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**SECURITIES AND FUTURES ORDINANCE (Chapter 571)**

Pursuant to section 399 of the Securities and Futures Ordinance, the Securities and Futures Commission publishes the following Guidelines on Online Distribution and Advisory Platforms ('the Guidelines'). The Guidelines shall become effective on 6 April 2019.

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**SECURITIES AND FUTURES COMMISSION**  
證券及期貨事務監察委員會

## **Guidelines on Online Distribution and Advisory Platforms**

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# Guidelines on Online Distribution and Advisory Platforms

## Chapter 1: Introduction

- 1.1 These Guidelines are issued under section 399 of the Securities and Futures Ordinance (SFO) and set out principles and requirements applicable to online distribution and advisory platforms for investment products operated by licensed or registered persons (Online Platforms). These Guidelines are not intended to be exhaustive and may be updated and revised from time to time.

*Note: A licensed or registered person may operate different websites, platforms and other channels such as social media accounts for posting information about investment products and transacting in them. The Securities and Futures Commission (SFC) will take into account activities targeting Hong Kong investors conducted by a licensed or registered person via all channels in their totality in considering the licensed or registered person's compliance with the requirements in these Guidelines.*

- 1.2 These Guidelines apply to all licensed or registered persons when conducting their regulated activities in providing order execution, distribution and/or advisory<sup>1</sup> services in respect of investment products via Online Platforms (Platform Operators).
- 1.3 Where an Online Platform also provides automated trading services (ATS) as defined in the SFO, the principles and standards set out in the Guidelines for the Regulation of Automated Trading Services<sup>2</sup> will apply.
- 1.4 Platform Operators who conduct electronic trading should also ensure that the requirements in paragraph 18 (Electronic Trading) of and Schedule 7 to the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (Code of Conduct) and any relevant guidelines are complied with.
- 1.5 Unless specified otherwise, terms used in these Guidelines bear the same meaning as defined in the SFO.
- 1.6 These Guidelines do not have the force of law and shall not be interpreted in a way which would override the provision of any law.
- 1.7 Failure by any person to comply with any applicable provision of these Guidelines:
- (a) shall not by itself render it liable to any judicial or other proceedings, but in any proceedings under the SFO before any court, these Guidelines may be admissible in evidence, and if any provision set out in these Guidelines appears to the court to be relevant to any question arising in the proceedings, it may be taken into account in determining the question; and

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<sup>1</sup> Including advisory services provided on a discretionary basis and automated/robo-advice.

<sup>2</sup> The SFC's Guidelines for the Regulation of Automated Trading Services, as amended from time to time. These guidelines are applicable to providers of ATS authorized under Part III of the SFO or licensed or registered for Type 7 regulated activity under Part V of the SFO.

- (b) may cause the SFC to consider whether such failure adversely reflects on the person's fitness and properness.

## Chapter 2: Core Principles

- 2.1 The SFC has identified six core principles which Platform Operators should comply with in the operation of their Online Platforms.

### CP1. Proper design

- 2.2 A Platform Operator should ensure that the Online Platform is properly designed and operated in compliance with all applicable laws and regulations.

*Note: This includes, but is not limited to, ensuring that:*

- (i) appropriate access rights and controls are put in place such that the public (including retail clients) would not be able to invest in or view materials relating to investment products in circumstances that would constitute a breach of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (C(WUMP)O) or Part IV of the SFO;*
- (ii) the Online Platform is operated with due skill, care and diligence, for example:
  - (a) a Platform Operator should act with due skill, care and diligence when selecting investment products to be made available on its Online Platform and when posting any information and materials on its Online Platform; and*
  - (b) when providing investment advice or recommendations to clients on its Online Platform, a Platform Operator should design its Online Platform to ensure that the investment advice or recommendations provided are based on thorough analysis and take into account available alternatives;**
- (iii) any conflicts of interest should be properly managed and minimised to ensure that clients are fairly treated, for example, when providing investment advice to clients on its Online Platform, a Platform Operator should not design its Online Platform in such a way that commission rebates or other benefits are taken as the primary basis for soliciting or recommending particular investment products to clients;*
- (iv) where available, exercise due skill, care and diligence to ensure the methodology for risk profiling investment products and/or clients is properly designed. In this connection, Platform Operators should make reference to the requirements in Chapter 5 of these Guidelines; and*
- (v) all systems and processes underpinning the operation of the Online Platform are robust and properly maintained such that the risk of fraud, errors and omissions, interruptions or other operational or control failures is minimised and appropriately managed.*

### CP2. Information for clients

- 2.3 A Platform Operator should make clear and adequate disclosure of relevant material information on its Online Platform.

