

31 August 2010

Circular to Licensed Corporations

Code of Conduct Requirements with respect to Derivative Products

The Commission would like to remind licensed corporations to ensure compliance with the obligations under the Code of Conduct¹ when providing services to clients with respect to derivative products. Currently in the Hong Kong market, these products would generally include derivative warrants, callable bull/ bear contracts, and those exchange-traded funds that invest in derivative instruments designed to replicate the performance of an index. In particular, licensed corporations should be mindful of the following requirements:

1. A licensed corporation is required under the Code of Conduct to know its clients and ensure the transaction is suitable for a client when making a recommendation or solicitation to the client.
2. A licensed corporation should assure itself that the client understands the nature and risks of the derivative products and has sufficient net worth to be able to assume the risks and bear the potential losses of trading in the products.

Furthermore, under the new paragraph 5.1A of the Code of Conduct which will come into effect in June 2011, where a client who has been characterized as without knowledge of derivative wishes to purchase a derivative product which is traded on an exchange and the licensed corporation has not solicited or provided a recommendation to the client, the licensed corporation should explain the risks associated with the product to the client.

Licensed corporations are reminded to put in place appropriate measures to ensure that their staff are familiar with the risks and features of the investment products and comply with the applicable requirements when serving their clients.

Should you have any queries regarding the contents of this circular, please contact Ms Lorraine Chan on 2842-7751.

Intermediaries Supervision Department
Securities and Futures Commission

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¹ Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission