

# **GUIDELINES ON COMPLIANCE FUNCTION FOR FUND MANAGEMENT COMPANIES**

**SC-GL/CGL-2005 (R2-2018)**

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## Chapter 1

### INTRODUCTION

- 1.01 The *Guidelines on Compliance Function for Fund Management Companies* is issued by the SC pursuant to section 377 of the *Capital Markets and Services Act 2007* (CMSA). These guidelines set out requirements to be complied with by any person intending to establish or carry out portfolio fund management activities in Malaysia.
- 1.02 These guidelines replaced the following guidelines:
- (a) *Guidelines on Compliance Function for Fund Managers*; and
  - (b) *Guidelines on Reporting Requirements for Fund Managers*.
- 1.03 These guidelines are aimed at ensuring that there are controls and compliance established towards ensuring investor protection and market confidence. In addition, these guidelines are also drawn up to ensure that fund management activities are carried out in compliance with regulatory requirements.
- 1.04 These Guidelines are in addition to and not in derogation of any other guidelines issued by the SC or any requirements as provided for under the securities laws; and must be read with:
- (a) *Guidelines on Islamic Fund Management*;
  - (b) *Guidelines on Prevention of Money Laundering and Terrorism Financing for Capital Market Intermediaries*;
  - (c) *Guidelines on Management of Cyber Risk*; and
  - (d) applicable provisions provided in the CMSA and all other relevant guidelines including the *Licensing Handbook*.
- 1.05 The SC may exempt where it deems appropriate or, upon application, grant exemptions or variations from compliance with any requirement in these guidelines.

## Chapter 2

### DEFINITIONS AND INTERPRETATION

2.01 In these guidelines, the following words have the following meanings, unless the context otherwise requires:

assets	means all monies (including cash and bank deposits) or other property received or retained by, or deposited with a holder of a CMSL in the course of its business for which the CMSL holder is liable to account to its clients, and any monies received or property deposited with or held by a custodian;
associated person	has the meaning as provided for in section 3 of the CMSA;
auditor	has the meaning as provided for in section 2 of the CMSA;
client	has the meaning as provided for in section 2 of the CMSA;
CMSL	means the Capital Markets Service Licence;
CMSRL	means the Capital Markets Service Representative Licence;
CMSA	means the <i>Capital Markets and Services Act 2007</i> ;
compliance officer	means the principal person responsible for compliance function;
cross trade	means a buy and sell transaction of the same security between two or more clients' accounts managed by a fund management company;
custodian	means an institution within the meaning of section 121 of the CMSA;
dealer	means a CMSL holder carrying on the business of dealing in securities;
employees	means persons employed by a fund management company including persons that are on secondment as well as the fund management company's representative, who is licensed under the CMSA to carry on the business of fund management;
fund management company	means a CMSL holder carrying on the business of fund management as defined in Part 2 of Schedule 2 of the CMSA;
IMA	means an investment management agreement;
related corporation	has the meaning as provided for in section 2 of the CMSA;
representatives	has the meaning as provided for in Section 2 of the CMSA;

relatives	means spouse and children;
SC	means the Securities Commission Malaysia;
statement of account	means the summary position of portfolio which includes revenues earned and expenses incurred as well as movement of cash and investment activities in a stated period.

## Chapter 3

### CORE PRINCIPLES

- 3.01 The SC is actively promoting a culture of compliance, professionalism, ethical standards and responsible conduct among fund management companies and their representatives and employees.
- 3.02 A fund management company must ensure compliance with the following core principles:

<b>Core Principles</b>	
1. Integrity	A fund management company must conduct its business with integrity.
2. Skill, care and diligence	A fund management company must conduct its business with due care, skill, and diligence.
3. Acting in clients' interests	A fund management company must always act in the interest of its clients and must not jeopardise or prejudice clients' interests.
4. Supervision and control	A fund management company must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management and supervisory system.
5. Adequate resources	A fund management company must maintain adequate financial, human and other resources which commensurate with its business.
6. Business conduct	A fund management company must conduct its business in a manner that promotes a fair and orderly market.
7. Client asset protection	A fund management company must ensure that clients' assets are safeguarded at all times and must not make improper use of clients' assets.
8. Communication with investors and clients	A fund management company must provide relevant information to investors and its clients in a manner that is fair, accurate and timely.
9. Conflict of interest	A fund management company must manage conflict of interest fairly, both between itself, its employees and clients, and between a client and another client.