Note: This includes, but is not limited to:

- (i) *providing clients with access to up-to-date product offering documents or information<sup>3</sup>;*
- (ii) *providing clients with material information as soon as reasonably practicable to enable clients to appraise the position of their investments (eg, in the event of any suspensions in the redemption of funds, any proposed merger or termination of funds or any other material information provided by issuers). In this connection, a Platform Operator should put in place proper arrangements and take adequate measures to enable it to access and be informed of up-to-date information concerning all non-exchange-traded investment products available on its Online Platform;*
- (iii) *communicating any information in an easily comprehensible manner. A Platform Operator should use plain language in any disclosures made and presentation of information to make them easy to read and understand;*
- (iv) *making available information on the methodology adopted for assessing and assigning ratings to investment products and categorising clients on the Online Platform, if any. Such information should also be accompanied by an explanation of the risk profiles of investment products and clients;*
- (v) *where selected list(s) of investment products are posted on its Online Platform, setting out or making available the objective criteria by reference to which such investment products are selected;*
- (vi) *informing clients of the scope and limitations of services and investment products that are provided through and on the Online Platform (eg, the availability of investment products is limited to those issued by related companies); and*
- (vii) *disclosing to clients any remuneration to be paid by the client or other persons (eg, product issuers) to the Platform Operator, such as commission, brokerage and any other fees and charges, and any other monetary benefits received or receivable by the Platform Operator, pursuant to applicable codes, guidelines, circulars and frequently-asked questions (FAQs); and*
- (viii) *providing clients with the Platform Operator's contact details for handling client enquiries and complaints.*

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<sup>3</sup> In respect of non-exchange-traded investment products, Platform Operators are expected to provide up-to-date product offering documents on their Online Platforms. For exchange-traded investment products, a good practice would be to provide a hyperlink to where up-to-date information could be accessed or a reminder to clients to refer to any such information before making an investment decision.

### **CP3. Risk management**

- 2.4 A Platform Operator should ensure the reliability and security (including data protection and cybersecurity) of its Online Platform.

*Note: This includes, but is not limited to:*

#### System reliability

- (i) a Platform Operator should ensure that its Online Platform, and all modifications to the Online Platform, are tested before deployment and are regularly reviewed to ensure that the Online Platform and its modifications are reliable;*
- (ii) a Platform Operator should promptly report to the SFC any material service interruption or other significant issues related to its Online Platform;*

#### Contingencies

- (iii) a Platform Operator should identify and manage the associated risks (including any unintended consequences) prudently with appropriate contingency arrangements in place. Such arrangements should include a written contingency plan to cope with emergencies and disruptions related to the Online Platform. The contingency plan should at least include:
  - (a) a suitable backup facility or alternative arrangements for order execution in the event of an emergency;*
  - (b) arrangements to ensure business records, client and transaction databases, servers and supporting documentation are backed up in an off-line medium. Off-site storage is generally expected to be subject to proper security measures; and*
  - (c) a plan for dealing with client and regulatory enquiries by trained staff;**
- (iv) a Platform Operator should ensure that the contingency plan to deal with potential emergencies and disruptions is periodically tested and the plan is viable and adequate;*
- (v) in the event of a material delay or failure of the Online Platform, a Platform Operator should, in a timely manner:
  - (a) ensure the material delay or failure is rectified; and*
  - (b) inform clients about the causes or possible causes of the material delay or failure and how client orders will be handled.**



### System security

- (vi) a Platform Operator should also refer to guidance issued by the SFC from time to time on cybersecurity<sup>4</sup>.

#### **CP4. Governance, capabilities and resources**

- 2.5 A Platform Operator should ensure that there are robust governance arrangements in place for overseeing the operation of its Online Platform as well as adequate human, technology and financial resources available to ensure that the operations of its Online Platform are carried out properly.

*Note: A Platform Operator should establish and implement written internal policies and procedures on the operation of its Online Platform to ensure that:*

- (i) there is at least one responsible officer or executive officer responsible for the overall management and supervision of the Online Platform;*
- (ii) there is a formalised governance process with input from the dealing, information technology, risk and compliance functions;*
- (iii) there are clearly identified reporting lines with supervisory and reporting responsibilities assigned to appropriate staff members; and*
- (iv) there are managerial and supervisory controls that are designed to manage the risks associated with the use of the Online Platform.*

*A Platform Operator should conduct regular reviews to ensure that these internal policies and procedures are in line with regulatory developments and promptly remedy any deficiencies identified.*

*In operating its Online Platform, a Platform Operator should ensure that it has sufficient technology resources to, for example, safeguard data integrity, including confidential client information, and meet current and projected operational needs (eg, in respect of system capacity).*

#### **CP5. Review and monitoring**

- 2.6 Appropriate reviews of all activities conducted on the Online Platform should be performed by a Platform Operator as part of its ongoing supervision and monitoring obligation.

*Note: This includes, but is not limited to, regular reviews as well as ad hoc reviews where appropriate, for example, if a major market event occurs. It is expected that a regular review should be conducted at least annually.*

*Such regular review should cover all activities conducted on the Online Platform in relation to the design and operation of the Online Platform,*

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<sup>4</sup> For example, the Guidelines for Reducing and Mitigating Hacking Risks Associated with Internet Trading, as amended from time to time.

*including the processes and outcomes of any client profiling, investment product selection and risk profiling, suitability assessment, as well as the reasonableness of any recommendation or advice generated by the algorithm used (including any recommended model portfolio) and any rebalancing conducted. It should include sample checking and testing by a suitably-qualified person. There should also be policies and procedures to follow up on any review results and to implement any enhancements required.*

*Where any function is outsourced to external service provider(s), the Platform Operator should exercise due skill, care and diligence in the selection, appointment and ongoing monitoring of the outsourced service provider(s) to ensure proper performance of the outsourced function.*

## **CP6. Record keeping**

2.7 A Platform Operator should maintain proper records in respect of its Online Platform.

*Note: This includes, but is not limited to, comprehensive documentation on platform design, operational processes and risk management controls, including any testings, reviews, modifications, upgrades or rectifications of its Online Platform and records of the applicable software versions (including programmes and any algorithms). The documentation should be retained for a period of not less than 2 years after the Online Platform ceases to operate.*

