

Appendix 1

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 at all times, comply with the relevant rules and regulations regarding 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 2024 Annual Attestation and Inspection Programme, some CCEPs and TTEPs were found to be deficient in the following areas:

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

▪ ***Multiple BCANs assigned for the same client***

- (i) Clerical mistakes during client onboarding process, staff oversight in handling client profile updates, and inaccurate input of client data were common reasons that led to multiple BCANs being generated and assigned to the same client.
- (ii) Some CCEPs assigned multiple BCANs to clients for whom the CCEP has maintained multiple account records. In this circumstance, the CCEP has already assigned a BCAN to the client's first account but subsequently, further assigned another BCAN when the client set up a second account, resulting in two BCANs assigned for the same client at the same time.

▪ ***Accurate and Up-to-date Information in the BCAN-CID Mapping File***

Inaccurate Client Identification Data (“**CID**”)

- (i) Due to insufficient understanding or misunderstanding of the BCAN requirements, clerical mistakes, staff oversight, absence of diligent review of BCAN-CID Mapping File by CCEPs' affiliate, system error and/or inadequate User Acceptance Test (UAT) performed during system upgrade, some CCEPs/TTEPs failed to provide the exact CID as shown on clients' official identity documents, including but not limited to incorrect client name, identity number, ID type, and country/region of issuance. Some CCEPs also mistakenly included *alias* of client name and/or internal reference in the BCAN-CID Mapping File.
- (ii) Due to incorrect system setting, some CCEPs mistakenly used a particular ID type by default for the BCAN-CID Mapping File input.

- (iii) For corporate clients, some CCEPs/TTEPs incorrectly used the Business Registration Certificate as identity documents instead of using the Certificate of Incorporation (Col) or other official incorporation documents / Legal Entities Identifiers (LEI).

Incorrect client type classification

- (iv) Due to insufficient understanding of the classification requirement and lack of/ineffective maker-checker process for client data input, some CCEPs/TTEPs mistakenly assigned the house accounts of their corporate clients and/or discretionary account under *Proprietary or Principal Trading* (Type 5), which is intended for the house accounts of the CCEP/TTEP or that of their affiliates only.
- (v) Due to human errors and misunderstanding of the BCAN requirements, some CCEPs mistakenly assigned their house accounts under *Legal Entity – Fund* (Type 3), which is intended for fund clients only.
- (vi) Due to human errors, insufficient understanding or misunderstanding of the BCAN requirements and/or deficiencies in system design, some CCEPs mistakenly assigned their own house account and/or their affiliates' house account under *Legal Entity – Fund managers and others* (Type 4), which is intended for fund managers or other corporate clients only.
- (vii) Due to legacy issue, human errors, insufficient understanding of the BCAN requirements and/or internal policy prohibiting activation of China Connect Services for client trading in agency capacity, some CCEPs mistakenly assigned corporate clients and joint accounts under *Individual* (Type 1), which is intended for individual clients only.
- (viii) Some CCEPs failed to assign the corresponding client type for its own or affiliate's fund or fund manager clients, and wrongly classified fund clients under *Legal Entity – Fund managers and others* (Type 4), or fund managers or other corporate clients under *Legal Entity – Fund* (Type 3).

Incomplete / Not up-to-date information

- (ix) Due to system limitations, some CCEPs failed to remove obsolete data from the BCAN-CID Mapping File. Some of them also mistakenly deleted existing client BCAN from the BCAN-CID Mapping File.
- (x) Due to system limitations, some CCEPs failed to input client names in languages other than English (including Chinese) in the BCAN-CID Mapping File as required.

- ***Insufficient controls / arrangements to ensure BCAN-CID Mapping File data accuracy***
 - (i) ***No regular review.*** Some CCEPs/TTEPs did not conduct any regular review of the data in the BCAN-CID Mapping File and failed to detect inaccurate client type assignments and/or incorrect CID input.
 - (ii) ***Absence or ineffective maker-checker process for client data input.*** Some CCEPs/TTEPs did not put in place maker-checker process to ensure client data is accurately inputted into their internal systems. While some CCEPs/TTEPs represented that they had put in place such maker-checker process and/or have such process documented in their written policies and procedures, there was no audit trail to support their representation, or the audit trail did not show a clear segregation of maker-checker duties. The absence of, or an ineffective maker-checker control, could contribute to inaccurate client type assignments and/or incorrect CID input.
 - (iii) ***Lack of adequate control over data accuracy regarding BCAN assigned by its affiliate to underlying clients.*** Some CCEPs on-boarded their non-EP affiliates as their clients where BCANs were assigned to the affiliates' underlying clients. However, they did not put in place adequate control to ensure data accuracy on those BCANs concerned, leaving the data inaccuracy issue at the affiliates level undetected.