<b>Core Principles</b>	
10. Compliance culture	The Board of Directors of a fund management company must ensure proper policies and procedures are in place to ensure a sound compliance framework which safeguards clients' interests.
11. Dealing with the SC	A fund management company must deal with the SC in an open, co-operative and timely manner.



## Chapter 4

### KEY RESPONSIBILITIES

#### The Board's responsibilities

- 4.01 These guidelines place the responsibility for compliance with all laws, regulations and guidelines on the Board of Directors.
- 4.02 At all times, the Board of Directors must ensure–
- (a) only licensed persons can carry out regulated activities;
  - (b) at least one director is a CMSRL holder;
  - (c) the fund management company complies with the 11 core principles as set out in Chapter 3 and the securities laws, regulations and all relevant guidelines;
  - (d) the fund management company–
    - (i) establishes, maintains and implements an effective internal control framework to prevent and detect abusive or inappropriate investment practices or conflicts of interest between proprietary transactions, employees' transactions, and clients' transactions;
    - (ii) conducts at least yearly review on the effectiveness of its internal control framework; and
    - (iii) reports to the shareholders of any findings from the review as specified in the above (d)(ii);
  - (e) written policies and procedures are in place to–
    - (i) enable full disclosure of clients' accounting records and assets to the clients;
    - (ii) provide clear line of reporting, authorisation and proper segregation of functions with a view to manage conflicts of interest that may arise in the course of doing its business;
    - (iii) prevent any flow of price sensitive information between the different areas of operations of the organisation;
    - (iv) prevent unauthorised or fraudulent transactions;
    - (v) prevent front running, churning or any other market misconduct by directors or employees;
    - (vi) preserve confidentiality of clients' information; and

- (vii) mitigate the risk arising from a situation where an individual is in control of all aspect pertaining to a single transaction;
- (f) the fund management company has a written business continuity plan in place;
- (g) policies and procedures affecting the staff responsibilities are effectively communicated;
- (h) competent persons are appointed to supervise and manage the fund management company and that such persons are always subject to oversight of the Board;
- (i) that the fund management company always has adequate financial, human, technology and other resources which commensurate with its business;
- (j) that it assess the fund management company's cyber security resilience and preparedness including confidentiality, integrity and availability of data and services as stipulated under the *Guidelines on Management of Cyber Risk*;
- (k) the fund management company establishes and maintains proper system of record keeping relating to-
  - (i) fund management company's information; and
  - (ii) clients' information;
- (l) clients' assets are safeguarded and clients receive information as specified in these guidelines;
- (m) one or more compliance officers are appointed, who-
  - (i) have the qualifications and experience as stipulated in the *Licensing Handbook*;
  - (ii) have the necessary authority, resources and support to administer independently and effectively, the implementation of the fund management company's compliance policies and procedures;
  - (iii) must not perform any other duties that may compromise or conflict with the compliance officer's responsibilities;
  - (iv) reports directly to the Board and compliance committee (where such committee has been established);
- (n) all matters raised by the compliance officer or the compliance committee (where such committee has been established), including any non-compliance with any provisions of the relevant laws, regulations and guidelines, are properly addressed;

- (o) that it undertakes an effective oversight function on the overall compliance framework of the fund management company;
- (p) that it conducts at least an annual review on the effectiveness of the compliance framework;
- (q) that it provides effective and adequate support to the compliance officer and ensure that the compliance officer is not prevented in any way from discharging his responsibilities including making the appropriate report to the relevant regulatory authority on any breaches or non-compliance; and
- (r) that where the fund management company offers digital investment management services, the additional requirements set out in Chapter 13 of these Guidelines must be complied with.

4.03 The requirements set out in the above paragraph 4.02 (e) (ii) and (iii) must also be taken into account where the fund management company is part of a group of companies.

### **Compliance officer's responsibilities**

4.04 A compliance officer's responsibilities include–

- (a) acting as a liaison person with the SC;
- (b) establishing and maintaining a comprehensive compliance manual;
- (c) establishing, maintaining and administering the implementation of policies and procedures to–
  - (i) ensure compliance with securities laws, regulations and relevant guidelines; and
  - (ii) detect and prevent breaches of securities laws, regulations and relevant guidelines;
- (d) reviewing and updating the compliance policies and procedures in line with changes in the laws, regulations and guidelines;
- (e) keeping abreast of changes to securities laws, regulations and relevant guidelines, and relevant industry developments, and ensure timely dissemination of information pertaining to such changes and developments within the fund management company;
- (f) co-ordinating the fund management company's compliance efforts including disseminating compliance manuals, policies and procedures and any other compliance related information within the company;
- (g) establishing a compliance programme and carrying out an annual review of the said programme;

