

Investment Management Alert

January 4, 2017

Key Points

- New Managers-In-Charge regime
- Outlines the regulatory obligations and potential liabilities of the senior management of licensed corporations who do not conduct regulated activities
- Deadlines for implementation of new regime for existing licensed corporations



SFC Introduces Measures for Enhancing the Accountability of Senior Management

Introduction

On 16 December 2016, the Securities and Futures Commission (SFC) published a *Circular to Licensed Corporations Regarding Measures for Augmenting the Accountability of Senior Management* (“Circular”), in which the SFC set out specific measures for enhancing the accountability of senior management, with the aim to:

- add clarity as to which individuals should be regarded as members of the senior management of a licensed corporation, and enhance awareness of their accountability, regulatory obligations and potential liabilities
- standardize the format for submission of information by licensed corporations and corporate licence applicants in respect of overall management structures
- better align senior management with the existing regime governing responsible officers (ROs)
- help further strengthen the corporate governance of licensed corporations.

The Regime

Meaning of Senior Management

The senior management of a licensed corporation includes, among others, its (a) directors, (b) ROs and (c) MICs (defined below). These categories are not mutually exclusive. For instance, an individual can simultaneously be a director, RO and MIC of the corporation.

Managers-In-Charge of Core Functions

The new regime requires that an individual be designated by a licensed corporation (“Managers-In-Charge” or “MIC”) to be principally responsible, either alone or with others, for managing any of the following functions of the corporation (“Core Functions”):

- overall management oversight
- key business line
- operational control and review
- risk management
- finance and accounting
- information technology
- compliance
- anti-money laundering and counter terrorist financing.

A licensed corporation may appoint one or more individuals to manage a Core Function. The SFC expects that a licensed corporation should adopt a formal document, approved by its board of directors, clearly setting out the management structure of the corporation, including the roles, responsibilities, accountability and reporting lines of its senior management personnel in each of the designated functions. Where a licensed corporation designates more than one individual to be the MICs of a particular Core Function, the board of directors should ensure that the aforesaid document contains sufficient details regarding the specific responsibilities of each MIC concerned.

In determining whether to designate an individual as an MIC for a particular Core Function, the licensed corporation should take into account the individual's seniority and authority within the corporation. An MIC should hold a senior position with sufficient authority to make decisions and manage the Core Function on a daily basis. Also, he or she should report directly, and be accountable, to the board of directors or the MIC with the overall management oversight function.

An MIC who is not a licensed person or a licence applicant need not be approved by the SFC, with the exception of the MICs with responsibility for overall management oversight and key business line function. A licensed corporation should, however, ensure that any person it employs or appoints to conduct business is fit and proper and is qualified to act in the capacity so employed or appointed.

An MIC can be located in Hong Kong or outside Hong Kong. In addition, an MIC will not necessarily be employed by the licensed corporation. However, an MIC should hold a position of authority within the licensed corporation and should be properly accountable to it.

Responsibilities of Senior Management

In stating that the contents of the Circular constitute merely a clarification of the position to date, the SFC referred to:

- General Principle 9 of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ("Code of Conduct") states that the senior management of a licensed

corporation should bear primary responsibility for ensuring the maintenance of appropriate standards of conduct and adherence to proper procedures by the corporation.

- Paragraph 14.1 of the Code of Conduct further specifies that senior management of a licensed corporation should:
 - a. properly manage the risks associated with the business of the corporation, including performing periodic evaluation of its risk management processes
 - b. understand the nature of the business of the corporation, its internal control procedures and its policies on the assumption of risk
 - c. understand the extent of their own authority and responsibilities.

The Internal Control Guidelines state that members of a licensed corporation's senior management, including its directors, chief executive officer, managing director or other senior operating management personnel (as the case may be), are ultimately responsible for the adequacy and effectiveness of the corporation's internal control systems.

Legal Liabilities of Senior Management

Under Part IX of the Securities and Futures Ordinance, the SFC may exercise disciplinary powers to sanction a "regulated person" if the person is, or was at any time, guilty of misconduct or is considered not fit and proper to be or remain the same type of regulated person.

Whether the SFC will discipline an MIC who is guilty of misconduct depends on the specific facts of each case. In determining where responsibility lies, the SFC will take into account the individual's apparent or actual authority in relation to the particular business and operations, his or her level of responsibility within the licensed corporation concerned, any supervisory duties he or she may perform, and the level of control or knowledge that he or she may have concerning any failure by the corporation or persons under his or her supervision to follow the Code of Conduct. The SFC's power to discipline an MIC applies regardless of where that MIC is located.

Roles and Responsibilities of the Board of Directors of a Licensed Corporation

The board of directors of a licensed corporation, to which the senior management is accountable, has the ultimate responsibility for the conduct, operations and financial soundness of the corporation. The board of directors retains responsibility for delegated decisions and is required to have systems and controls in place to supervise those who act under the delegated authority.

The SFC expects that the licensed corporation should adopt a formal document, approved by the board of directors, clearly setting out the management structure of the corporation, including the roles, responsibilities, accountability and reporting lines of its senior management personnel.

The management structure of a licensed corporation (including its appointment of MICs) should be approved by its board of directors. Furthermore, the board of directors should ensure that each of the

corporation's MICs has acknowledged his or her appointment as an MIC and the particular Core Function(s) for which he or she is principally responsible.

Submission of Management Structure Information

The SFC expects an applicant for an SFC licence to provide information regarding its MICs and its organisational chart in its licence application.

In respect of each of its MICs, an applicant for an SFC licence should submit the following particulars via the SFC Online Portal using a new form (Supplement 8A):

1. full name
2. identification information
3. job title
4. place of residence
5. the Core Function(s) which he or she is in charge of
6. the job title(s) of the person(s) to whom he or she reports within the corporation and, if applicable, within its corporate group.

In addition, the applicant should submit an organisational chart illustrating its management and governance structure, business and operational units, and key human resources and their respective reporting lines. The chart should include all MICs engaged by the corporation, their respective reporting lines and the job titles of the persons reporting directly to these MICs in relation to the operations of the corporation.

A licensed corporation should notify the SFC of any changes in its appointment of MICs (including any new appointment and cessation of appointment) or any changes in the particulars of its MICs within seven business days of the changes. Where a change involves a new appointment or cessation of appointment, or a change in the particulars referred to in items (5) and (6) above, the licensed corporation should also submit an updated organisational chart reflecting the same.

Next Steps for Existing Licensed Corporations

The new regime will come into effect on 18 April 2017.

Existing investment managers will need to submit the MIC information and organisational charts to the SFC on or before 17 July 2017. The MICs of the overall management oversight function and the key business line function who are not already ROs will be required to make an application for approval to become ROs on or before 16 October 2017.

The full text of the Circular can be accessed via the link below:

<http://www.sfc.hk/edistributionWeb/gateway/EN/circular/openFile?refNo=16EC68>

Contact Information

If you have any questions regarding this alert, please contact the Akin Gump Strauss Hauer & Feld lawyer with whom you usually work or:

Anne-Marie Godfrey

anne-marie.godfrey@akingump.com

+852 3694.3040

Hong Kong