- ***Insufficient controls / arrangements to ensure BCAN confidentiality and BCAN access granted strictly on a need-to-know basis only***

Some CCEPs unnecessarily displayed BCANs in their internal systems and some CCEP/TTEPs unnecessarily granted BCAN access to Responsible Officers, dealers, compliance staff, settlement staff, finance staff, licensed representatives or account executives without proper or adequate justifications provided. These CCEPs/TTEPs are considered failing to ensure that the use of and accessibility to BCANs are strictly restricted on a need-to-know basis.

- ***BCAN Consent***
 - (i) Some CCEPs' client consent did not adequately cover the collection, storage, use, disclosure and transfer of personal data in relation client's BCAN and CID for the purposes as set out in SEHK Rule 1425A(5).
 - (ii) Some CCEPs did not follow up and confirm with their clients who refused to provide the necessary consent that he/she had not otherwise provided such consent to other CCEPs for Northbound Trading, but at the same time allowed them to transfer-in and sell China Connect Securities through their accounts.

- ***Insufficient controls to ensure correct BCAN tagging***

Human errors and staff oversight in processing high-touch orders have led to incorrect BCAN tagging.

- ***Incorrect usage of BCAN error report***

Due to misunderstanding of the relevant requirement, some CCEPs were found to have used BCAN error reports for reporting trade errors other than BCAN tagging, which in fact should have been handled by submission of Trade Discrepancy Forms. CCEPs should note that BCAN error reports should not be used to reflect any trade reallocation from client accounts to their house accounts resulting from trade errors such as incorrect trade quantity / price / stock. CCEP should make reference to relevant publication concerning the usage of Trade Discrepancy Forms and BCAN Error Reports (Ref. No.: [MSM/005/2024](#)).

- ***Incorrect BCAN assignment for CCEPs***

Due to misunderstanding of the BCAN requirements, some CCEPs assigned BCAN to another CCEP but not for contingency purpose. Pursuant to SEHK Rule 590, it permits only a TTEP to trade through a CCEP. Accordingly, as an executing CCEP, it should not accept instructions from another CCEP or grant China Connect trading permission to another CCEP unless for contingency purpose.

- ***Incorrect BCAN assignment for TTEPs***

Due to misunderstanding of the BCAN requirement or clerical mistakes, a single BCAN, instead of a BCAN range was assigned to a TTEP. In fact, a CCEP executing for TTEPs should set aside BCAN ranges for each of its TTEPs for them to assign to their clients so that BCANs used by the CCEP will not overlap with those used by its TTEPs. The BCANs of a TTEP for proprietary trading should also be within the same BCAN range designated by its executing CCEP.

- ***Registration of CHN BCANs***

With effect from 25 July 2022, neither CCEPs nor TTEPs shall register new BCAN for clients who are Mainland investors, i.e. no registration of new BCANs with 'CHN' as the country/region of issuance ("**CHN BCANs**"). Due to staff oversight and system configuration errors, some CCEPs registered or attempted to register CHN BCANs in the BCAN-CID Mapping File.

CCEPs and TTEPs are reminded to observe and comply with the BCAN requirements as set out in SEHK Rule 1425A, and to refer to various guidance, including but not limited to the [Northbound Investor ID Model FAQ](#), [Guidance Notes on BCAN-CID Mapping File](#), [BCAN – CID Mapping File Data Record Examples](#) and [Northbound Trading Investor ID Model - System File Interface Specification](#).

In this regard, CCEPs and TTEPs should put in place necessary controls and arrangements, and regularly assess their effectiveness, such that they can, amongst other things, (i) assign unique BCAN to each of their Northbound trading clients, (ii) ensure BCAN client type and CID submitted to the Exchange is accurate and up to date, (iii) keep BCANs strictly confidential, (iv) ensure BCAN assignment is correct, and (v) ensure BCAN consent with adequate coverage is obtained from clients before proceeding with order placing. Regardless whether the controls and arrangements are performed by CCEPs or TTEPs themselves or are outsourced to / handled by their affiliates, CCEPs and TTEPs are accountable for the effectiveness of the controls and arrangements pertaining to the aforementioned areas. In addition, CCEPs and TTEPs are reminded that once a BCAN was assigned to a client, it shall not be changed and shall not be reused for other clients, unless with the prior written approval from the Exchange. Comprehensive guidelines should be in place to ensure that the controls and arrangements are being implemented as designed and in a consistent manner. Furthermore, adequate training should be provided to staff involved in BCAN-related process on a regular and on-going basis.

