

# Consultation Conclusions on Hong Kong Investor Identification Regime and OTC Securities Transactions Reporting Regime

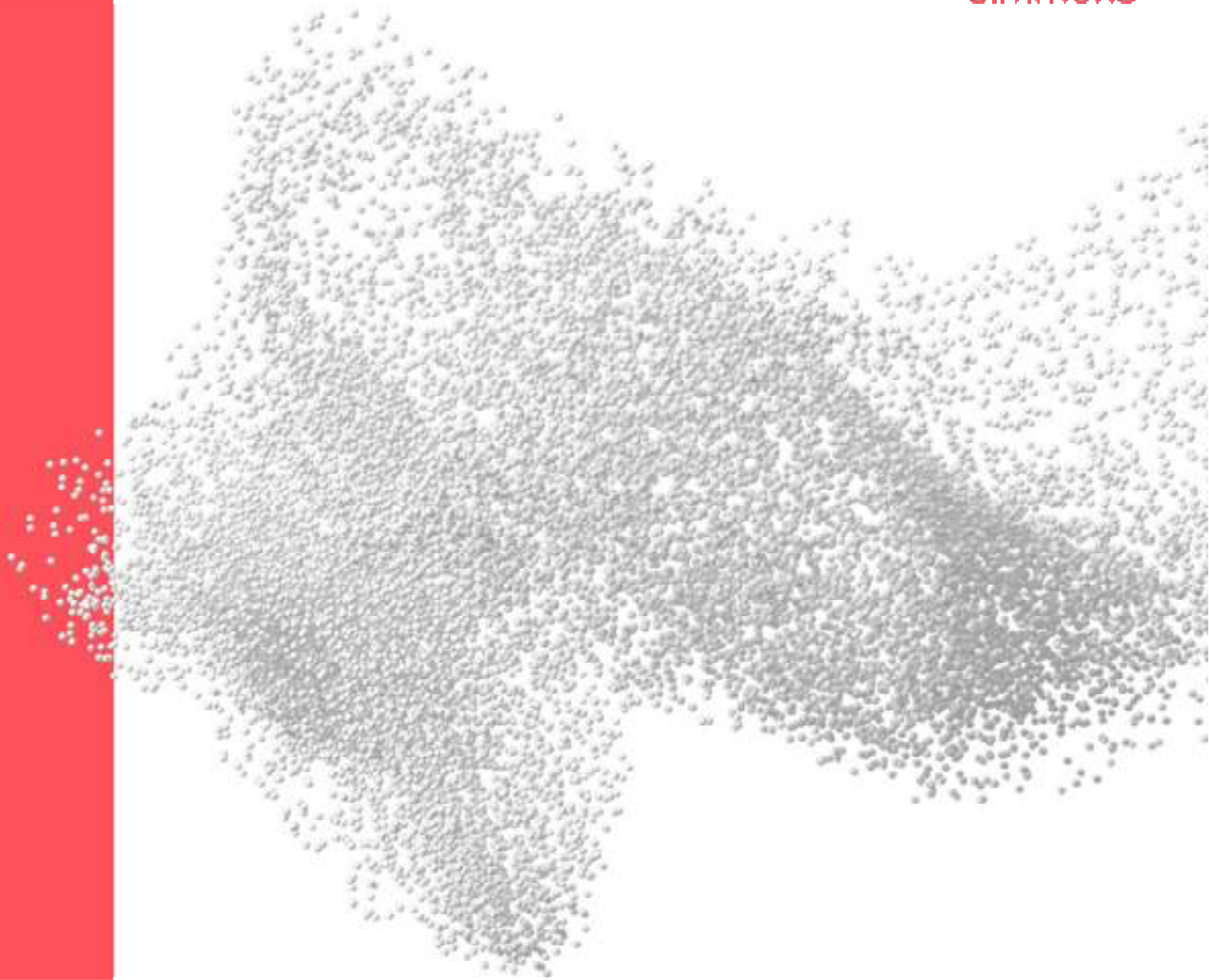
ASIFMA and Simmons & Simmons  
30 August 2021

# Agenda



- Introduction
- Hong Kong Investor Identification Regime
- OTC Securities Transactions Reporting Regime
- Q&A