*A Platform Operator should also keep proper audit trails of activities and transactions conducted on its Online Platform, including the processes and outcomes of any client profiling, investment product selection and risk profiling, suitability assessment, provision of product information, disclosure of warning statement, advice provided and any rebalancing conducted, and incident reports for all material delays or failures of the Online Platform. The audit trails and records should be retained for a period of not less than 2 years or such longer period as may be required under the Code of Conduct or related guidance issued by the SFC from time to time. Further, audit trails and records relating to all suitability assessments (including audit trails and records demonstrating that transactions are suitable) should be retained for at least 2 years for exchange-traded investment products and at least 7 years for non-exchange-traded investment products.*

## Chapter 3: General Requirements

- 3.1 Platform Operators when conducting their regulated activities in providing order execution, distribution and/or advisory services in respect of investment products via Online Platforms must comply with all applicable laws and regulations including the SFC's conduct requirements, restrictions on the offer of investments, and those applicable to materials that may be posted on their Online Platforms.

### *Conduct requirements*

- 3.2 The regulatory framework governing the conduct of licensed or registered persons (including Platform Operators) is set out in the Code of Conduct, the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the Securities and Futures Commission (Internal Control Guidelines), and other codes, guidelines, circulars<sup>5</sup> and FAQs issued by the SFC from time to time.
- 3.3 These conduct requirements are in general principles-based such that they apply irrespective of the medium through which a licensed or registered person provides its services in carrying on the regulated activities for which the person is licensed or registered.
- 3.4 Conduct requirements include the General Principles in the Code of Conduct which set out the standards and requirements licensed or registered persons should meet in carrying out regulated activities. The Code of Conduct further sets out requirements augmenting the General Principles.
- 3.5 In particular, paragraph 5.2 of the Code of Conduct sets out the suitability requirement pursuant to which a licensed or registered person should, when making a recommendation or solicitation to a client, ensure the suitability of the recommendation or solicitation for that client is reasonable in all the circumstances having regard to information about the client of which the licensed or registered person is or should be aware through the exercise of due diligence (the Suitability Requirement).
- 3.6 This requirement forms part of a suite of duties set out in the Code of Conduct to which licensed or registered persons who distribute investment products or provide financial advice are subject. Such duties include a duty to "know your client" (General Principle 4 and paragraphs 5.1 and 5.1A), a duty to exercise due skill, care and diligence, in the best interests of clients and the integrity of the market (General Principle 2 and paragraph 3.4), a duty to disclose relevant material information (General Principle 5), a duty to ensure that clients understand the nature and risks of derivative products and have sufficient net worth to bear the risks and potential losses of trading in derivative products (paragraph 5.3), and a duty to implement internal controls and supervise staff to ensure compliance with regulatory requirements (General Principles 3 and 7 and paragraphs 4.2, 4.3 and 12.1). Guidance in respect of these duties is found in guidelines, circulars and reports issued by the SFC from time to time.

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<sup>5</sup> Including the Circular to Intermediaries – Frequently Asked Questions on Triggering of Suitability Obligations, and the Circular to Intermediaries – Frequently Asked Questions on Compliance with Suitability Obligations, and as amended from time to time (Suitability FAQs)

- 3.7 Further guidance on the Suitability Requirement in the context of Online Platforms is also set out in Chapter 5 of these Guidelines.
- 3.8 Platform Operators should note in particular, but without limitation, the following conduct requirements:
- (a) for derivative products (including futures contracts and options) and any leveraged transaction, the investor characterization requirements in paragraph 5.1A of the Code of Conduct and the know-your-client requirement in paragraph 5.3 of the Code of Conduct;
  - (b) the requirement to disclose monetary and non-monetary benefits in paragraph 8.3 of the Code of Conduct;
  - (c) the requirement to disclose transaction related information in paragraph 8.3A of the Code of Conduct;
  - (d) the requirement to ensure best execution in paragraph 3.2 of the Code of Conduct;
  - (e) the requirement to handle client orders fairly and in the order in which they are received in paragraph 9.1 of the Code of Conduct;
  - (f) the requirement governing the priority for client orders in paragraph 9.2 of the Code of Conduct;
  - (g) where a Platform Operator only makes available on its Online Platform investment products issued by it and/or its related companies, the requirement to disclose this limited availability of investment products to clients<sup>6</sup>;
  - (h) the requirement not to take commission rebates or other benefits receivable by them or their related companies as the primary basis for soliciting or recommending particular investment products to clients<sup>7</sup>;
  - (i) the prohibition on the use of gifts in promoting a specific investment product in paragraph 3.11 of the Code of Conduct; and
  - (j) compliance requirements in paragraph 12 of the Code of Conduct, including the requirements in relation to complaints-handling in paragraph 12.3 and the obligation in paragraph 12.5 to report any material breach or suspected material breach of any law, rules, regulations, and codes administered or issued by the SFC, etc to the SFC immediately.