- (h) monitoring that only licensed persons conduct the activities stipulated in paragraph 5.16;
- (i) working closely with the Board and senior management personnel on all compliance matters and liaising with other departments/divisions to discharge the duties and functions effectively;
- (j) assisting in training and educating staff members on compliance matters;
- (k) reviewing reports to ensure that clients' portfolios are managed in accordance with agreed mandate;
- (l) monitoring that account opening procedures are strictly adhered to, which includes–
  - (i) obtaining the necessary information of the client;
  - (ii) being satisfied that the client has the authority or approval to enter into an IMA; and
  - (iii) ensuring that a written IMA is executed;
- (m) ensuring that processes and procedures are in place to deal with clients' complaints in a fair, timely and effective manner;
- (n) furnishing the Board and compliance committee (where such committee has been established) at least on quarterly basis, with a written report which includes–
  - (i) any material changes or recommendations made in respect of those changes to the fund management company's compliance policies and procedures;
  - (ii) listing out all breaches of securities laws, regulations, relevant guidelines and steps taken to remedy and prevent such breaches from recurring; and
  - (iii) listing out all clients' complaints;
- (o) extending to the SC information as specified in the above subparagraph (n)(ii);
- (p) submitting in a timely and accurate manner any information that is required by the SC;
- (q) where a fund management company manages a Shariah mandate, the compliance officer must ensure compliance with requirements stipulated in the *Guidelines on Islamic Fund Management* and any relevant SC regulations; and

- (r) where a fund management company offers digital investment management services, the compliance officer must also ensure compliance with the additional requirements set out in Chapter 13 of these Guidelines.

## Chapter 5

### ORGANISATION AND MANAGEMENT

#### Internal audit

- 5.01 The Board of Directors is encouraged to establish an internal audit function to develop, implement and maintain an appropriate internal audit framework that commensurate with the fund management company's business.
- 5.02 The internal audit function may be carried out internally or may be outsourced in the manner specified in the *Licensing Handbook*.
- 5.03 Notwithstanding that the fund management company's internal audit function may be outsourced, the Board of Directors must ensure that the internal audit framework includes–
- (a) planning, controlling and recording all internal audit work performed;
  - (b) recording all findings, conclusions and recommendations of the internal audit work performed; and
  - (c) producing an internal audit report at the conclusion of each internal audit work.
- 5.04 The Board of Directors must review the internal audit report and ensure that all matters raised in the internal audit report are resolved in a manner that does not jeopardise or prejudice clients' interests.

#### Risk management

- 5.05 The Board of Directors must establish, implement and maintain a risk management framework that commensurate with the fund management company's business.
- 5.06 A fund management company's risk management framework must include–
- (a) continuously identifying, assessing and monitoring the fund management company's risks;
  - (b) managing and monitoring risks assumed by the fund management company on behalf of its clients; and
  - (c) mitigation actions to address such risks.
- 5.07 Where functions are outsourced, a fund management company's risk management framework must include–
- (a) performing due diligence on the nature, scope and complexity of the outsourcing to identify key risk areas and risk mitigation strategies;

- (b) conducting review of its outsourcing arrangement and identifying new risks which may arise; and
  - (c) analysing the impact of the outsourcing arrangement on the overall risk profile of the fund management company, and whether there are adequate measures and resources in place to mitigate the risks identified.
- 5.08 A fund management company must conduct at least an annual review of its risk management framework.

### **Business continuity plan**

- 5.09 A fund management company's business continuity plan must–
- (a) ensure that the fund management company's critical operations can continue to function in the event of any interruptions;
  - (b) include an annual review and testing to ensure its effectiveness; and
  - (c) deal with interruptions in any of the fund management company's outsourced functions.
- 5.10 The business continuity plan including the outcome of its annual review and testing under subparagraph 5.09(b) must be reported to the Board of Directors.

### **Outsourcing**

- 5.11 A fund management company may outsource any of its functions to a service provider subject to the requirement stipulated in the *Licensing Handbook*.
- 5.12 A fund management company must ensure that the service provider has the capabilities and capacity to efficiently fulfil its duties and responsibilities in respect of the outsourced function and there must be ongoing monitoring of the service provider to ensure that the *Licensing Handbook* are complied with.