# Introduction



# Introduction



## Overview

- SFC published the consultation paper on 4 December 2020
- ASIFMA submitted response in March 2021 and attended various conference calls with SFC and the HKEx respectively, with Simmons & Simmons
- SFC published the consultation conclusions on 10 August 2021

## Implementation timeline

- The target implementation date to introduce the regimes are extended:
  - HK Investor ID Regime – by **the second half of 2022**
  - OTC Securities Transactions Reporting Regime – by **the first half of 2023**
- The SFC will amend the Code of Conduct – introduce new Chapters 5.6 and 5.7
- The amendments to the Code of Conduct will come into effect on a future date to be determined by the SFC in line with the implementation timeline

# Introduction



## Further guidance to be issued

- **Implementation circular:** To be issued by SFC by September 2021 on preparations required and relevant timeline
- **Consent circular:** To be issued by SFC by September 2021 on (i) specified purposes of use of personal data, (ii) how consent may be obtained (e.g. in writing, electronically or by phone) and (iii) the requirements to be observed
- **Regime-specific guidance:**
  - **Hong Kong Investor ID Regime – HKEX Information Paper:** To be issued by SEHK on technical operational details and logistics
  - **OTC Securities Transactions Reporting Regime – Technical Document:** To be issued by SFC by the end of 2021 on technical details (e.g. file specifications, reporting templates and submission channels for the OTCR submission portal)
- SFC will work with SEHK to provide a **system testing period** and conduct **training sessions** for the industry prior to implementation

# Hong Kong Investor Identification Regime



# Hong Kong Investor ID Regime

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## Relevant Regulated Intermediary

A licensed or registered intermediary which:

- submits or arranges to submit for execution an on-exchange order (“On-Exchange Order”)
- carries out an off-exchange trade executed outside the exchange’s automatic order matching system (“Off-Exchange Trade”) which is subject to the reporting requirement to the exchange (“OE Trade Reporting”)
- carries out an off-exchange order (“Off-Exchange Order”)

in connection with “Specified Activities”

is a “Relevant Regulated Intermediary”

“Specified Activities” is defined as (i) proprietary trading; and (ii) the provision of securities brokerage services for a person in respect of order placed through an account opened and maintained for that person (our emphasis added)



# Hong Kong Investor ID Regime

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However.....

# Hong Kong Investor ID Regime

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## Overseas Booking Model

### Paragraph 61 of the SFC's Consultation Conclusion:

“When a Relevant Regulated Intermediary routes securities orders abroad to an overseas broker, it should include the client's BCAN in the securities order to that broker and put in place arrangements with that overseas broker so that the securities order can be transmitted together with the BCAN to the executing exchange participant. The client's CID should be submitted directly by the Relevant Regulated Intermediary to the Stock Exchange of Hong Kong by way of inclusion in a BCAN – CID Mapping File.”

### Paragraph 64 of the SFC's Consultation Conclusion:

“Failure by a Relevant Regulated Intermediary to provide a BCAN in a securities order to its overseas broker for onward transmission to an EP or to establish arrangements with its overseas broker for onward transmission of the BCAN **may constitute a breach of the Code of Conduct and subject to regulatory action by the SFC.**”

# Hong Kong Investor ID Regime



## Overseas Booking Model/“In-Scope Client”

### Issues:

- Who should be treated as an “In-Scope Client”?
- The SFC has revised the definition of “client” in the Code of Conduct
  - it will no longer include a client of an EP’s overseas affiliate
  - the term “client” generally refers to a party which has placed or proposes to place a securities order *through a securities trading account* with a Relevant Regulated Intermediary
- However, it is very common in the industry for a Hong Kong client to open a securities trading account with a Relevant Regulated Intermediary’s overseas affiliates and executes trades through the Relevant Regulated Intermediary
- It is also common for an overseas client to open accounts with an overseas entity, but places trades with a Relevant Regulated Intermediary
  - are these clients in scope? who should be assigned with BCAN?
  - the definitions of “client” and “Specified Activities” appear to contradict paragraph 61 of the SFC’s Consultation Conclusion
  - DMA/electronic trading?