#### *Offer of investments*

- 3.9 Platform Operators should note in particular, but without limitation, the following offer of investments requirements:

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<sup>6</sup> Suitability FAQs

<sup>7</sup> Suitability FAQs

- (a) prospectus requirements for offering of shares and debentures under the C(WUMP)O<sup>8</sup> ;
- (b) restrictions on offers of investments under Part IV of the SFO - in particular the restrictions on offering of unauthorized collective investment schemes (CIS) and structured products (eg, overseas exchange-traded ETFs, unauthorized CIS and structured products) notwithstanding the offer is made by or on behalf of an intermediary licensed or registered for Type 1, Type 4 or Type 6 regulated activity<sup>9</sup>;
- (c) restrictions applicable to certain overseas exchange-traded products or ATS products under the relevant ATS authorization conditions; and
- (d) relevant requirements relating to the offering of CIS on the internet as set out in the Guidance Note for Persons Advertising or Offering Collective Investment Schemes on the Internet.

#### *Materials posted on an Online Platform*

3.10 In respect of the posting of any advertisement, research report and other investment product-specific materials on their Online Platforms, Platform Operators should note in particular, but without limitation, the following requirements relevant to the issue of such materials:

- (a) the issue of advertisements in respect of investment products is regulated under Part IV of the SFO. In particular, certain misrepresentations made by a person may attract civil<sup>10</sup> and/or criminal<sup>11</sup> liability under Part IV of the SFO and the disclosure of false or misleading information inducing transactions may constitute market misconduct which is subject to civil or criminal liability under the SFO<sup>12</sup>;
- (b) the contents of advertisements must also comply with relevant advertising guidelines<sup>13</sup>, offer awareness guidelines<sup>14</sup>, marketing materials guidelines<sup>15</sup> and/or the SEHK Listing Rules<sup>16</sup> where applicable;
- (c) the requirement to ensure that advertisements do not contain information that is false, biased, misleading or deceptive<sup>17</sup>;

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<sup>8</sup> Parts II and XII of the C(WUMP)O

<sup>9</sup> Sections 103(2)(a) and 103(11) of the SFO

<sup>10</sup> Section 108 of the SFO

<sup>11</sup> Section 107 of the SFO

<sup>12</sup> Sections 277 and 298 of the SFO

<sup>13</sup> Advertising Guidelines Applicable to Collective Investment Schemes Authorized under the Product Codes issued by the SFC

<sup>14</sup> Guidelines on use of offer awareness and summary disclosure materials in offerings of shares and debentures under the Companies Ordinance issued by the SFC

<sup>15</sup> Guidelines on Marketing Materials for Listed Structured Products issued by the SFC

<sup>16</sup> Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited

<sup>17</sup> GP1 (Honesty and fairness) and paragraphs 2.1 and 2.3 of the Code of Conduct, Advertising Guidelines Applicable to Collective Investment Schemes Authorized under the Product Codes issued by the SFC, Guidelines on Marketing Materials for Listed Structured Products issued by the SFC

- (d) for research reports, the conflicts of interest requirements<sup>18</sup> and the applicable requirements under paragraph 16 (Analysts) as well as the General Principles<sup>19</sup> of the Code of Conduct; and
- (e) the requirement to act with due skill, care and diligence in expressing any opinion<sup>20</sup>.

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<sup>18</sup> GP6 (Conflicts of interest) and paragraph 10.1 of the Code of Conduct

<sup>19</sup> Including GPs 1 (Honesty and fairness), 2 (Diligence), 5 (Information for clients) and 6 (Conflicts of interest) of the Code of Conduct

<sup>20</sup> GP2 (Diligence) of the Code of Conduct, which requires a licensed or registered person to act with due skill, care and diligence, in the best interests of its clients and the integrity of the market in conducting its business activities.

## Chapter 4: Robo-Advice

- 4.1 Robo-advice (sometimes referred to as digital advice or automated advice) involves the provision of financial advice in an online environment using algorithms and other technology tools.

*Note: There are many different types of robo-advice services, for example, (i) full automation (ie, fully-automated investment advice via an Online Platform with no human intervention); (ii) adviser-assisted (ie, the Online Platform also provides an option for clients to contact an adviser depending on their needs); and (iii) guided advice (ie, investment advice is provided by an adviser who is assisted and supported by technology tools).*

*These Guidelines generally intend to apply to robo-advice services which are provided directly to clients in an online environment by way of direct use of technology tools by clients ("client-facing tools"). Licensed or registered persons providing such robo-advice through client-facing tools are hereinafter referred to as "robo-advisers".*

*In the case where client-facing tools are not involved, licensed and registered persons should refer to other relevant applicable requirements governing the conduct of their regulated activities in providing guided advice, including the Code of Conduct, Internal Control Guidelines and other codes, guidelines, circulars<sup>21</sup> and FAQs issued by the SFC from time to time.*

*Robo-advisers, whether providing advice on a discretionary basis or otherwise, should also refer to guidance issued by the SFC from time to time in respect of compliance with the Suitability Requirement<sup>22</sup>.*

*Where the robo-advice services provided involve web-chats or similar interactive facilities, the licensed or registered person should also comply with the guidance<sup>23</sup> in the context of transactions conducted in an interactive environment issued by the SFC from time to time.*

### *Information for clients*

- 4.2 A robo-adviser should provide sufficient information on its Online Platform to enable investors to make an informed decision regarding whether to employ its services. A robo-adviser should also make clear and adequate disclosure of relevant material information to clients on its Online Platform on an ongoing basis.

*Note: This would include information on the limitations, risks and how key components of its services are generated (such as a description of how underlying algorithms operate, any limitations of the algorithm, how the portfolio rebalancing mechanism operates and associated risks).*

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<sup>21</sup> Including the Suitability FAQs

<sup>22</sup> For example, the Suitability FAQs.