The Exchange wishes to draw CCEPs' and TTEPs' attention to some of the good practices that we observed during the onsite inspection:

- (i) In order to avoid treating a client with multiple accounts as different clients, and inadvertently assigning that client with multiple BCANs as a result, some CCEPs/TTEPs would request the client to declare in its account opening form that he/she has not opened any account with the firm previously. Some CCEPs/TTEPs would also compare other client information (e.g. address, contact number) to identify any potential matches.
- (ii) To handle multiple trading accounts setup arrangement (e.g. cash and margin accounts, master/sub-accounts, fund and fund manager accounts etc.) in a prudent manner, some CCEPs/TTEPs assign BCANs based on the ID number for individual clients and business registration number for corporate clients, rather than on trading account level.
- (iii) Some CCEPs/TTEPs conduct independent review on all client information obtained during onboarding to ensure data accuracy.
- (iv) Some CCEPs/TTEPs perform regular review on all data in the BCAN-CID Mapping File, including but not limited to changes (e.g. addition/deletion/amendment) and timely reconciliation between internal system records and the BCAN-CID mapping file to ensure the CIDs submitted to the Exchange are complete, accurate and up-to-date.
- (v) Adopt automation and minimize manual intervention as much as possible. Where manual procedures are involved in BCAN assignment and submission process, maker-

checker mechanism is implemented with audit trail and properly documented in the written policies and procedures.

CCEPs and TTEPs are encouraged to make reference to our Compliance Bulletin (Ref. No.: [MSM/005/2024](#), [MSM/007/2023](#) and [MSM/002/2022](#)) which listed out some common deficiencies and related issues identified, and also good practices observed with respect to compliance with the relevant BCAN requirements.

2. **TTEP registration and Provision of brokerage service in China Connect Securities to CCEPs**

▪ ***TTEP registration***

When onboarding clients who are also Exchange Participants (“EPs”), some CCEPs failed to conduct thorough due diligence checks, which include but not limited to checking their trading capacity to ensure that the EP clients that wish to conduct trading through the China Connect Service for the account of their clients have been registered as TTEPs.

▪ ***Provision of brokerage service in China Connect Securities to CCEPs***

- (i) Some CCEPs activated China Connect trading services for their CCEP clients without ascertaining their purposes of activating such services at their firm.
- (ii) Pursuant to SEHK Rule 590, only a TTEP (not CCEP) is allowed to trade through a CCEP; the only exception would be for contingency purpose.

The Exchange wishes to draw EPs’ attention to the following:

- (i) Pursuant to SEHK Rules 590(2) and 590(4) and as stated in paragraph 1.43 of the [Stock Connect Frequently Asked Questions \(“Stock Connect FAQ”\)](#), EPs who are not registered as CCEPs but wish to provide services to their clients to trade in China Connect Securities may do so through CCEPs for the account of their clients as TTEPs.
- (ii) TTEPs are required to provide a declaration to the Exchange confirming such matters as the Exchange may require, including the TTEPs’ awareness of and the ability and undertaking to comply with the applicable laws in respect of the trading of China Connect Securities. Among other things, their systems must have the capability of conducting pre-trade checking, client agreements must be amended to allow for Northbound trading and appropriate arrangements must be made to ensure that their clients understand the risks of investing in China Connect Securities, etc. TTEPs are required to abide by the rules governing Northbound trading under the SEHK Rules as if they were CCEPs. From time to time, the Exchange may publish on the HKEX website (or by such other means as it considers appropriate), a list of TTEPs who have

submitted declarations to the Exchange. TTEPs must not provide instructions to a CCEP, whether directly or indirectly, to trade in China Connect Securities for the account of their clients before their names are included in such published list of TTEPs.

- (iii) CCEPs should put in place adequate controls to ensure that their intermediary broker clients, who are EPs and conduct trading for their clients, must be registered as TTEPs both initially and on an on-going basis.

3. Trading of ChiNext and STAR Shares

- ***Insufficient communication of regulatory requirements with clients***

Due to operational errors, some CCEPs did not provide their clients who engaged in trading China Connect Securities with the documentation containing regulatory requirements for trading ChiNext and STAR shares, including explanation on the relevant investor eligibility requirements.