# Hong Kong Investor ID Regime



## Relevant Regulated Intermediary

### Custodian/Fund Manager

- Whether a custodian will be subject to the Hong Kong Investor ID Regime will depend on whether it is acting in the capacity of a Relevant Regulated Intermediary when it handles a securities order
  - if a custodian submits an On-Exchange Order, carries out an Off-Exchange Trade which is subject to the OE Trade Reporting requirement or carries out an Off-Exchange Order in the capacity of a Relevant Regulated Intermediary (for example, if a custodian opens and maintains a securities trading account for an investor at its own entity and provides securities brokerage services to the investor), **it will be subject to the Hong Kong Investor ID Regime**
  - if a fund manager provides discretionary investment management services and places orders with an executing broker for execution, **it will not be subject to the Hong Kong Investor ID Regime**

# Hong Kong Investor ID Regime

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## In-Scope Securities

- securities listed or traded on the trading system of the Stock Exchange of Hong Kong will be covered by the Hong Kong Investor ID Regime
  - includes ETFs
  - includes some derivative products, such as callable bull/bear contracts, derivative warrants and inline warrants
  - excludes odd lot/special lot market (however, mandatory BCAN tagging still applies to special lots traded on Stock Exchange of Hong Kong's trading platform)
  - excludes stock options and futures which are traded on the Hong Kong Futures Automated Trading System

# Hong Kong Investor ID Regime

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## Assignment of BCAN

### Trade Give-Up

- Raised in ASIMFA's responses to SFC's Consultation Paper in paragraph 2.3(B)
- However, this was not addressed by the SFC specifically in the SFC's Consultation Conclusion
  - to re-cap, under a trade give-up arrangement, some financial institutions will treat the fund manager as the client and assign BCAN to the fund manager
  - however, some financial institutions will treat the prime broker who issues a swap as the client (as a beneficial owner of the executed position) and these financial institutions consider it is necessary to amend the BCAN to reflect the difference in beneficial ownership
- The SFC now permits amendments of BCAN (discussed below)
- However, it is not clear whether a Relevant Regulated Intermediary must amend the BCAN for trade give-up activities

# Hong Kong Investor ID Regime



## Assignment of BCAN

### Fund Manager

- Whether a fund manager or an investment fund should be assigned with a BCAN depends on which entity is the account holder of the securities trading account through which an order is placed
  - If a fund manager's securities trading account maintained with a Relevant Regulated Intermediary is used, the fund manager should be assigned with BCAN
  - If an order is placed from an investment fund's securities trading account maintained with a Relevant Regulated Intermediary, the investment fund should be assigned with BCAN
- Where a securities order placed by a fund manager is tagged with the fund manager's BCAN, it is not required to report the BCANs of the investment funds to which the securities are subsequently allocated by the fund manager
- If a fund manager has two legal entities which are onboarded with a Relevant Regulated Intermediary but the orders and instructions are only placed by one entity, who should be assigned with the BCAN?

# Hong Kong Investor ID Regime



## Assignment of BCAN

### Discretionary Account

- The approach to tagging BCANs to orders for discretionary accounts and investment funds should be consistent
- The BCAN tagged to an order should be the BCAN of the person whose securities trading account is used for placing the order
  - If a discretionary account manager's securities trading account is used, the discretionary account manager's BCAN should be tagged
  - If an order is placed from a discretionary account opened in the name of the discretionary account client, the discretionary account client's BCAN should be tagged, even when the discretionary account is managed by the discretionary account manager



# Hong Kong Investor ID Regime



## Reporting of BCANs in aggregated orders

- The term “aggregated order” is defined as “an order which comprises two or more buy orders and/or sell orders for the same listed security placed by different clients, which may be executed as an On-Exchange Order or an Off-Exchange Order”
- The following will not constitute an “aggregated order”:
  - orders placed by a single client throughout a trading day
  - an order placed by a fund manager for different funds it manages which is tagged with the fund manager’s BCAN
- The HKEx Information Paper will set out the details of the required information which needs to be submitted for underlying order (i.e. trade allocation)
- Reporting of underlying trade allocations will only be required for an aggregated trade and not for an aggregated order which is cancelled, unmatched or revised prior to execution
- Relevant Regulated Intermediaries will have up to T+3 to report the orders underlying an executed aggregated order

