

G.N. 1414

## SECURITIES AND FUTURES ORDINANCE (Chapter 571)

Pursuant to section 399(1) of the Securities and Futures Ordinance, the Securities and Futures Commission published the Client Identity Rule Policy in the Schedule for information.

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### Schedule

#### **Client Identity Rule Policy**

**April 2003**

##### **Summary of Client Identity Rule Policy**

1. The Rule applies to all licensed or registered persons who deal in securities and/or futures contracts that are listed or traded on a recognized stock market or a recognized futures market or derivatives, including over the counter derivatives, written over such securities or futures contracts, regardless of where such trades are effected.
2. If upon request from one of the exchanges and/or the SFC (singularly or collectively "the Regulators" unless the distinction is important) client identity information is provided within two business days, disciplinary action will not be taken.
3. For collective investment schemes, discretionary accounts or discretionary trusts, the only information normally required is the name of the scheme, account or trust in question and the person who ultimately originates the instruction in relation to that transaction (i.e. usually the individual investment manager responsible for the investment decision). The Regulators will not ask for information in relation to subscriptions in, redemptions from or switches between collective investment schemes.
4. The SFC will not specify any particular way to comply with the Rule as long as

request. The agreement would have to provide that the information would still be available even after the agreement ended.

5. Failure to follow the Rule may reflect on the licensed or registered person's fitness and properness. However, where the licensed or registered person can demonstrate that it was satisfied on reasonable grounds at the time of the transaction that the required information would be provided in due time, disciplinary action will not be taken.
6. In summary, a licensed or registered person is under a duty to know with whom

that it must take to comply with the Rule, it should focus on its responsibility to act in a fit and proper manner. If it acts honestly and reasonably in attempting to comply with the Rule, it will not be the subject of disciplinary action.

5. The SFC will administer the Rule flexibly and will, in deciding whether or not to take disciplinary action, take into account difficulties that a licensed or registered person may face in complying.
6. The SFC will assess compliance by whether, in practice, the information is available to the Regulators upon request. During inspections, the Regulators will check that systems are in place to ensure that the required information will be made available and, if they are not, will normally require correction, rather than take disciplinary action.

#### **C. Transactions to which the Rule applies**

7. The Regulators will usually ask for client identity information in relation to transactions in securities listed or futures contracts that are listed or traded on a recognized stock market or a recognized futures market but may occasionally ask for it in relation to over-the-counter ("**OTC**") transactions in Hong Kong.
8. The Rule does not apply to transactions executed before 13 November 1998. However, the Rule applies to all transactions executed on or after 13 November 1998, irrespective of whether the client was taken on before or after that date.

#### **D. Timing of the provision of information to the Exchanges and/or to the SFC**

9. Strictly, the Rule requires that the client identity information must be obtained and recorded before anything is done to effect a transaction.
10. The SFC expects this to be done where it is practicable. For example, a licensed or registered person with a local client acting as principal should be able to obtain and record the information required by the Rule before anything is done to effect a transaction on that client's behalf.
11. The SFC understands that, in some circumstances, it may not be practicable to obtain or to record all of the required information before a transaction. For example:

where the client is an institutional client acting as agent for a large number of underlying clients through a nominee or omnibus account;

where the client uses a central dealing desk and the procedures used do not enable the full allocation details of a transaction to be provided until after the transaction is executed; and

where, in relation to a block order from a fund manager, the information about the allocation of that order between several collective investment

schemes or accounts is not available at the time the order is effected by the licensed or registered person.<sup>1</sup>

12. For surveillance purposes, the Regulators

For example, some market participants may not want to disclose the identities of their clients to their competitors.

18. The SFC will not take disciplinary action where satisfactory alternative measures to fulfil the objective of the Rule are in place. The SFC will not specify any particular way in which a licensed or registered person can comply with the spirit of the Rule. For example, for a financial intermediary client, it is not expected that a licensed or registered person would have recorded the details of the ultimate client prior to execution of an order on that client's behalf.
19. For example, the records of the client information of a licensed or registered person could be kept outside Hong Kong in the same corporate group.
20. It would also be acceptable if, before executing a transaction, an agreement were in place whereby the licensed or registered person's client agreed to provide information about the beneficiary of that transaction and details of the person originating the instruction for that transaction on request directly to the Regulators, without having to pass the same information to the licensed or registered person. The agreement would have to provide that the obligation to ensure that the information was provided to the Regulators continued even after the agreement ended. Examples of such an arrangement in practice are as follows.

A = licensed or registered person

B = financial intermediary unaffiliated with A, acting as agent for C

C = B 's underlying client

A<-----

The same facts as the example above, but B is not dealing directly with the





A then sells 1 million XYZ Ltd shares to C.

Since A bought the 1 million XYZ Ltd shares knowing that it already had an order from C for the same shares, the SFC would consider that these transactions were possibly structured so as to avoid disclosing C as the ultimate beneficiary of the purchase of 1 million XYZ Ltd shares and would consider disciplinary action against A.

**"Instruction"**

37. The "instruction" in relation to a transaction is anything that the order-giver communicates to the licensed or registered person, or to their own immediate financial intermediary or anyone else in the chain of persons processing the transaction, that has a direct bearing on th