### **Training and education**

- 5.13 A fund management company must ensure that its executive directors and employees, including the compliance officer and personnel involved in operations are adequately trained and kept abreast of industry developments.
- 5.14 Details of all training provided are to be properly maintained by the fund management company.

## **Delegation of fund management function**

- 5.15 A fund management company may delegate its fund management function to another fund management company.
- 5.16 Notwithstanding paragraph 5.15, a fund management company must ensure that the following activities are not delegated:
- (a) Soliciting investors to be clients of the fund management company;
  - (b) Performing risk profiling of clients;
  - (c) Any interaction and communication with clients of the fund management company;
  - (d) Recommending investment policies or investment recommendations to clients; and
  - (e) Reporting to clients in respect of the clients' portfolios under management.
- 5.17 Where a fund management company delegates its fund management function–
- (a) responsibilities and obligations to the clients; and
  - (b) compliance with obligations and principles provided for in these guidelines,
- must remain at all times with the fund management company.
- 5.18 A fund management company must ensure that the company to which the function is delegated–
- (a) is a CMSL holder carrying on the regulated activity of fund management; or
  - (b) in the case of a company outside Malaysia, is properly licensed or authorised by the relevant regulator in its home jurisdiction to carry out fund management activities; and
  - (c) has the necessary expertise, systems, procedures and processes to carry out the function.
- 5.19 A fund management company must have an arrangement in place to monitor the conduct and activities of the company to whom the function is delegated.
- 5.20 A fund management company must provide prior notification to the SC in writing if it delegates its fund management function to another company and inform the SC of subsequent changes to the delegation arrangement.



## Chapter 6

### DISCLOSURE AND CONDUCT

#### Disclosure of interests

- 6.01 A fund management company must establish, maintain and implement written policies and procedures for the fund management company, its directors, investment committee members (where such committee has been established) and employees to disclose all interests or holdings in securities, other assets including alternative products, and any interests in a special purpose vehicle (SPV) arrangement.
- 6.02 All disclosures by the fund management company's directors, investment committee members (where such committee has been established) and employees of their interest as provided in paragraph 6.01 must be made:
- (a) upon joining;
  - (b) at least annually thereafter; and
  - (c) as and when there are changes to their interests or holdings.
- 6.03 A fund management company must ensure that clients' interests are not superseded by the interests of associated persons related to the-
- (i) fund management company;
  - (ii) directors of the fund management company;
  - (iii) investment committee members of the fund management company; and
  - (iv) employees of the fund management company.
- 6.04 A fund management company must maintain records of disclosures made by the fund management company, its directors, investment committee members and employees.

#### Disclosure by a fund management company

- 6.05 A fund management company must disclose to clients of its interest or holdings in securities, other assets including alternative products, and any interests in a SPV arrangement.

### **Disclosure and conduct of directors**

- 6.06 A director must disclose to the fund management company of his interests or holdings in securities, other assets including alternative products, and any interests in a SPV arrangement, whether directly or indirectly, including through nominees or relatives.
- 6.07 Where the director is an Executive Director, the prior approval of any other directors, a compliance committee (where such committee has been established) or compliance officer must be obtained before he carries out his investment.

### **Disclosure and conduct of Investment Committee members**

- 6.08 Investment committee members (where such committee has been established) must disclose to the fund management company of their interests or holdings in securities, other assets including alternative products, and any interests in a SPV arrangement, whether directly or indirectly, including through nominees or relatives.
- 6.09 Members of the investment committee must abstain from meetings where their presence may cause any conflict or potential conflict of interest.

### **Disclosure and conduct of employees**

- 6.10 An employee must disclose to the fund management company of his interests or holdings in securities, other assets including alternative products, and any interests in a SPV arrangement, whether directly or indirectly, including through nominees or relatives.
- 6.11 The prior approval of any director or compliance officer must be obtained by the employee before he carries out his investment.

## **Chapter 7**

### **DEALING WITH CLIENTS**

#### **Fees, charges and other remunerations**

7.01 All fees and charges imposed on a client must be fair, reasonable and transparent.

#### **Valuation of clients' portfolios**

7.02 A fund management company must perform at least on monthly basis, valuation of clients' portfolios in a manner that is agreed by the clients.

#### **Statements and reports to clients**

7.03 A fund management company must provide a statement relating to a client's portfolio directly to each client, at least on monthly basis. The statement must, among others, include the following information:

- (a) A statement of account showing the client's actual portfolio position; and
- (b) Fees and charges payable by the client.