# Hong Kong Investor ID Regime



## Amendment of BCANs

- No prior approval for a BCAN change will be required
- Amendment process will differ depending on the stage at which BCAN is to be amended:
  - For on-exchange (i.e. automated) trades:
    - Before an order is matched and executed: Cancel the order and re-input the order with the correct BCAN, in which case the order has to line up afresh
    - After an order is matched and executed: Submit an error notification to the SEHK as soon as possible
  - For manual trades:
    - Submit an error notification to the SEHK as soon as possible
- Trade Give-Up: appears it is necessary to submit an “error notification”, which is misleading
- Executed orders will not be cancelled or become invalid due to BCAN amendment
- SEHK will make forms available for filing a post-trade error correction of BCAN and provide further guidance in the HKEX Information Paper

# Hong Kong Investor ID Regime



## BCAN format and confidentiality

- BCAN consists of up to 10 digits to be assigned by a Relevant Regulated Intermediary, prefixed by its CE number (i.e. “ABC123.[BCAN]”)
- To distinguish between BCANs assigned by different Relevant Regulated Intermediaries, a Relevant Regulated Intermediary will need to insert its CE number as a prefix before the BCAN on the trading system and in the BCAN-CID Mapping File
- Provided the BCAN is compliant with the requirements set out in the HKEX Information Paper:
  - a client’s BCAN can be the same under the Hong Kong Investor ID Regime and the NB Investor ID Regime
  - BCAN may include reference to a Relevant Regulated Intermediary’s internal client number or account number
- No obligation to disclose BCAN to clients
  - No prohibition against voluntary disclosure of BCAN to clients, but need to consider compliance with applicable data privacy laws and regulations because BCAN, when read with CID, would disclose a person’s identity and constitute personal information

## Responsibility to ensure CIDs are accurate and kept up-to-date

- Relevant Regulated Intermediaries should take all reasonable steps to ensure that the client information (including the data constituting the CID) they collect and submit to SEHK's data repository is accurate and kept up-to-date (drawing on Chapter 5.1 of the Code of Conduct)
- Such reasonable measures may include:
  - Obtaining relevant representations and warranties from clients
  - Putting in place measures to require clients to give notice of any updates to CID
  - Conducting a refresher of the CID exercise based on the timeframe prescribed by the AML/CFT Guidelines
- Relevant Regulated Intermediaries should submit updated BCAN-CID Mapping File to SEHK as soon as practicable upon actual notice of a change in CID

# Hong Kong Investor ID Regime



## Acceptable identity documents for CID

- See Chapter 5.6(o) for the CID to be used for different types of clients
- SFC rejected the idea of giving Relevant Regulated Intermediaries the flexibility to rely on individual clients' HKID card information or passport details in their records
  - Mandatory to provide HKID card information for all Hong Kong residents
- SFC also opined that it is not appropriate for LEI to be used in place of BCAN
- Relevant Regulated Intermediaries should issue a notification to their existing securities trading account holders (regardless of nationality) to inform them of the waterfall of identity documents and request an identity document required under the waterfall (if not already obtained) or updated identity document information, as appropriate

# Hong Kong Investor ID Regime



## Confidentiality of data submitted to SEHK and SFC

- BCANs and BCAN-CID Mapping Files collected from Relevant Regulated Intermediaries will not be made publicly available
- Access to BCAN and CID information by SFC and HKEX staff will be on a strict need-to-know basis and they will have to adhere to security requirements and measures
- SFC and SEHK will keep the data only for as long as necessary to perform their statutory functions and will put in place measures to comply with the PDPO
- It is not anticipated that information collected under the regime would be disclosed to law enforcement agencies in other jurisdictions

## Consent from investors – Individual clients

- Relevant Regulated Intermediaries will be required to obtain express consent from their individual clients for the use of personal data under the two regimes
  - No standard form of client consent would be prescribed by SFC
  - No need to obtain new consent if both of the following are met:
    - 1) client consent on the use of personal data has already been obtained from these clients; and
    - 2) the consent expressly includes all purposes of use specified by SFC in the Consent Circular (which will be substantially similar to those set out in the consultation paper)
  - Client consent need not to include the purposes prescribed by SFC in exactly the same words
  - The requirement to obtain express consent will not be complied with where the specified purposes of use may only be implied or inferred from client documentation
  - Consent can be obtained in writing, by phone and other electronic means (including email and instant messaging applications)

