

BRIEFING

REGULATED FUNCTIONS – LICENSING REQUIREMENTS

In early October 2019, the Securities and Futures Commission of Hong Kong (the “SFC”) took enforcement action against a Type 9 licensed corporation for employing / appointing persons, who were not licensed by the SFC, to perform regulated functions in relation to its business in regulated activities. The carrying out of a regulated function (as opposed to a regulated activity) requires the person to be licensed with the SFC (and consequently the failure of such person to be licensed will lead to disciplinary action by the SFC). This case serves as a useful clarification as to the SFC’s position on what may constitute a regulated function, in particular within the context of a fund manager managing a fund.

The concept of ‘regulated function’

The SFC’s concept of ‘regulated function’ is not new and is defined in Section 113 of Part V of the Securities and Futures Ordinance, Chapter 571 of the Laws of Hong Kong (the “SFO”) as follows:

‘regulated function’, in relation to a regulated activity carried on as a business by any person, means any function performed for or on behalf of or by arrangement with the person relating to the regulated activity, other than work ordinarily performed by an accountant, clerk or cashier.

Where a person carries out a regulated function for a licensed corporation in relation to a regulated activity carried on as a business, such person must be a licensed representative accredited to such licensed corporation pursuant to section 114(3) and (4) of the SFO. Furthermore, where such person is an executive director of the licensed corporation, he must also be approved as a responsible officer pursuant to section 125(1)(a) of the SFO.

Activities that fall within the definition of ‘regulated function’

The type of activities which constitute a regulated function, particularly within a specific business setting, have often been less clear than what constitutes carrying on regulated activities. Careful analysis must be undertaken with respect to each staff’s specific roles and responsibilities to ensure that those staff conducting regulated functions are appropriately identified and licensed, even though these staff may not be carrying out any regulated activities.

From this case, it is now clear that the following activities, carried out by an individual with respect to a Type 9 licensed corporation’s business of managing a private fund, constitute regulated functions:

1. introducing potential investors / clients to the licensed corporation;
2. answering investors’ questions about, *inter alia*, calculation of the subscription fee and the management fee of a fund managed by the licensed corporation; and
3. arranging for the execution of the subscription agreement and know-your-client questionnaire.

The person carrying out the above activities with respect to a licensed corporation's regulated activities need to be licensed regardless of whether that person is an employee, a director or an independent consultant of that licensed corporation and notwithstanding that the person is not carrying out any regulated activities for the licensed corporation.

It is interesting to note that the SFC took disciplinary action against the licensed corp for point 1 above on the basis that introducing investors / clients to the licensed corporation is a regulated function, and not on the basis of that such activities may constitute carrying out a regulated activity (ie Type 1 regulated activity).

Concluding Remarks

Licensed corporations should assess each of its unlicensed staff's roles and responsibilities within the licensed corporation and, where a staff interacts with clients, assess the extent of the interaction, to ensure that all relevant staff are appropriately licensed. It would be prudent for licensed corporations to consider whether all its staff who undertakes any so called "client-facing activities" generally are appropriately licensed. Unlicensed individuals conducting a regulated function can have serious consequences and may ultimately result in a breach of section 114(3) of the SFO, General Principle 7 and paragraphs 12.1 and 4.1 of the Code of Conduct for Persons Licensed by or Registered with the SFC. Penalties for such breaches include a public reprimand and fine.

Useful links:

<https://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=19PR92>

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[Ben Wong](#)
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[ALTQUEST LIMITED](#)
Suite 1703, 17/F., Harcourt House
39 Gloucester Road
Wan Chai
Hong Kong
<http://www.altquest.com.hk>