operate outside the Sandbox.

If the SFC considers that a qualified firm operating in the Sandbox is not fit and proper to remain licensed (for example, because its internal controls fail to meet the regulatory requirements), its licence may be revoked.

The SFC expects the great majority of applicants applying for a corporate licence under the SFO, including firms which make use of Fintech in conducting their regulated activities, such as robo-advisors, to go through the normal licence application process without the need to enter the Sandbox.



The SFC will discuss with a corporate applicant if it considers that an applicant's case should enter the Sandbox. For enquiries, please refer to the [SFC Fintech Contact Point](#).

Licensing Department  
Intermediaries Division  
Securities and Futures Commission

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