# Hong Kong Investor ID Regime



## Consent from investors – Corporate clients

- The requirement to obtain express consent will not apply to corporate clients



# Hong Kong Investor ID Regime



## Retention period

- BCANs, BCAN-CID Mapping File information and records of client consent should be retained:
  - as long as the client remains a client of the Relevant Regulated Intermediary; and
  - for no less than two years after the client has ceased to be its client

# OTC Securities Transactions Reporting Regime



# OTC Securities Transactions Reporting Regime



New types of transactions exempted from reporting obligations

- A transfer of shares made in accordance with the terms of a structured product or a derivative (whether listed or not), or for the conversion of a depository receipt into shares and vice versa, is exempted from reporting

# OTC Securities Transactions Reporting Regime



## Scenarios with stamp duty relief

- Share transfers where no stamp duty is payable or where stamp duty relief is granted (whether in full or in part) are not reportable (e.g. intra-group transfer of shares with stamp duty relief, stock borrowing and lending, repo and reverse repo with stamp duty relief and transfer of a basket of securities for allotment or redemption of an ETF with stamp duty remission)
  - When an application for stamp duty relief has been or will be submitted to the IRD, the Relevant Regulated Intermediary which makes the share transfer would not be required to report it prior to the IRD's determination
  - However, if the IRD subsequently determines that no stamp duty relief (whether in full or in part) would be granted, the Relevant Regulated Intermediary should report the share transfer as soon as practicable after being notified of the IRD's determination

# OTC Securities Transactions Reporting Regime



## Issues related to custodians

- Similar to the Hong Kong Investor ID Regime, only “Relevant Regulated Intermediaries” will be subject to the OTC Securities Transactions Reporting Regime
  - A custodian who does not act as an execution broker would not be subject to the regime
  - The taking up of bonus shares is not reportable under the regime as no stamp duty is chargeable on issuance of new shares including bonus shares
  - Mere provision of administrative services (such as payment of stamp duty and tax filing), without making the transfer, does not trigger reporting obligations

# OTC Securities Transactions Reporting Regime



## OTC securities transactions booked overseas

- Where an OTC securities transaction is booked overseas but arranged by a Relevant Regulated Intermediary for a client of its overseas affiliate:
  - A Relevant Regulated Intermediary is only subject to reporting obligation if it makes a share transfer in connection with a transaction chargeable with stamp duty in Hong Kong
  - When the Relevant Regulated Intermediary does not make the share transfer, the corresponding OTC securities transaction is not reportable even if the Relevant Regulated Intermediary arranges for a client of an overseas affiliate to buy or sell Hong Kong stocks by way of an OTC securities transaction
  - Time to report under the regime will be based on transfer date but not the trading day or stamp duty payment date – SFC rejected the idea of changing the time to report cross-border trades to 30 days after the trading day as it would unnecessarily complicate the regime

# OTC Securities Transactions Reporting Regime



## Time to report

- Extended the time to report to within three Hong Kong trading days after the transfer/deposit/withdrawal day (Hong Kong time)

# OTC Securities Transactions Reporting Regime



## Reporting information when clients do not provide consent

- For an individual client who does not provide consent to a Relevant Regulated Intermediary for transfer of personal data to the SFC:
  - A Relevant Regulated Intermediary should only effect transfers of shares out of, and withdrawals of physical share certificates from, the client's account
  - A special indicator (to be specified in the Technical Document) will need to be submitted instead of the client's CID for such reporting



# Q&A



# Hong Kong Investor ID Regime



## In-scope securities

- For both HKIDR and OTCR the products that are eligible for reporting are mainly related to stocks only, is it accurate to say that Fixed Income business is out of scope for both regimes?
- We understand all “securities” listed and traded on SEHK are in scope. Could we confirm that ETFs are in scope, and if so:
  - a) in the case of ETF market making, the market maker’s (i.e. the EP’s) BCAN should be tagged to the market making order; and
  - B) in the case of ETF Designated Specialist (which is a client of the EP), the Designated Specialist entity’s BCAN should be tagged to the market making order?