<sup>23</sup> For example, the Circular to Intermediaries – Frequently Asked Questions on Triggering of Suitability Obligations.

*Robo-advisers should also inform and explain to investors and clients the degree of human involvement that it provides.*

- 4.3 A robo-adviser should ensure that it accurately describes the services it provides.
- 4.4 Information disclosed by a robo-adviser should be easily comprehensible.

*Note: This could be achieved by presenting information through design features such as pop-up boxes or tooltips, or other means or media.*

#### *Client profiling*

- 4.5 Where a robo-adviser uses client profiling tools and/or questionnaires to obtain information about clients as part of its know your client process, it should ensure that the client profiling tools and/or questionnaires are properly designed such that sufficient information is obtained to enable it to provide advice that is suitable based on clients' personal circumstances.

*Note: This would include designing the client profiling tools and/or questionnaires such that clients are provided with the opportunity to provide additional explanatory and contextual information, where appropriate.*

- 4.6 A robo-adviser should have in place proper mechanisms to identify and seek to reconcile any inconsistencies in the information provided by a client.

*Note: For example, robo-advisers could alert a client to such inconsistencies through pop-up boxes and could provide the client with an opportunity to change the information provided. Robo-advisers could also internally flag any inconsistent information for review and follow-up.*

- 4.7 Where a robo-adviser uses risk-scoring questionnaires to risk profile clients and/or to determine the advisory services to be provided to clients, it should pay particular attention to the design of the questions and the underlying scoring mechanism, which should be properly designed to accurately reflect the personal circumstances of a client.

*Note: In this connection, robo-advisers should also make reference to the requirements in Chapter 5 of these Guidelines.*

#### *System design and development*

- 4.8 Algorithms are the core components of digital financial advice tools adopted by robo-advisers. It is essential that a robo-adviser effectively manages and adequately supervises the design, development, deployment and operations of algorithms used in digital-advice tools. In particular, a robo-adviser should:

- (a) ensure the design and operations of algorithms used are in compliance with relevant conduct requirements including, where applicable, requirements in paragraph 18 (Electronic Trading) of and Schedule 7 to the Code of Conduct and any relevant guidelines;
- (b) ensure that the algorithms take into account all relevant information about each client obtained through the know-your-client process and use objective criteria



to generate investment recommendations and/or advice which match the client's personal circumstances against suitable investment products and operate in a manner that is not biased; and

*Note: This would include ensuring that algorithms used should not be programmed to direct clients towards particular investment products for which the robo-adviser or its affiliates receive higher commissions or other forms of compensation.*

- (c) maintain appropriate documentation on the design and development (including any modifications) of the algorithms. The documentation should set out the rationale for the design, development and modification, as well as the intended outcome, objectives, and scope of the algorithms.

#### *Supervision and testing of algorithms*

4.9 A robo-adviser should supervise the operation and testing of the algorithms that form the basis of any investment advice it provides. A robo-adviser should:

- (a) have a documented plan with details on the scope and strategy for the testing of algorithms (including the design and implementation of test plans, selection of test cases, treatment of test results and defect rectification procedures);
- (b) have security measures in place to prevent and detect unauthorized access to the algorithms;
- (c) test algorithms before deployment and any subsequent developments and/or modifications to assess whether the methodology (including any assumptions made) is well-suited, the data input used is appropriate to cover the expected scenarios and the output conforms with the robo-adviser's expectations;
- (d) have robust policies and procedures in place to monitor and test the algorithms and the reasonableness of the advice provided to clients (eg, regular and random samples of robo-advice provided should be tested/reviewed by a suitably-qualified person to ensure all applicable requirements are complied with);
- (e) have proper policies and procedures for a suitably-qualified person to manage, supervise, review and modify algorithms where appropriate (eg, when there are market or regulatory changes);
- (f) exercise due skill, care and diligence when selecting and monitoring any outsourced service provider, including in the selection and monitoring of any third party in the development, management, or ownership of the algorithms used;
- (g) conduct regular reviews of advice. When modifications to the algorithms are made, the robo-adviser should arrange for a suitably-qualified person to perform validation and other appropriate tests to ensure the reasonableness of the advice provided; and

- (h) take immediate measures to rectify any problem when errors are detected in the algorithms and have controls in place to suspend provision of advice or service where necessary.

#### *Adequate resources*

- 4.10 A robo-adviser should ensure that it has adequate staff who have sufficient expertise and understanding of the technology, operations and algorithms (including the rationale, risks and rules behind the algorithms), and who are closely involved in the design, development, deployment and ongoing supervision of the operation of the algorithms.
- 4.11 Adequate training or testing should be provided by the robo-adviser to all staff who make use of the robo-advisory tools of the robo-adviser.
- 4.12 A robo-adviser should ensure that it has sufficient technology resources and up-to-date infrastructure to support the proper operation of the Online Platform (including any system requirements arising from modifications to the algorithms used).

