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New sophisticated professional investor regime – what you need to know



Background

The suitability requirement is the cornerstone of investor protection. It requires intermediaries to, when making a recommendation or solicitation of an investment product, ensure that the investment product in question is suitable for the client, having regard to the client's personal circumstances and risk tolerance.

On 23 December 2022, both the Hong Kong Monetary Authority ("HKMA") and the Securities and Futures Commission ("SFC") updated their Frequently Asked Questions (see HKMA [FAQ](#) and SFC [FAQ](#) here) to clarify the expected standards concerning the execution of suitability assessments and level of explanation needed to clients of varying degrees of financial sophistication.

The updated FAQs make it clear that intermediaries may vary their processes and perform suitability assessments in proportionate and risk-based manners. For example, as a wider range of investment products is more likely to be suitable for high net-worth clients who also exhibit financial expertise in relevant products and higher levels of risk tolerance, intermediaries could vary the suitability assessment process for these clients so long as they can demonstrate that the overall outcome is that recommendations provided to them are reasonably suitable.

Introduction to the new SPI regime

To address the feedback received from intermediaries about complying with their suitability obligations, the HKMA and SFC issued a [joint circular](#) on 28 July 2023 introducing a "**Streamlined Approach**" for compliance with suitability obligations when dealing with "sophisticated professional investors" ("**SPIs**"), effectively creating a new sub-category of individual professional investors who possess higher levels of net worth and knowledge or experience. See also the [detailed guidance](#) and [FAQs](#).

Under the new SPI regime, an intermediary may adopt the Streamlined Approach when dealing in eligible transactions for SPI clients, under which various investor protection measures do not apply.

We explore the SPI regime in greater detail below.

SPI qualifying criteria

An individual professional investor may be categorised as an SPI if an intermediary is satisfied that he/she meets all of the following criteria:

Financial Situation	Has a portfolio of at least HK\$40 million, or net assets (excluding primary residence) of at least HK\$80 million
Investment Objective	Is not a "conservative" client (an example of a conservative client is one whose investment objective is capital appreciation and/or regular income)
Knowledge or Experience	Possesses at least one of the following: (a) a degree or post-graduate diploma in accounting, economics or finance or a related discipline; (b) a qualification in CFA, CIIA, CPWP, CFP or other comparable qualification; (c) at least 1 year work experience in the financial sector; or (d) executed at least 5 transactions in the past 3 years for the product category in question.

A corporation which has as its principal business the holding of investments and is wholly-owned by one or more SPIs may be treated the same as the SPIs.

Eligible investment transactions

Intermediaries may only execute transactions for SPIs under the "Streamlined Approach" if the transaction in question falls within (a) a "Product Category" and (b) the "Streamlining Threshold", each as specified by and agreed upon with, the SPI.

In terms of the Product Category limb, intermediaries should:

- (a) devise "Product Categories", categorising investment products based on their terms, features, characteristics, nature and extent of risks;
- (b) document the SPI's choice of specified Product Categories;

- (c) provide a "Product Category Information Statement" (including warning statements where applicable) to the SPI to explain the terms, features, characteristics, nature and extent of risks of investment products within such Product Category; and
- (d) upon request, facilitate the SPIs' understanding of the Product Category Information Statement, as well as the terms and features of products within such Product Category.

The Streamlining Threshold refers to the maximum threshold of investment specified by the SPI, either as an absolute amount or a percentage relative to the SPIs' assets under management with the intermediary. In this regard, intermediaries should:

- (a) maintain proper records of any Streamlining Threshold set by the SPI, including the SPI's rationale for setting such a threshold;
- (b) establish and maintain effective systems and controls to ensure compliance with the Streamlining Threshold;
- (c) implement measures to detect outsize or material transactions, and issue warning statements to the SPI for these transactions; and
- (d) review compliance with the Streamlining Threshold at least annually, and alert the SPI where the gross exposure arising from investment transactions executed under a Streamlined Approach and/or positions maintained in the designated accounts have exceeded the Streamlining Threshold.

Exemptions under the Streamlined Approach

Under the "Streamlined Approach", intermediaries can execute investment transactions for an SPI if the investments in question fall within the Product Categories and Streamlining Threshold specified by the SPI.

What this means is that:

- (a) intermediaries are not required to:
 - (i) match the SPI's risk tolerance level, investment horizon or objective against the transactions;
 - (ii) assess the SPI's knowledge, experience or concentration risk; or
 - (iii) provide product explanation (unless the SPI requests otherwise);
- (b) intermediaries are not required to maintain records documenting the rationale underlying investment recommendations or solicitations made to SPIs; and
- (c) subject to the provision of offering documents, intermediaries are not required to perform due diligence on complex products where there is no element of recommendation or solicitation on their part, and can provide warning statements on an annual basis (instead of on a per-transaction basis).

Intermediaries should, however, always provide up-to-date product offering documents or summaries of key terms and features of the investment product in question, which could be done by sending a hyperlink to the relevant documents or as attachments via electronic means.

Steps to take before applying the Streamlined Approach

Prior to applying the Streamlined Approach, intermediaries will need to:

- (a) document the assessment of the client as an SPI and maintain all relevant records and supporting documents;
- (b) maintain records of all correspondences with the SPI to support the choice of Product Categories and Streamlining Threshold;
- (c) enter into a written agreement(s) (setting out the SPI's consent to be treated as an SPI, and his/her choice of Product Categories and Streamlining Threshold); and
- (d) explain the consequences of being treated as an SPI.

Intermediaries that would like to adopt the new SPI Streamlined Approach should also:

- (a) revisit and revise their written agreements, forms and templates concerning individual professional investors;
- (b) update their internal policies and procedures in relation to onboarding, suitability and selling practices;
- (c) devise product categories and prepare "Product Category Information Statements"; and
- (d) prepare the relevant documents for SPI assessment purposes; and
- (e) carry out annual reviews to ensure that SPIs continue to fulfil the requisite requirements to be treated as such, and continue to agree to the intermediary's adoption of the Streamlined Approach.

The HKMA and SFC have reminded intermediaries that they remain accountable for upholding proper conduct standards and managing related risks. Adoption of the Streamlined Approach does not in any way negate the requirement to have robust internal systems and controls in place.

How we can help

Individual investors with higher net worth, knowledge or experience, are a major component of Hong Kong's wealth management market. The new SPI regime is a positive development in allowing greater flexibility in product and service offerings, and should help attract more local and overseas high net worth investors to invest in Hong Kong, further boosting Hong Kong's role as an asset and wealth management hub.

The new Streamlined Approach will undoubtedly be welcome by intermediaries, as it will reduce administrative and regulatory overhead. Perhaps more importantly, it allows intermediaries to design portfolios and offer services that better suit the needs of the ultra-wealthy.

But an intermediary's documents, policies and systems will need to be revisited and updated, and that work will not be unsubstantial. That is where we can help.

We have extensive experience advising our clients in the financial sector on issues regarding suitability and the professional investor regime. Please get in touch if you are interested in discussing any of the above.

Contact us



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