



Hong Kong

September 2017

SFC HONG KONG FINTECH SANDBOX LAUNCHED AND HKMA HONG KONG SMART BANKING AND ENHANCED FINTECH SANDBOX

On 29 September 2017, the Securities and Futures Commission (SFC) launched the SFC Regulatory Sandbox¹ (**Hong Kong Fintech Sandbox**) which will provide a confined regulatory environment for qualified firms to operate under the Securities and Futures Ordinance (Cap 571) (SFO). This follows the launch of the Hong Kong Monetary Authority (HKMA) Fintech Supervisory Sandbox in September 2016 (**HKMA Hong Kong Sandbox**). For information about the HKMA Hong Kong Sandbox, please see Charltons' October 2016 newsletter². On 29 September 2017, the HKMA also announced several initiatives that prepare Hong Kong to enter a New Era of Smart Banking³, including the Enhanced Fintech Supervisory Sandbox 2.0.

Hong Kong Fintech Sandbox

The advantage of the Hong Kong Fintech Sandbox is that it will encourage firms to utilise financial technology (**Fintech**), thereby expanding the range and quality of goods and services for investors, as well as be of benefit to the Hong Kong financial services industry. At the same time the Hong Kong Fintech Sandbox will establish a regulatory scheme prior to Fintech being used on a fuller scale.

Given that the underlying technology may be novel, it will be important from market integrity and investor protection purposes, to examine and monitor in a confined regulatory

- ¹ <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR126>
- ² <https://www.charltonslaw.com/hkma-launches-a-fintech-supervisory-sandbox-fss/>
- ³ <http://www.hkma.gov.hk/eng/key-information/press-releases/2017/20170929-3.shtml>

environment, the reliability of the delivery of the firm's financial services and its internal control systems. Here, the Hong Kong Fintech Sandbox may provide a testing ground before the financial services are allowed to be expanded and made available to a wider public in Hong Kong. The Hong Kong Fintech Sandbox would enable qualified firms, through close dialogue with and supervision by the SFC under the licensing regime, to readily identify and address any risks or concerns relevant to their regulated activities.

The Hong Kong Fintech Sandbox should not be regarded as a mechanism to avoid relevant legal and regulatory requirements. Accordingly, Hong Kong's SFC will not remove any regulations that are fundamental to investor protection. For example, a qualified firm operating in the Hong Kong Fintech Sandbox will be subject to a fit and proper requirement and must comply with the applicable financial resources requirements. The SFC points out that these obligations are not burdensome, and that the financial resources requirements are a practical necessity for operating a credible business.

The major characteristics of the Hong Kong Fintech Sandbox are:

(1) Eligibility:

Both licensed corporations and start-up firms that intend to carry on a regulated activity under the SFO may be eligible to enter the Hong Kong Fintech Sandbox. The qualified firm must be fit and proper, apply innovative technologies, and be able to show a genuine and serious commitment to carry on regulated activities through the use of Fintech.

It is a requirement under the SFO that no person may carry on a business in a regulated activity unless the person is licensed by the SFC to conduct such regulated activity. Thus, a qualified person in the Hong Kong Fintech Sandbox will be required to be licensed and comply with the applicable requirements, such as the applicable financial resources requirements.

(2) Licensing conditions:

For the purpose of minimising risks to investors, the SFC may impose licensing conditions on a qualified firm operating in the Hong Kong Fintech Sandbox. Licensing conditions may include restrictions on the firm's business in regulated activities, appropriate compensation schemes for investors, or periodic supervisory audits by the SFC.

(3) Closer monitoring and supervision by the SFC:

The SFC may place qualified firms operating in the Hong Kong Fintech Sandbox under closer SFC monitoring and supervision. Here, the SFC may engage in frank discussions with the firms, pointing out compliance areas which require additional improvement, for example, in relation to internal controls and risk management. These discussions will enable firms to refine their business models and deal with any risks or concerns arising at the initial stage.

(4) Investor protection measures:

Qualified firms are expected to have adequate investor protection measures that deal with actual or potential risks or concerns identified when they operate in the Hong Kong Fintech Sandbox. For example, qualified firms will be required to inform their clients that they are operating in the Hong Kong Fintech Sandbox, and give complete disclosure of potential risks and any applicable compensation arrangements.

(5) Exit:

When a qualified firm has shown that its technology is reliable and fit for purpose, and that its internal control procedures have adequately addressed all identifiable risks, the firm may apply to the SFC for the removal or variation of any licensing conditions. The SFC may then allow the firm to conduct its regulated activities on the same conditions as licensed firms which operate outside the Hong Kong Fintech Sandbox. Alternatively, if the SFC considers that a firm in the Hong Kong Fintech Sandbox is not fit and proper to remain licensed, it may revoke its license.

Hong Kong's SFC expects that the great majority of applicants for a corporate license, including robo-advisors and other firms making use of Fintech, to be subject to the normal license process without any need to enter the Hong Kong Fintech Sandbox. The Licensing Department of the SFC is open for discussions with any firm concerning any proposed application to enter into the Hong Kong Fintech Sandbox, and additional information may be found through the SFC Fintech Contact Point⁴.

HKMA Hong Kong Smart Banking and Enhanced Fintech Sandbox

The HKMA Hong Kong's New Era of Smart Banking initiatives include the Enhanced Fintech Supervisory Sandbox 2.0, which comprises three features:

- a Fintech Supervisory Chatroom (**Chatroom**) will be established to provide quick feedback to banks and tech firms at an early stage of their Fintech projects;
- tech firms may be able to directly access the sandbox by seeking feedback from the Chatroom without necessarily going through a bank; and
- the sandboxes of the HKMA, the SFC and the Insurance Authority will be connected so that there will be one point of entry for pilot trials of cross-sector Fintech products.

The HKMA intends to launch the Enhanced Fintech Supervisory Sandbox 2.0 by the end of 2017.

Other initiatives under the New Era of Smart Banking include:

- Faster Payment System (FPS) – the FPS, scheduled for a September 2018 launch, will support the use of mobile phone numbers or email addresses for payments in Hong Kong dollars and Renminbi. Both banks and Stored Value Facilities (SVF) operators will be able to participate in the FPS. Further, an industry working group has been set up to facilitate a common QR code standard, so as to increase convenience for customers and merchants, and encourage the use of mobile retail payments generally.
- Promotion of Virtual Banking – the HKMA supports the introduction of virtual banks in Hong Kong, and will undergo industry consultation to review and amend the Guide to Authorization of Virtual Banks that it issued in 2000.

⁴ <http://www.sfc.hk/web/EN/sfc-fintech-contact-point/>

- Banking Made Easy initiative – a new HKMA task force will be established to work with the banking industry so as to reduce regulatory frictions in customers' digital experience.
- Open Application Programming Interface (API) – by the end of 2017, the HKMA intends to finalise a policy on Open API which will facilitate an increased adoption of API by the banking sector. This will promote innovation and improve financial services through collaboration between banks and tech firms.
- Closer cross-border collaboration – increased efforts by the HKMA to collaborate with authorities in other jurisdictions in relation to the development of Fintech.
- Enhanced research and talent development – the HKMA will collaborate with the Hong Kong Applied Science and Technology Research Institute, Science Park and Cyberport to foster the introduction of new technology and processes that will increase convenience and speed for banking customers.

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