



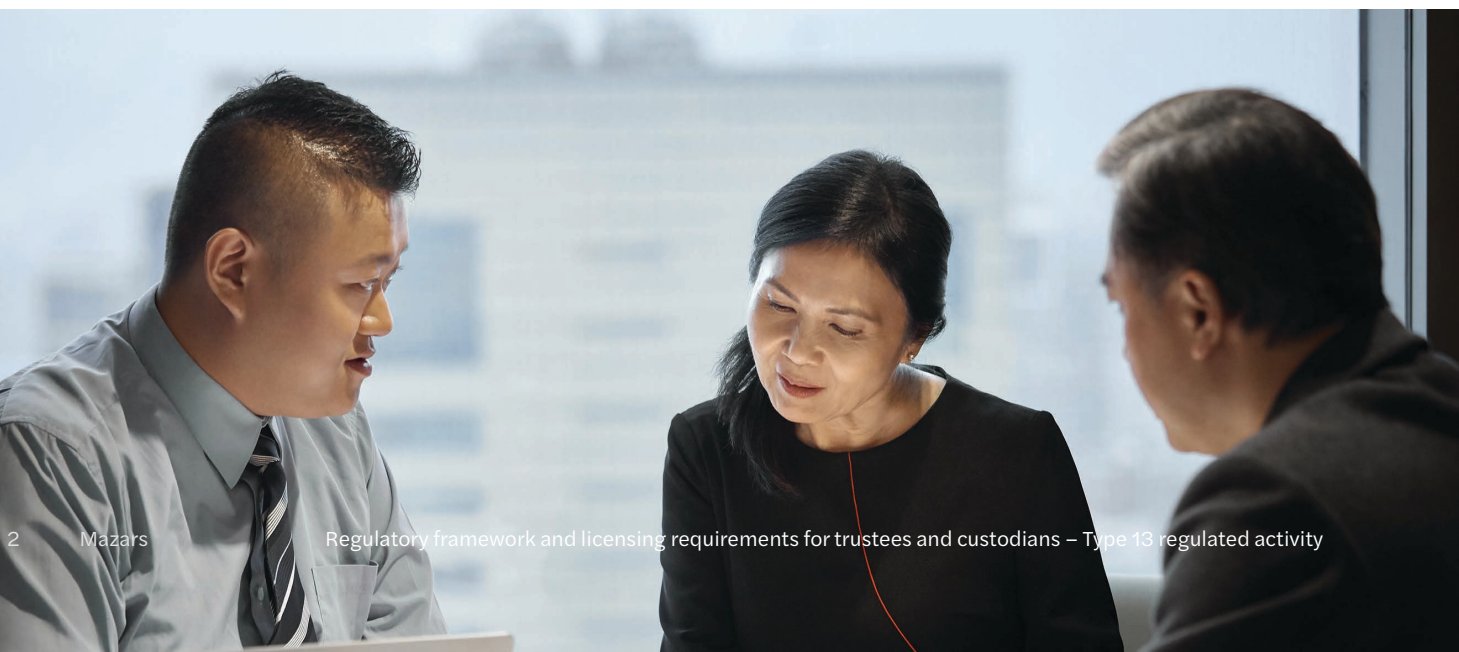
Regulatory framework and licensing requirements for trustees and custodians – Type 13 regulated activity

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Protection of fund assets has become a regulatory priority in the aftermath of the global financial crisis. Particularly, the lack of a specific licensing regime gives rise to practical difficulties in ensuring appropriate regulation and supervision on trustees and custodians of public funds.

In view of this, the Securities and Futures Commission (“SFC”) issued a Consultation Paper in September 2019 proposing a framework for a new Type 13 regulated activity (“RA 13”), to regulate top-level trustees and custodians (generally referred to as the “Depositaries”) of SFC-authorized collective investment schemes (“Relevant CIS”) under the Securities and Futures Ordinance (“SFO”). It will supervise how Depositaries safeguard scheme assets and oversee scheme operations for public funds in Hong Kong. In February 2022, the SFC released the result of the preliminary 2019 Consultation, followed by a further consultation on the proposed amendments to the relevant subsidiary legislation, SFC codes and guidelines to implement the regime. On 24 March 2023, the SFC issued the consultation conclusions on proposed legislative and code amendments on the RA 13 regime, and the legislative amendments were gazetted on the same day.

