

**Appendix 3**

**Compliance Reminder on China Connect Rules**

*(Applicable to China Connect Exchange Participants and Trade-through Exchange Participants only)*

China Connect Exchange Participants (“CCEPs”) and Trade-through Exchange Participants (“TTEPs”) are required to comply at all times with the relevant rules and regulations regarding to the trading of China Connect Securities as stipulated in the Rules of the Exchange (“SEHK Rules”), including but not limited to Chapters 5, 14, 14A and 14B.

In the 2019 Annual Attestation and Inspection Programme, some CCEPs and TTEPs were found deficient in the following areas:-

**1. Broker-to-Client Assigned Number (BCAN)**

- ***Failure to obtain client written consents.*** We noted that some CCEPs only issued one-way notification but did not obtain written consents from each individual client regarding the collection, storage, use, disclosure and transfer of personal data in relation to its clients.
- ***Failure to properly assign BCANs.*** We noted that some CCEPs assigned different BCANs to the same client holding multiple accounts and provided inaccurate client information in the BCAN-CID Mapping File.
- ***Insufficient controls / arrangements to ensure that BCANs are kept confidential.*** We noted that some CCEPs displayed the BCANs in some internal systems and failed to ensure that the use of and accessibility to BCANs are strictly restricted to a need-to-know basis.

CCEPs and TTEPs are reminded to observe and comply with SEHK Rule 1425A and paragraphs 4, 21 and 22 of the Northbound Investor ID Model FAQ<sup>1</sup>. To these ends, CCEPs and TTEPs should put in reasonable and effective controls / arrangements to obtain the necessary client approval / consent for handling and transferring of clients’ confidential information, assign unique BCAN to each client and keep BCANs strictly confidential.

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<sup>1</sup> <https://www.hkex.com.hk/-/media/HKEX-Market/Mutual-Market/Stock-Connect/Reference-Materials/Northbound-Investor-ID-Model/NB-Investor-ID-FAQ-Eng.pdf?la=en>

## 2. Client Agreement and Risk Disclosure

- ***Insufficient provisions in client agreements or other account opening documents to ensure clients acknowledged and are aware of the differences in the restrictions, requirements, conditions and risk associated with Northbound trading of China Connect Securities, as well as the scope of services available to clients.***
- ***Failure to communicate clearly the scope of services provided to the clients.*** We noted that some CCEPs included in the client agreement certain provisions and clauses related to services which they did not provide to the clients.

To comply with the requirements under SEHK Rules 14A10, 14B10 and 14B06(16) to (18), and 1.26 and 1.53 of the FAQ, CCEPs and TTEPs should include in the client agreement sufficient provisions covering Northbound trading of China Connect Securities including the risks involved, and clearly communicate the scope of services provided to the clients.

## 3. Pre-trade Controls and Post-trade Monitoring

- ***Lack of effective and sufficient pre-trade controls and post-trade monitoring on their Northbound trading activities.***

CCEPs and TTEPs are reminded to observe and comply with SEHK Rules 14A06(4), 14B06(5), 14A06(9)-(10), 14B06(11)-(12), 14A17, 14B17, 1421(2), 1428(1), 1432 and 1433 in particular. To these ends, CCEPs and TTEPs should put in place reasonable and necessary controls that can effectively prevent day trading, overselling of sellable inventory positions, misflagging of short selling orders and mischievous behavior towards the use of the Northbound quota and ensure compliance with all applicable laws with regard to the Northbound trading of China Connect Securities including but not limited to laws and regulations prohibiting insider dealing, market manipulation, price rigging, false trading or the creation of a false or misleading appearance of active trading on any China Connect Securities.

## 4. Margin Trading

- ***Providing funds or securities margin financing arrangement to their clients on a portfolio basis.*** We noted that some CCEPs provided securities margin financing arrangement to their clients, by reference to the aggregated collateral values of all securities held in their portfolio, to purchase securities including China Connect Securities which may **not** be confined to those included in the List of Eligible SSE/SZSE Securities for Margin Trading.

Under SEHK Rules 14A15 and 14B15, CCEPs and TTEPs shall ensure that Margin Trading is confined to those China Connect Securities that are included in the List of Eligible SSE/SZSE Securities for Margin Trading published by the Exchange from time to time.

## 5. Trading of ChiNext Shares

- **Failure to put in place adequate controls to ensure that only Institutional Professional Investors (“IPIs”) are allowed to buy ChiNext shares.** In particular, we noted that some CCEPs failed to conduct (i) regular review on the IPI status of their clients, and/or (ii) regular and appropriate post trade review which covers all clients including the underlying clients of intermediary clients.

The Exchange is of the view that effective controls on pre-trade and post-trade level are essential to ensure compliance with the investor eligibility requirement for trading in ChiNext shares under SEHK Rules 14B06(16) to (18).

## 6. Off-exchange Trades or Transfers

- **Inadequate policies, procedures and controls to ensure that off-exchange trades or transfers are prohibited.** In particular, we noted that some CCEPs failed to establish written policies and procedures in relation to handling of off-exchange trades or transfers for the purposes prescribed under SEHK Rules 14A12 and 14B12.

To comply with the requirements under SEHK Rules 14A12 and 14B12, CCEPs and TTEPs shall put in place adequate controls to prevent or detect non-trade transfers or to handle those permitted under SEHK Rules 14A12(2) and 14B12(2).

## 7. Policies and Procedures

- **Inadequate and lack of regular review on policies and procedures.** We noted that the written policies and procedures of some CCEPs contained inadequate details and guidance relating to trade monitoring, margin trading, shareholding monitoring and non-trade transfer.

The Exchange wishes to remind CCEPs that adequate policies and procedures should be established to ensure ongoing compliance with the relevant rules and requirements. Regular review and revision should also be conducted to ensure they are consistent, effective and up-to-date.

## 8. Staff Training

- **Inadequate staff training.** Some CCEPs did not provide adequate and product-specific training for staff involved in the business activity in the Priority Areas, and merely relied on on-the-job training through sharing and coaching by senior staff members.

To foster a culture of compliance, the Exchange wishes to remind CCEPs that they should provide staff with adequate and appropriate training both initially and on an ongoing basis.