# Hong Kong Investor ID Regime



## Overseas booking model

- It was noted in #9a of consultation conclusion paper that the scope of Relevant Client will be revised to exclude clients of overseas affiliates from HKIDR. On the other hand, #61-64 of the paper mentioned that the Relevant Regulated Intermediaries need to provide a client BCAN to overseas broker for onward transmission to an EP.

Hence, we would like to seek clarification that if the business model is set up in a way that Relevant Regulated Intermediaries are on-boarded with overseas broker affiliates, does it mean the scope of Relevant Client would still include clients of Relevant Regulated Intermediaries?

# Hong Kong Investor ID Regime



## Overseas booking model

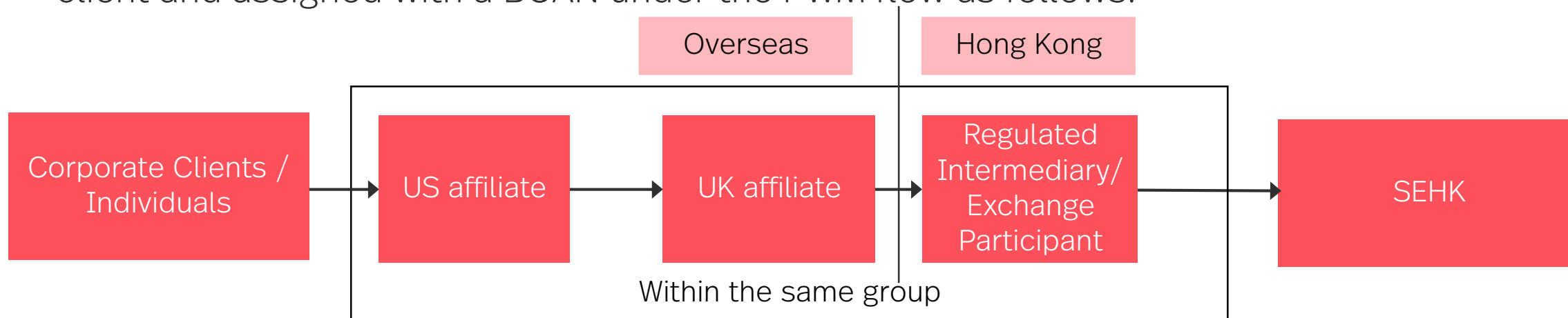
- We note that para 62 of the consultation conclusion specifically clarified that where a Relevant Regulated Intermediary (RI) books a securities order with an overseas broker before routing the order back to an EP, such RI shall tag the client's BCAN with such order. A few industry members adopt remote booking/global account carrier model for their execution services in the sense that clients will open trading account with overseas affiliate of a RI/EP and their orders will be booked into such overseas affiliate which further routes the orders to the EP for execution. However, execution desk of RI/EP may directly liaise with certain clients for order placing under such remote booking/global account carrier model. Please clarify if the remote booking/global account carrier model mentioned above will be in scope for the purpose of para 62.

# Hong Kong Investor ID Regime



## Overseas booking model

- In relation to the question in the previous slide, please clarify who should be treated as direct client and assigned with a BCAN under the PWM flow as follows:



Regulated Intermediary executing an order which originates from a Corporate client or individual who contracts with the US broker affiliate which in turn contracts with the UK affiliate of the Regulated Intermediary. From the Regulated Intermediary's perspective, it treats its UK broker affiliate as its direct client and **those corporate clients or individuals of the US broker affiliate remain anonymous to the Regulated Intermediary.**

# Hong Kong Investor ID Regime



## Overseas booking model

- With reference to para 61 and 62 of the SFC consultation conclusion, for orders from an overseas client that directly handled by sales traders of the Relevant Regulated Intermediary located in HK, but booked in an overseas affiliate, should BCAN be assigned to (i) the overseas affiliated entity or (ii) the overseas client?

# Hong Kong Investor ID Regime



## Tagging of BCAN

- Fund Manager A has 2 Legal Entities (Entity A and Entity B) onboarded with a Relevant Regulated Intermediary. The orders and instructions for Entity A and B will be managed by Trading Desk of Entity A. When the order sends to SEHK, can BCAN of Entity A be used for orders of Entity A and B?
- If we have a client who has accounts with 2 different Relevant Regulated Intermediaries of our group, is it acceptable to assign BCAN with one RRI only and send that relevant BCAN to SEHK when trading at SEHK regardless the involvement of 2 RRIs?

# Hong Kong Investor ID Regime



## Format of BCAN

- How to define the BCAN code? We did assume the following but please help to double confirm: The standard format of the BCAN field consists in a code that cannot exceed 10 digits representing the client. The field will have 2 parts:
  - A) The prefix: The client CE (central entity) number (6 digits), which is assigned by the SFC to a regulated entity. It will be followed by a separator dot(“.”) and then
  - B) The BCAN (4 digits) assigned randomly to the client (by who? The Regulated Entity? The broker?)



# Hong Kong Investor ID Regime



## Amendment of BCAN – Trade give-up

- Whether there was any previous discussion around resubmission/amending BCANS for failed trades or accommodation. Otherwise, it could be clarified if these are considered erroneous BCAN or not under the rules as these trades are legit but failed or subsequently accommodated by Relevant Regulated Intermediaries.
- Previously one of the firms raised a question regarding give up flow whereby the client initially placed an agency order (the client's BCAN would be used for trading). However, after execution and at allocation phrase, the client could give up the trade to a swap broker and the swap broker will become the beneficiary of the transaction. It is not clear the expectation on whether we are required to file any BCAN amendment for this kind of activity.
- Refer to para 93 and 94, for cash to swap trades (i.e. trade give-up), an “erroneous BCAN” should be reported to SEHK. Indeed, trade give-up is a legitimate reason for amending BCAN. As such, the name of the “error report” seems to be misleading. .
- Can you cover the BCAN tagging arrangement of give-up trades in the webinar on Monday? This was raised in ASIFMA's responses to SFC's consultation under paragraph 2.3B but not specifically addressed by the SFC in the consultation conclusion

# Hong Kong Investor ID Regime



## Amendment of BCAN – Other queries

- Why orders should be cancelled in case of BCAN amendments while the order is not yet executed or matched?
- China Connect process of BCAN correction is manual. For HK, which is more complex market, there can be legitimate cases of revising BCAN on an order or part of the order. Can we please get more clarity on how HKEx can introduce an operational efficient workflow with minimal human intervention to submit erroneous BCAN correction report to exchange?

# Hong Kong Investor ID Regime



## Aggregated order

- In the aggregated flow or normal allocation flow, there is a case where the BCAN code for execution may not be equal to the BCAN code in the allocation flow. In this case, the Regulated Entity may need extra efforts to fill in the amendment form. Is that correct?
- What is the difference between aggregated orders and Fund Managers orders?

# Hong Kong Investor ID Regime



## Confidentiality

- It Is mentioned in the documents that the LEI cannot be used to protect client's confidentiality, but clients can be identified with their CE number is that correct?

# Hong Kong Investor ID Regime



## Other questions

- In the documents, it is mentioned that the BCAN should be sent to SEHK for execution (FO). However, it doesn't mention any change about sending the message to CCASS for settlement.
- In the agency flow, how to distinguish the “Relevant Regulated Intermediary” from the “Non-Relevant Regulated Intermediary”? The “Relevant Regulated Intermediary’s” message to SEHK will have to include the CE number? Is that correct?
- Will there be a matching process available for OE orders for reconciliations purposes as the input will be manual?

# Hong Kong Investor ID Regime



## Other questions

- What are the eligibility criteria for NB Investor ID Regime?
- Under China Connect, if any abnormal trading activity is identified in the orders of a specific BCAN, the Mainland exchanges may take the relevant measures including rejecting all orders associated with that BCAN. Please advise if HKEx will have similar power under HKIDR to suspend trading or require the EP to suspend trading of a particular BCAN.

# OTC Securities Transactions Reporting Regime



## Securities lending and borrowing transactions

- Whether securities lending and borrowing transactions (SBL) fall outside the OTC securities transactions reporting regime? This is a bit unclear from the consultation conclusions.

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