#### *Rebalancing*

- 4.13 When algorithms are used to rebalance a predefined model portfolio automatically in order to maintain a target asset allocation over time, the robo-adviser should ensure effective practices for automatic rebalancing are in place. Such practices should include, without limitation, the following:
  - (a) informing clients clearly at the outset that automatic portfolio rebalancing (where applicable) would occur on a periodic basis to maintain the target asset allocation and, where applicable, additional costs may be incurred due to such rebalancing;
  - (b) disclosing to clients how the portfolio rebalancing mechanism operates, including:
    - (i) if the robo-adviser uses deviation thresholds on an asset class or a particular type of securities, disclosing what the thresholds are and whether (and, if so, how) they vary by asset class or particular type of securities; and  

*Note: The composition of an investment portfolio may deviate from time to time from its intended target asset allocation for different reasons (eg, market volatility). In such cases, portfolio rebalancing may become necessary.*
    - (ii) if portfolio rebalancing is scheduled, disclosing the frequency; and
    - (iii) any risks associated with automatic rebalancing (such as rebalancing may occur irrespective of market conditions);
  - (c) establishing and maintaining policies and procedures to define how the algorithms would handle any major market event; and

- (d) where there are changes to the existing algorithm that may materially affect clients' portfolios, clearly and promptly informing the relevant clients of such changes.

- 4.14 Where a robo-adviser offers its clients the flexibility to opt-out of automatic portfolio rebalancing, it should inform clients of the potential risks and consequences of opting-out of automatic rebalancing.

*Note: The robo-adviser should provide appropriate warnings to clients such as the warning that the original portfolio that a client may invest into or has invested into according to the robo-adviser's recommendation could become unsuitable for the client as a result of the opt-out and that by choosing to opt-out, the client would require a different service to be provided.*

- 4.15 Before a client confirms to opt-out of automatic rebalancing, the robo-adviser should ensure the client has acknowledged and confirmed agreement to the change in the scope and terms of services to be provided by the Online Platform going forward.

*Note: Although the Platform Operator may no longer have an advisory relationship with the client as a result, it should still comply with all other applicable requirements in these Guidelines, including the requirement to ensure that a transaction in a complex product is suitable for the client in all the circumstances pursuant to paragraph 6.3 of these Guidelines.*

## Chapter 5: Suitability Requirement and other conduct requirements applicable to the Sale of Investment Products

- 5.1 Platform Operators should comply with all existing conduct requirements under the Code of Conduct applicable to the regulated activities they conduct via their Online Platforms.

### *Suitability Requirement*

- 5.2 The sale of investment products on Online Platforms is also subject to the Suitability Requirement set out in paragraph 5.2 of the Code of Conduct. Under paragraph 5.2, a licensed or registered person should, when making a recommendation or solicitation, ensure the suitability of the recommendation or solicitation for the client is reasonable in all the circumstances having regard to information about the client of which the licensed or registered person is or should be aware through the exercise of due diligence.

### *Triggering of the Suitability Requirement*

- 5.3 The question of whether there has been a “solicitation” or “recommendation” triggering the Suitability Requirement is a question of fact which should be assessed in light of all the circumstances leading up to the point of sale or advice.

*Note: To facilitate a better understanding of the circumstances under which the Suitability Requirement would be likely or unlikely to be regarded as being triggered under paragraph 5.2 of the Code of Conduct, Platform Operators should refer to guidance<sup>24</sup> published by the SFC (which may be updated from time to time).*

*The context (such as the manner of presentation) and content of product-specific materials posted on an Online Platform coupled with the design and overall impression created by the content of the Online Platform would determine whether the Suitability Requirement is triggered.*

*The posting of factual, fair and balanced product-specific materials would not in itself amount to a solicitation or recommendation and will not trigger the Suitability Requirement. This is so in the absence of other circumstances that amount to a solicitation or recommendation in a particular investment product. This would occur, for example, where the Online Platform emphasises some investment products over others or there have been interactive one-to-one communications involving solicitations or recommendations through the Online Platform.*

*Platform Operators should also note the additional requirements applicable to transactions in complex products set out in Chapter 6 of these Guidelines.*

- 5.4 Platform Operators should also refer to guidance published by the SFC (which may be updated from time to time) on how the posting of materials on Online Platforms would or would not trigger the Suitability Requirement.

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<sup>24</sup> For example, the Circular to Intermediaries – Frequently Asked Questions on Triggering of Suitability Obligations.

- 5.5 For the avoidance of doubt, the provision of investment advice (including robo-advice<sup>25</sup>) on investment products on an Online Platform will trigger the Suitability Requirement.

#### *Discharging the Suitability Requirement*

- 5.6 Once the Suitability Requirement is triggered, Platform Operators must discharge the suitability obligations at the point of sale or advice in accordance with the existing requirements under the Code of Conduct<sup>26</sup>.
- 5.7 As part of its existing obligation to discharge the Suitability Requirement, Platform Operators should match the risk return profile of the investment product selected by a client with the personal circumstances of that client<sup>27</sup>.

*Note: This may involve an Online Platform making an assessment of a client's risk tolerance level and risk profile and accordingly risk profiling the client, and the Platform Operator conducting product due diligence to ascertain the risk return profile of an investment product and accordingly risk profiling the investment product. It should be noted, however, that merely mechanically matching an investment product's risk rating with a client's risk tolerance level may not be sufficient to discharge the Suitability Requirement<sup>28</sup>.*

*A Platform Operator should ensure that in assigning risk profiles to investment products, its risk profiling methodology is properly designed to take into account both quantitative and qualitative factors and consider all risks involved, including credit risk, liquidity risk, counterparty risk, use of leverage, etc. Platform Operators should have appropriate processes in place to periodically review the risk profiling methodology and mechanism for investment products. The risk profiles of investment products should also be reviewed at regular intervals.*

*In determining a client's risk profile, a Platform Operator should base its assessment on information about the client obtained through its know-your-client process<sup>29</sup>. The individual risk profile of a client should also be reviewed and updated regularly, where appropriate<sup>30</sup>. Where risk-scoring questionnaires are used to risk profile clients, Platform Operators should pay particular attention to the design of the questions and the underlying scoring mechanism, which should be properly designed to accurately reflect the personal circumstances of a client<sup>31</sup>. Platform Operators should also have appropriate processes in place to periodically review the risk profiling methodology and mechanism for clients.*

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<sup>25</sup> This would include automatic rebalancing conducted by robo-advisers.