This publication outlines the key elements of the RA 13 regime and how our financial advisory service offerings can assist you in applying for an RA 13 licence.



Proposed regulatory framework of RA 13

1. Proposed Scope for Entities

Intermediaries acting as a trustee or custodian (i.e., Depositories) will be required to be licensed or registered for RA 13 if they provide depository services for a Relevant CIS¹ in Hong Kong with reference to two core functions, being:

- a. custody and safekeeping of Relevant CIS property, and
- b. oversight of the operation of the Relevant CIS to ensure that it is operated in accordance with its constitutive documents.

2. Proposed Scope for Individuals

Where an individual performs the abovementioned core function(s), he or she will be required to be licensed representatives or relevant individuals accredited to the intermediary, subject to the following scenarios:

Core Function 1: Custody and safekeeping of Relevant CIS property

If the Depository **delegates its custody and safe keeping function to another entity**, the staff of the Depository should be licensed if he/she is responsible for monitoring the performance of the delegate.

If the Depository **performs part or all of its custody and safe keeping function within the firm**, the staff of the Depository should be licensed if he/she

- is empowered to approve instructions or transactions for custody-related purposes for a relevant CIS, and
- assumes oversight duties over the performance of this function.

Core Function 2: Oversight of the operation of the Relevant CIS

The staff of a Depository should be licensed if he/she is responsible for performing the duties of this oversight function, including but not limited to:

- monitoring compliance with the investment,
- borrowing restrictions, cash flow, fund accounting and valuation, and
- the issue, repurchase, redemption and cancellation of the units or shares of the CIS.

Those engaged to provide fund administration, transfer agent, registrar services without an oversight responsibility are **excluded** from the proposed activities.

An important point to note is that RA 13 will be applied to “top-level” Depositories, who are responsible for safeguarding the fund assets and overseeing the fund operations. If the Depositories delegate their functions to third parties (e.g. sub-custodians), such delegates, sub-delegates and their staff will not fall within the proposed scope.

¹ A Relevant CIS covers SFC-authorized unit trusts, mutual funds companies, real estate investment trusts, pooled retirement funds and open-ended fund companies. To minimize duplicate regulation by the SFC and the Mandatory Provident Fund Schemes Authority, the following products will be exempted from the definition of relevant CIS:

- a. registered schemes or its constituent funds under Mandatory Provident Fund (“MPF”) Schemes
- b. approved pooled investment fund (“APIF”) which are offered only to professional investors, employers, MPF schemes, occupational retirement schemes, pooling agreements, and other APIF.

Proposed regulatory framework of RA 13

3. Proposed Amendments to Subsidiary Legislation

To reflect the introduction of RA 13, amendments to subsidiary legislation under the SFO² have been proposed by the SFC accordingly. Among the proposed amendments, the SFC has set out new provisions in the following subsidiary legislation:

Subsidiary Legislation	New Provisions for Introduction of RA 13
CMR	<ul style="list-style-type: none"> ▪ Scheme money received or held by intermediaries in conduct of RA 13 and their associated entities <ul style="list-style-type: none"> > Payment of scheme money into segregated accounts and relevant CIS accounts > Payment of scheme money out of segregated accounts and relevant CIS accounts > Treatment of interest on scheme money held in segregated accounts and relevant CIS accounts > Requirements in respect of a written instruction > Receipt of cheques for scheme money
CSR	<ul style="list-style-type: none"> ▪ Scheme securities received or held by intermediaries in conduct of RA 13 and their associated entities <ul style="list-style-type: none"> > Requirement for deposit or registration of scheme securities > Dealings with scheme securities ▪ Limitations on treatment of scheme securities
KRR	<ul style="list-style-type: none"> ▪ Record keeping requirements for intermediaries licensed or registered for RA 13 ▪ Record keeping requirements for associated entities of intermediaries licensed or registered for RA 13
FRR	<ul style="list-style-type: none"> ▪ Inclusion of scheme money and other proceeds related to relevant CIS not held in a designated segregated account in ranking liabilities of the entity licensed or registered for RA 13

It is crucial to note that the proposed amendments to the subsidiary legislation will impose obligations in respect of scheme securities, scheme money, scheme assets and relevant CIS property held by RA 13 Depositories and their associated entities.