- ***Inadequate pre-trade controls in place***

Some CCEPs put in place pre-trade controls to block all clients / non-Institutional Professional Investors (“IPI”) from trading ChiNext shares but did not update the relevant system configurations or put in place other pre-trade controls for STAR shares (which share the same investor eligibility requirements) due to staff misunderstanding and staff oversight.

- ***Inadequate procedures and controls for a timely identification of non-compliance incident in relation to investor eligibility requirements***

- (i) Some CCEPs/TTEPs did not put in place adequate post-trade reviews on direct clients and/or intermediary broker clients to identify potential violation of the investor eligibility requirements for trading ChiNext and STAR shares. This was attributed to their sole or heavy reliance on pre-trade controls such as system controls to block all clients/non-IPIs from trading ChiNext and STAR shares, which is considered insufficient for the purpose of timely identification of non-compliance incidents.
- (ii) Some CCEPs and TTEPs only conducted post-trade review at direct client level but failed to cover all clients including the underlying clients of the intermediaries.
- (iii) Some CCEPs represented that they had performed post-trade review, which, however, was not covered by adequate documentation.

The Exchange is of the view that effective controls on client onboarding, pre-trade and post-trade level are essential to ensure compliance with the investor eligibility requirements for trading in ChiNext and STAR shares respectively under SEHK Rules 14A06(13) to (15) and 14B06(16) to (18).

The Exchange wishes to draw CCEP's and TTEP's attention to a good practice we observed during the onsite inspection. We noted that some CCEPs have adopted automation to utilize ChiNext/STAR product flagging directly from the websites¹ of Shanghai and Shenzhen Stock Exchanges respectively on a daily basis to help them to ascertain whether a particular stock is listed on the ChiNext or STAR board, followed by a reconciliation conducted between the information obtained from the exchange data feeds and third party vendor on a real time basis.

CCEPs and TTEPs are also encouraged to make reference to our Compliance Bulletin (Ref. No.: [MSM/005/2024](#), [MSM/009/2023](#) and [MSM/002/2022](#)), which listed out some common deficiencies and related issues identified, and good practices observed with respect to compliance with the relevant investor eligibility requirements.

4. Policies and Procedures

- ***Inadequate policies and procedures, and lack of regular reviews***

- (i) ***BCAN requirements.*** Some CCEPs/TTEPs failed to establish adequate written policies and procedures in relation to the handling of BCAN assignment and CID collection for the purpose of ensuring compliance with the BCAN requirements under SEHK Rule 1425A.
- (ii) ***TTEP registration.*** The written policies and procedures of some CCEPs did not contain adequate details and guidance relating to the provision of brokerage services to EPs for the purpose of ensuring compliance with the TTEP registration requirement under SEHK Rule 590.
- (iii) ***Client consent.*** No written policies and procedures in place to document the workflow for not accepting clients to transfer in China Connect Securities if the clients refused to provide prior written consent.

¹ SSE: <http://www.sse.com.cn/assortment/stock/list/share/>
SZSE: <http://www.szse.cn/market/product/stock/list/index.html>

- (iv) **ChiNext and STAR trading.** The written policies and procedures of some CCEPs did not contain adequate details and guidance in relation to (i) regular review of the stock code range to ensure such range is accurate and up-to-date, (ii) regular and appropriate post-trade review to cover all clients, and/or (iii) handling of intermediary clients with dual capacity, for the purpose of ensuring compliance with the investor eligibility requirement for trading in ChiNext and STAR shares respectively under SEHK Rules 14A06(13) to (15) and 14B06(16) to (18).
- (v) **Client onboarding and communication of regulatory requirements.** Some CCEPs/TTEPs failed to establish adequate written policies and procedures in relation to the handling of client onboarding and communication of regulatory requirements as well as prior arrangements during the reactivation of client accounts.

Non-comprehensive policies and procedures may pose compliance risk as well as operational risk on the participants. The Exchange wishes to remind CCEPs and TTEPs of the need to establish and maintain comprehensive policies and procedures to ensure compliance with all relevant rules and requirements. Regular review and revision should also be conducted to ensure they are consistent, effective and up-to-date.

5. Staff Training

- **Inadequate staff training**

Some CCEPs/TTEPs did not provide adequate and product-specific training for staff involved in the business activities of the Priority Areas, but 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 and TTEPs that they should provide their staff with adequate and appropriate training both initially and on an on-going basis.