7.04 A fund management company must provide, at least on quarterly basis, reports to its clients on the following:

- (a) The performance of each client's portfolio against appropriate benchmarks;
- (b) Any changes in risk (if any) which will affect the client's investments; and
- (c) Any impact on the client's capital and earning of the client's investment arising from the change in risk as specified in subparagraph (b) above.

#### **Confidentiality**

7.05 A fund management company must establish, maintain and implement written policies and procedures to maintain confidentiality of clients' records and information which includes policy relating to access by a service provider or a sub-contractor (as the case may be) and measures against access by employees managing proprietary accounts.

7.06 Any clients' information must not be disclosed to a third party or an unauthorised person, unless clients' prior consent has been obtained or where there is a legal or regulatory requirement to disclose such information.

## **Complaints by clients**

- 7.07 A fund management company must establish, maintain, and implement written policies and procedures to ensure that–
- (a) complaints from its clients are handled in a timely and appropriate manner; and
  - (b) clients' complaints are satisfactorily resolved.
- 7.08 A fund management company must maintain a register of complaints received and any actions taken, and ensure that the compliance officer has a copy of the register.

## Chapter 8

### MARKETING, ADVERTISING AND PROMOTIONAL MATERIALS

#### Representation by fund management company

8.01 A fund management company must ensure that any representations, including in the form of electronic communication made to clients are conducted with due care, skill and diligence to enable the clients to make balanced and informed decisions.

#### Information about the fund management company

8.02 A fund management company must–

- (a) provide clients with adequate information about the fund management company's shareholding, business address, relevant conditions or restrictions under which its business is conducted, key personnel and persons with whom clients may have contact, and subsequent changes made thereafter;
- (b) inform the clients of any significant changes to the organisation that could affect clients' interests; and
- (c) provide any other relevant information required by the clients.

#### Advertisements and promotional materials

8.03 A fund management company must ensure that information disclosed or contained in marketing, advertising and promotional materials is fair, accurate and timely and such information must include the following:

- (a) Risks of investments;
- (b) Unique features, characteristics of investments and the nature of underlying assets (if any);
- (c) Any conflict of interest that may arise from investments; and
- (d) Policies in handling conflict of interest stated in the above subparagraph (c) to enable the clients to make an assessment of whether such conflicts are managed and not detrimental to the clients' interest.

8.04 Where the marketing, advertising and promotional materials contain any statements on the fund management company's performance, where possible, the fund management company should ensure such statements are independently verified.

- 8.05 In the event the marketing, advertising and promotional materials contain any statements on compliance with an independent performance presentation standard, a fund management company must ensure that the statements are verified by an independent actuarial, financial or statistical reporting service provider.
- 8.06 A fund management company must disclose to its clients the source of such verification in the marketing, advertising and promotional materials. Where no such verification has been obtained, the same must also be disclosed to its clients.
- 8.07 A fund management company must ensure that any statements made as to the future investment performance mentioned in the marketing, advertising and promotional materials, are adequately supported.
- 8.08 Where any marketing, advertisements and promotional materials quotes an investment performance, a fund management company must ensure that the period for which the performance quoted is–
- (a) clearly stated;
  - (b) for a period of at least one year or more; and
  - (c) not based on selection of a preferential period.
- 8.09 All marketing, advertising and promotional materials should be reviewed by the compliance officer prior to issuance.

## Chapter 9

### PORTFOLIO MANAGEMENT

#### Investment within clients' mandates

- 9.01 A fund management company must have reasonable and adequate basis in setting the investment policy, making investment recommendation or carrying out any transactions for a client.
- 9.02 Implementation of each client's investment policy or investment recommendation can only be made after the fund management company–
- (a) establishes and understands each client's risk profile, investment objectives, limitations, restrictions and instructions;
  - (b) provides each client with complete and accurate information of investments including any unique features, characteristics of investments and the nature of underlying assets (if any), to enable the client to make an informed investment decision;
  - (c) obtains the client's prior approval;
  - (d) explains to the client of general and specific investment risks including but not limited to pricing, liquidity and any rights, obligations and attribution of ownership under the investment policy or investment recommendation;
  - (e) establishes and documents the client's ability and willingness to accept the risks identified in the above subparagraph (d); and
  - (f) has made the necessary arrangement to allow the fund management company to have the relevant investment information for monitoring purposes.
- 9.03 A fund management company must not recommend or invest in any investment products including alternative products where the fund management company does not understand its structure, pricing mechanism and nature of underlying assets (if any) of such products.
- 9.04 Where SPV or similar structures are used to pool clients' investments, a fund management company must ensure that such arrangement is structured in accordance with the *Guidelines on Unlisted Capital Market Products under the Lodge and Launch Framework*.
- 9.05 A fund management company must review a client's investment policy under discretionary mandate at least annually or whenever circumstances require changes to be made.