4. Licensing Requirements

To apply for an RA 13 licence, Depositories will be subject to the same licensing requirements as other SFC regulated activities, including the appointment of responsible officers (“RO”) and managers-in-charge (“MIC”), and compliance with relevant SFC codes, guidelines and circulars. The following are some of the more typical requirements:

A. Financial resources requirement:

The entity should maintain a minimum amount of (i) paid-up share capital of HK\$10,000,000; and (ii) liquid capital of HK\$3,000,000.

B. Managers-In-Charge requirement:

The entity should ensure the MICs of the overall management oversight function and the key business lines are approved as ROs of the entity.

² Including the Securities and Futures (Client Money) Rules (“CMR”); Securities and Futures (Client Securities) Rules (“CSR”); Securities and Futures (Keeping of Records) Rules (“KRR”); Securities and Futures (Financial Resources) Rules (“FRR”); Securities and Futures (Insurance) Rules (“Insurance Rules”); Securities and Futures (Account and Audit) Rules (“AAR”); Securities and Futures (Contract Notes, Statements of Accounts and Receipts) Rules (“Contract Notes Rules”); and Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules (“OTCD Reporting Rules”)

C. Competence requirement:

The SFC plans to adopt a “grandfathering” approach to bring existing staff of public funds Depositories within the RA 13 regime. As part of the fit-and-proper requirement, the relevant staff are required to complete a 5-hour training on legal and regulatory framework for RA 13 during the transitional period, on top of the normal CPT requirements.

D. Internal Controls:

The SFC has proposed Schedule 11 to the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (“**Code of Conduct**”) for RA 13, which sets out additional requirements on management and supervision, as well as operational controls and compliance, applicable to the entity licensed or registered for RA 13 (“**Additional Requirements**”). The entity applying RA 13 licence should establish and implement internal control policies and procedures to meet the Additional Requirements which cover the following areas:

Management and Supervision

- Communication with the management company of a relevant CIS
- Appointment and oversight of delegates or third parties