<sup>26</sup> Intermediaries should also refer to the Suitability FAQs.

<sup>27</sup> Please refer to the Suitability FAQs.

<sup>28</sup> Please refer to the Suitability FAQs.

<sup>29</sup> Paragraphs 5.1 and 5.1A of the Code of Conduct and the Suitability FAQs

<sup>30</sup> For example, this may not apply to a dormant client account.

<sup>31</sup> Please refer to the Suitability FAQs.

- 5.8 In discharging the Suitability Requirement, Platform Operators should also note in particular (but not exclusively) the following where applicable:
- (a) Platform Operators should act diligently and carefully in providing any advice and ensuring that advice and recommendations are based on thorough analysis and take into account available alternatives<sup>32</sup> (eg, availability of any similar investment products which may be less costly);
  - (b) when providing investment advice to clients, Platform Operators should not take commission rebates or other benefits as the primary basis for soliciting or recommending particular investment products to clients<sup>33</sup>;
  - (c) Platform Operators should establish a proper mechanism to assess the suitability of investment products via their Online Platforms. Such mechanism should be holistic (ie, all relevant factors concerning the personal circumstances of a client, including concentration risk, should be taken into account); and
  - (d) an Online Platform should have in place appropriate tools for assessing a client's concentration risk and such an assessment should be based on the information about the client obtained by the Platform Operator through its know-your-client process and any investment portfolio held with the Platform Operator.

*Other conduct requirements applicable to the sale of investment products*

- 5.9 In addition to the Suitability Requirement, a Platform Operator should also comply with other applicable conduct requirements under the Code of Conduct.

*Note: This would include (but is not limited to) the following where applicable:*

- (i) *A Platform Operator should establish appropriate governance and supervisory mechanisms for the client profiling tool provided on its Online Platform, if any, and identify the key elements of information necessary to profile a client accurately<sup>34</sup>.*
- (ii) *An Online Platform should enable a client to update the client's information in any client profiling tool provided at any time should there be any updates or changes to the client's personal information (eg, investment objectives, risk appetite etc.)<sup>35</sup>*
- (iii) *Where insufficient information is obtained from a client by a Platform Operator through any client profiling tool provided on the Online Platform or otherwise through its know-your-client process, there should be a proper mechanism in place to determine whether the client*

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<sup>32</sup> GP2 (Diligence) and paragraph 3.4 of the Code of Conduct

<sup>33</sup> Suitability FAQs

<sup>34</sup> Suitability FAQs

<sup>35</sup> Suitability FAQs

*should be allowed to proceed to place an order for an investment product<sup>36</sup>.*

- (iv) Where a client provides inconsistent answers in any online client profiling tool provided, the Platform Operator should have in place a proper mechanism to identify and seek to reconcile the inconsistencies (eg. by providing the client with an opportunity to change its input)<sup>37</sup>. Where inconsistencies cannot be reconciled, it may be appropriate to filter the client out of the Online Platform.*
- (v) An Online Platform should have in place proper systems to ensure that client orders are executed promptly in accordance with clients' instructions and are executed on the best available terms, where applicable. The Online Platform should also have in place proper mechanisms to promptly and fairly allocate any transactions executed on behalf of clients to the respective client accounts<sup>38</sup>.*

#### *Further points to note*

- 5.10 Platform Operators should note that where there are one-to-one interactions between a client and representatives of the Platform Operator via the Online Platform or there have been other communications between representatives of the Platform Operator and a client, this must be taken into account in determining whether the Suitability Requirement has been triggered. The Suitability Requirement may be triggered notwithstanding that some communications taken in isolation may not trigger the Suitability Requirement. Platform Operators should also refer to guidance concerning transactions conducted in an interactive environment issued by the SFC from time to time<sup>39</sup>.

*Note: Interaction between a client and representatives of the Platform Operator via the Online Platform or other communications between representatives of the Platform Operator and a client would include, for example, communications through live web-chat or where a client calls a hotline listed on the Online Platform and speaks with a representative of the Platform Operator.*

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<sup>36</sup> Suitability FAQs

<sup>37</sup> Suitability FAQs

<sup>38</sup> Paragraphs 3.1, 3.2, 3.3, 9.1 and 9.2 of the Code of Conduct

<sup>39</sup> For example, the Circular to Intermediaries – Frequently Asked Questions on Triggering of Suitability Obligations.

## Chapter 6: Complex Products

### *Definition of a complex product*

- 6.1 A complex product is an investment product whose, terms, features and risks are not reasonably likely to be understood by a retail investor because of its complex structure.

