



## **Appendix D**

### **Consequential amendments to the Code of Conduct**





## **Use of gifts by distributors in promoting a specific investment product**

A new paragraph 3.11 is to be inserted into the Code of Conduct as follows:

### **Diligence**

#### **3.11 Use of gifts by distributors in promoting a specific investment product**

In promoting a specific investment product to a client, a licensed or registered person should not offer any gift other than a discount of fees or charges.



## Investor characterization

A new paragraph 5.1A is to be inserted into the Code of Conduct as follows:

### Information about clients

#### **5.1A Know your client: investor characterization**

- (a) Except where a client is a Professional Investor for the purpose of paragraph 15 of the Code, a licensed or registered person should, as part of the know your client procedures, assess the client's knowledge of derivatives and characterize the client based on his knowledge of derivatives.
- (b) Where a client without knowledge of derivatives wishes to purchase a derivative product (hereafter refer to as a "transaction" in this paragraph) which is:
- (i) traded on an exchange and the licensed or registered person has not solicited the client or made a recommendation to the client in relation to the proposed transaction, the licensed or registered person should explain the relevant risks associated with the product to the client;
  - (ii) not traded on an exchange and the licensed or registered person has not solicited the client or made a recommendation to the client in relation to the proposed transaction, the licensed or registered person should warn the client about the transaction and, having regard to the information about the client of which the licensed or registered person is or should be aware through the exercise of due diligence, particularly the fact that he is a client without knowledge of derivatives, the licensed or registered person should provide appropriate advice to the client as to whether or not the transaction is suitable for the client in all the circumstances. Records of the warning and other communications with the client should be kept. If the transaction is assessed to be unsuitable for the client, the licensed or registered person may only proceed to effect the transaction if to do so would be acting in the best interests of the client in accordance with the general principles of the Code.



## Pre-sale disclosure of monetary and non-monetary benefits

A new paragraph 8.3 is to be inserted into the Code of Conduct as follows:

### Information for clients

#### **8.3 Pre-sale disclosure of monetary and non-monetary benefits**

##### **Part A**

##### **Disclosure of monetary benefits**

*Where the monetary benefits received are **quantifiable***

##### **(a) Specific disclosure**

###### *Explicit remuneration arrangement*

- (i) Where a licensed or registered person and/or any of its associates explicitly receives monetary benefits from a product issuer (directly or indirectly) for distributing an investment product, the licensed or registered person should disclose the monetary benefits that are receivable by it and/or any of its associates as a percentage ceiling of the investment amount or the dollar equivalent.

###### *Trading profit made from a back-to-back transaction*

- (ii) Where a licensed or registered person enters into a back-to-back transaction concerning an investment product, the licensed or registered person should disclose to the client the trading profit to be made. The trading profit should be disclosed as a percentage ceiling of the investment amount or the dollar equivalent.

##### *Notes*

*For the avoidance of doubt, the specific disclosure should be made on a transaction basis.*

*As a minimum, a licensed or registered person should disclose the monetary benefits that are receivable by it and/or any of its associates or the trading profit in the form of a percentage ceiling of the investment amount rounded up to the nearest whole percentage point or the dollar equivalent. However, having regard to its own circumstances, the licensed or registered person may disclose a specific percentage or the dollar equivalent instead.*

*Back-to-back transactions refer to those transactions where a licensed or registered person, after receiving a purchase order from an investor, purchases an investment product from a third party and then sells the same investment product to the investor and no market risk is taken by the licensed or registered person.*



**(b) Generic disclosure**

*Non-explicit remuneration arrangement*

- (i) Where a licensed or registered person does not explicitly receive monetary benefits for distributing an investment product which is issued by it or any of its associates, the licensed or registered person should disclose that it or any of its associates will benefit from the origination and distribution of this product.

*Where the monetary benefits received are **not quantifiable**:*

- (ii) Where the monetary benefits received by a licensed or registered person and/or any of its associates are not quantifiable prior to or at the point of sale, the licensed or registered person should disclose the existence and nature of such monetary benefits.

**Part B**

**Disclosure of non-monetary benefits**

- (a) Where a licensed or registered person and/or any of its associates receives from a product issuer non-monetary benefits for distributing an investment product, the licensed or registered person should disclose the existence and nature of such non-monetary benefits.