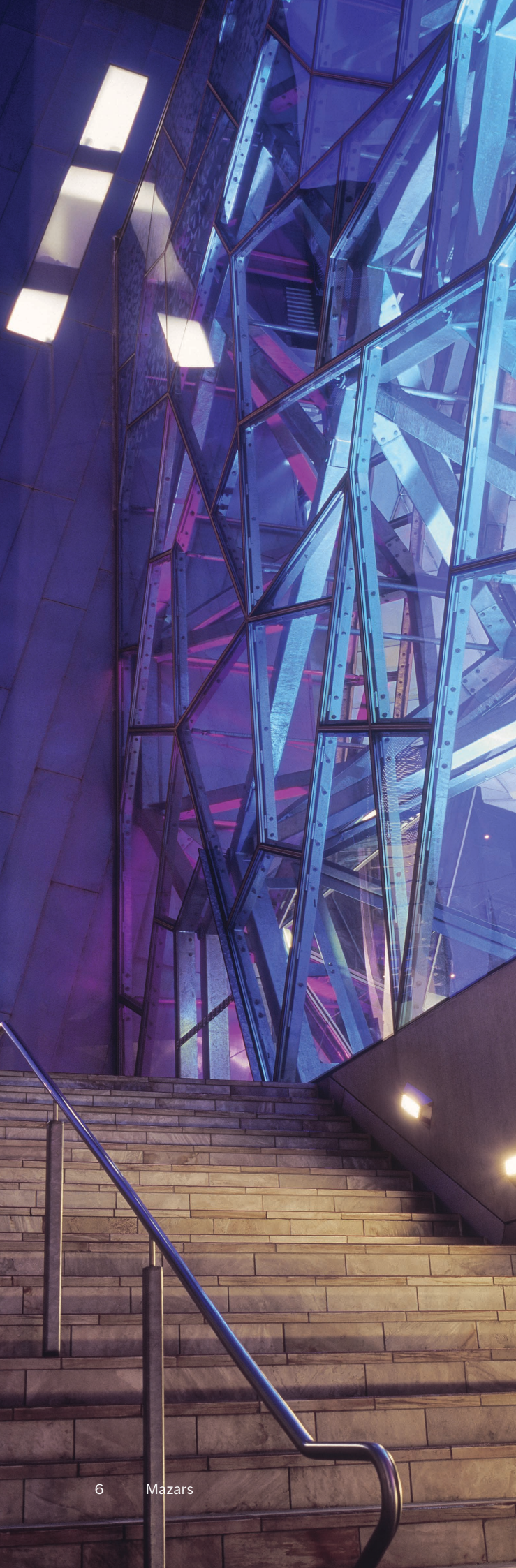
Operational Controls and Compliance

- Record keeping
- Oversight of the relevant CIS
- Subscription and redemption
- Valuation/price/net asset value calculation monitoring
- Distribution payments
- Cash flow monitoring
- Investment monitoring
- Custody and safekeeping of relevant CIS property
- Connected party transactions entered into by or on behalf of the relevant CIS
- Handling different classes of investors fairly
- Professional indemnity insurance

5. Way Forward: Implementation and Timeline

The legislative amendments have been gazetted on 24 March 2023 and the RA 13 regime is expected to come into effect on 2 October 2024, subject to the completion of the legislative process. The SFC expects that the electronic licensing forms for RA 13 will be made available in the third quarter of 2023 on its web-based platform for online submission services “WINGS”. Potential RA 13 Depositories and relevant staff members are expected to submit their licence or registration applications to the SFC within 4 months of the launch of the forms.





How can Mazars help?

At Mazars, we have extensive experience working with the diversity of financial services players. We assist major financial institutions including brokerage houses, asset managers, investment and corporate banks, retail and private banks, central banks, insurance companies and regulators in dealing with business and regulatory issues with impacts, domestic and international.

Mazars is here to assist you in complying with the regulatory standards and requirements in making a timely application for an RA 13 licence. Depending on the scope, coverage and specifics of your needs, our services would typically involve one or more of the following:

A. Assistance/advice on RA 13 licensing requirements

- I. Initiate a preliminary consultation on RA 13 licence:
 - Provide advice to management on the regulatory approval process
 - Assist in identifying and capturing regulatory issues / hurdles that may arise during the application process
 - Advise on the key areas considered by the SFC in granting the licence (e.g. governance and control arrangements, proposed business activities, financial projections, risk management controls, etc.)
 - Assist in the initial discussion with the SFC
 - Advise on practical questions during the application process
- II. Review / provide compilation advice for submission to the SFC (including the tailoring of documentation which is currently available with your institution to a standard acceptable by the regulators):
 - Review and provide compilation advice on business plan
 - Review and provide compilation advice on financial projection and pro-forma liquid capital calculation
 - Review and provide advice on organisation chart and staff plan (including qualification of RO candidates) against regulatory expectations
 - Review and provide advice on internal control systems against planned business operation and industry good practice e.g. risk management policy, anti-money laundering guideline, structure of management committees and their respective authorities, etc.
 - Review and provide advice on the overall consistency of the application documents and drafting of cover letter
- III. Provide assistance and advice in responding to further information requests from the SFC:
 - Accompany management to meetings with the SFC to address any issues and concerns arising during the approval process
- IV. Perform project management during the application process:
 - Set-up of project governance framework, structure and reporting arrangements
 - Design of project plan including milestones and working committee involvement
 - Ensure timely delivery of pre-determined targets
 - Tracking of application status with regulators

B. Design and implementation of policies and procedures

- I. Review documentation and records with a focus on the in-scope activities to ensure compliance, and
- II. Provide ongoing insights into how peer firms are dealing with the regulatory changes and any common challenges encountered along the way.

C. Training and insights

- I. Provide training and education for staff, the board and senior management on the legal and regulatory framework on the new RA 13 regime.
- II. Provide ongoing insights into how peer firms are dealing with the regulatory changes and any common challenges encountered along the way.

We also take on special projects and ad-hoc mandates. We are flexible in our approach and offerings. Please feel free to contact us with any enquiries.

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