*Note: Set out below are factors to determine whether an investment product is complex or not:*

- (i) whether the investment product is a derivative product;*
- (ii) whether a secondary market is available for the investment product at publicly available prices;*
- (iii) whether there is adequate and transparent information about the investment product available to retail investors;*
- (iv) whether there is a risk of losing more than the amount invested;*
- (v) whether any features or terms of the investment product could fundamentally alter the nature or risk of the investment or pay-out profile or include multiple variables or complicated formulas to determine the return; and*

*Note: This would include, for example, investments that incorporate a right for the investment product issuer to convert the instrument into a different investment.*

- (vi) whether any features or terms of the investment product might render the investment illiquid and/or difficult to value.*

- 6.2 A Platform Operator should determine whether a product may be treated as non-complex or complex with due skill, care and diligence. In making such determination, the Platform Operator should have regard to the factors set out in paragraph 6.1 and the non-exhaustive list of examples of non-complex and complex products (which may be updated from time to time) set out on the SFC's website.

*Note: Platform Operators should refer to the examples of investment products that the SFC considers are not complex, examples of complex products, and other guidance issued by the SFC, which are published on the SFC's website.*

*A Platform Operator should consider whether an investment product is of the same type as an investment product in the list of examples of non-complex and complex products and whether the product is being regulated in or traded on an exchange in a specified jurisdiction. Platform Operators should refer to the list of specified jurisdictions which is published on the SFC's website. Platform Operators should exercise extra caution where the product is regulated in or traded on an exchange in a jurisdiction which is not a specified jurisdiction.*



### *Ensuring suitability of transactions in complex products*

- 6.3 Subject to paragraphs 6.5 to 6.6 and 6.9 to 6.11, an Online Platform should ensure that a transaction in a complex product is suitable for the client in all the circumstances.
- 6.4 Online Platforms should discharge the requirement in paragraph 6.3 to the standard of, and in accordance with, the existing requirements under the Code of Conduct applicable to the Suitability Requirement under paragraph 5.2 of the Code of Conduct.

*Note: Platform Operators should refer to the guidance on the Suitability Requirement in the context of Online Platforms in Chapter 5 of these Guidelines.*

- 6.5 For complex products which are also derivative products traded on an exchange in Hong Kong or in a specified jurisdiction, where there has been no solicitation or recommendation, an Online Platform is not required to comply with paragraphs 6.3, 6.7 and 6.8 for transactions in such products executed on an exchange although it must still comply with paragraphs 5.1A and 5.3 of the Code of Conduct.

*Note: Platform Operators should refer to the list of specified jurisdictions for exchange-traded products which is published on the SFC's website. For derivative products traded on an exchange which is not in a specified jurisdiction, Platform Operators should comply with paragraphs 6.3, 6.7 and 6.8 unless such products could reasonably be treated on the same basis as derivative products traded on an exchange in Hong Kong or in a specified jurisdiction.*

- 6.6 For the avoidance of doubt, Platform Operators should also comply with the requirement to assess a client's knowledge of derivatives and characterize the client based on his knowledge of derivatives under paragraph 5.1A(a) of the Code of Conduct as part of their know your client procedures and, where a client without knowledge of derivative wishes to purchase a derivative product which is not traded on an exchange, warn the client about the transaction pursuant to paragraph 5.1A(b)(ii) of the Code of Conduct.

### *Minimum information and warning statements*

- 6.7 Subject to paragraphs 6.5 to 6.6 and 6.9 to 6.11, Platform Operators should ensure that their Online Platforms provide sufficient information on the key nature, features and risks of a complex product to enable clients to understand the complex product before making an investment decision.

*Note: Platform Operators should refer to guidance issued by the SFC from time to time in relation to the minimum information that should be provided. Where this information is contained in the offering documents of a complex product, the posting of such offering documents on the Online Platform would generally satisfy this requirement.*

- 6.8 Subject to paragraphs 6.5 to 6.6 and 6.9 to 6.11, Platform Operators should ensure that there are prominent and clear warning statement(s) on their Online Platforms, where appropriate, to warn clients about a complex product prior to and reasonably proximate to the point of sale or advice.

*Note: Platform Operators should refer to guidance issued by the SFC from time to time for examples of the warning statement(s) that should be made on their Online Platforms.*

*Exemptions for Institutional and Corporate Professional Investors*

- 6.9 Platform Operators dealing with Institutional Professional Investors (as defined in the Code of Conduct) are automatically exempt from the requirements in paragraphs 6.3, 6.7 and 6.8.
- 6.10 To be exempt from the requirements in paragraphs 6.3, 6.7 and 6.8 when dealing with Corporate Professional Investors (as defined in the Code of Conduct), Platform Operators should observe and comply with the same requirements and procedures as set out in paragraphs 15.3A and 15.3B of the Code of Conduct<sup>40</sup>.
- 6.11 For the avoidance of doubt, no exemption is available to Platform Operators from the requirements in paragraphs 6.3, 6.7 and 6.8 when dealing with Individual Professional Investors (as defined in the Code of Conduct).

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<sup>40</sup> In order to be exempt from the provisions set out in paragraph 15.4 of the Code of Conduct (which includes an exemption from compliance with the Suitability Requirement) when dealing with Corporate Professional Investors, intermediaries are required to observe and comply with the requirements and procedures set out in paragraphs 15.3A and 15.3B of the Code of Conduct. On the same basis, Platform Operators should observe and comply with the same requirements and procedures in order to be exempt from paragraphs 6.3, 6.7 and 6.8 of these Guidelines when dealing with Corporate Professional Investors.