## Disclosure of Sales Related Information

A new paragraph 8.3A is to be inserted into the Code of Conduct as follows:

### Information for clients

#### **8.3A Disclosure of sales related information**

- (a) Where a licensed or registered person distributes an investment product to a client other than a Professional Investor for the purpose of paragraph 15 of the Code, the licensed or registered person should deliver the following information to the client prior to or at the point of sale:
- (i) The capacity (principal or agent) in which a licensed or registered person is acting;
  - (ii) Affiliation of the licensed or registered person with the product issuer;
  - (iii) Disclosure of monetary and non-monetary benefits (*Please refer to paragraph 8.3 of the Code*); and
  - (iv) Terms and conditions in generic terms under which client may receive a discount of fees and charges from a licensed or registered person.
- (b) The disclosure must be made in writing, electronically or otherwise. The licensed or registered person should have adequate measures in place to ensure that the above information is provided to the client prior to or at the point of sale.
- (c) In circumstances where provision of information in written form is not possible before a transaction is concluded, the licensed or registered person should make a verbal disclosure and provide such information in writing to the client as soon as practicable after the conclusion of the transaction.
- (d) The information disclosed in written form should be in Chinese or English according to the language preference of the client.

#### Notes

The licensed or registered person should ensure that the disclosure in writing is prominent, is presented in a clear and concise manner and is easy for average clients to understand.



## Refund by distributors under a cooling-off period

A new paragraph 13.5 is to be inserted into the Code of Conduct as follows:

### Rebates, soft dollars, and connected transactions

#### 13.5 Refund obligation

Where a cooling-off mechanism is incorporated in an investment product and a client exercises his right under such mechanism to cancel the order, sell the product back to the issuer or its agent, or otherwise unwind the transaction in relation to that product, the licensed or registered person should promptly execute the client's instruction and pass on to the client the full amount of refund (including the sales commission<sup>1</sup>) received from the product issuer less a reasonable administrative charge<sup>2</sup>.

#### Notes

<sup>1</sup>This includes any sales commission retained by the licensed or registered person in relation to that transaction.

<sup>2</sup>The administrative charge should be disclosed to the client at or prior to point of sale and should not contain any profit margin.



## Professional Investors

### 15.1 Professional Investors: in general

Where a client of a licensed or registered person is a Professional Investor referred to in paragraph 15.2A or paragraph 15.2B (who has sufficient knowledge and expertise in relevant products and markets), the licensed or registered person will not be required to fulfil the requirements set out in paragraph 15.5 while serving such clients in respect of relevant products and/or markets of which they are treated as Professional Investors.

### 15.2 Professional Investors

There are 2 categories of Professional Investors:

- A. A person falling under paragraphs (a) to (i) of the definition of “professional investor” in Part 1 of Schedule 1 to the SFO.
- B. A person falling under paragraph (j) of the definition of “professional investor” in Part 1 of Schedule 1 to the SFO.

**15.3** Before waiving the requirements set out in paragraph 15.5 for persons referred to in paragraph 15.2B above, the licensed or registered person should assess and be reasonably satisfied that the person is knowledgeable and has sufficient expertise in relevant products and markets. In assessing the knowledge, expertise and investment experience of any of the persons referred to in paragraph 15.2B above, the licensed or registered person should have regard to the following:

- (a) the type of products in which the person has traded;
- (b) the frequency and size of trades (a Professional Investor would be expected to have traded not less than 40 transactions per annum);
- (c) the person’s dealing experience (a Professional Investor would be expected to have been active in the relevant market for at least 2 years);
- (d) the person’s knowledge and expertise in the relevant products; and
- ~~(d)~~(e) his awareness of the risks involved in trading in the relevant products and/or markets.

The above assessment should be in writing. Records of all relevant information and documents obtained in the assessment should be kept by the licensed or registered person so as to demonstrate the basis of the assessment.

15.3A A licensed or registered person should undertake a separate assessment prior to treating an existing Professional Investor under paragraph 15.2B as a Professional Investor in a different product type or market.





15.3B A licensed or registered person should undertake a new assessment where a Professional Investor under paragraph 15.2B has ceased to trade in the relevant product or market for more than 2 years.