- 9.06 A fund management company must ensure that the investment policy, investment recommendations and transactions carried out are in accordance with the clients' mandates, and sufficient assets are available in the clients' accounts to carry out such transactions.
- 9.07 A fund management company must maintain proper records of clients' details and other relevant information including supporting documents for investment policy and investment recommendation.

## **Research**

- 9.08 A fund management company must establish, maintain and implement written policies and procedures to ensure its research is independent and impartial in order to provide a reasonable and adequate basis for making investment decisions and taking investment action.

## **Investment management agreement**

- 9.09 A fund management company must ensure that its client has adequate authority and capacity to enter into an agreement for the management of assets.
- 9.10 A fund management company must ensure that it enters into a written IMA with each client before providing any fund management services, or transacting on behalf of a client.
- 9.11 A fund management company must ensure that the written agreement includes–
- (a) clients' risk profiles and investment objectives including any investment limitations, restrictions or instructions;
  - (b) notification of any significant changes to the investment policy or investment recommendation;
  - (c) clear authorisation from the clients for discretionary mandate;
  - (d) scope of services that will be provided by the fund management company including frequency of written statements and reports relating to the clients' portfolios;
  - (e) fees and charges to be paid by the clients or any other remuneration received by the fund management company from any other person in relation to services provided to the clients;
  - (f) details of custodial arrangement;
  - (g) basis of valuation to be used for any type of investments products;
  - (h) terms and conditions relating to soft commission, where applicable;
  - (i) liability of fund management company where there is a breach of the IMA;



- (j) conditions for alteration and termination to the IMA and its implications thereof in respect of settlement, repayment obligations and surrender of documentation; and
- (k) details of delegation of the fund management company's function (if any).

9.12 A fund management company must ensure that the written agreement as provided for in paragraph 9.11 must be in accordance to the requirements of the law and these guidelines.

## **Chapter 10**

### **SAFEGUARDING CLIENTS' ASSETS**

#### **General**

- 10.01 Assets of a fund management company and its clients must be properly identified and separately maintained in a trust account.
- 10.02 A fund management company must make adequate arrangements to safeguard clients' ownership rights on all clients' assets and ensure that the client assets are properly accounted for at all times.
- 10.03 A fund management company must ensure that clients' assets are properly safeguarded from conversion or inappropriate use by its employees.
- 10.04 Where a fund management company receives instruction to withdraw assets from a client's account, such assets must be delivered directly to that client and not to a third party.
- 10.05 A fund management company must promptly notify all clients in writing of its intention to cease its business and ensure proper arrangements are in place for the safekeeping of clients' assets. Where a fund management company is being wound up, it must comply with regulatory requirements stipulated in the CMSA.

#### **Appointment of a custodian**

- 10.06 A fund management company must appoint a custodian to maintain a trust account for its clients' assets to ensure that clients' assets are properly safeguarded.
- 10.07 Only persons who are listed in section 121 of the CMSA can be appointed as a custodian and a fund management company must not act as the custodian for the clients' assets.
- 10.08 Where the custodian is appointed directly by the client, a fund management company must notify the clients of the requirements relating to custodial arrangement.

#### **Custodial arrangement**

- 10.09 In appointing a custodian, a fund management company must–
  - (a) obtain clients' prior written consent for the appointment of the custodian;
  - (b) notify the clients in writing of the custodian's details, sub-custodian's details (if any) and any changes made to the custodial arrangements thereafter;

- (c) notify the clients that assets received or held outside Malaysia are subject to regulations of the foreign jurisdiction and may not be subject to the same protection as that conferred on client assets received or held in Malaysia;
- (d) provide the custodian with sufficient client identification documents;
- (e) ensure that clients' assets are segregated in the custodian's books to enable attribution and repatriation of the assets to the respective clients;
- (f) ensure that the trust account maintained by the custodian reflects that the assets belong to the clients of a fund management company;
- (g) require the custodian to ensure that all proceeds and revenue generated from investments are credited into the relevant clients' accounts immediately;
- (h) ensure that the custodian has sufficient control in place to safeguard clients' assets from conversion or inappropriate use by its employees;
- (i) notify the affected clients promptly and make proper arrangements to safe keep clients' assets prior to termination of any custodial agreements; and
- (j) perform at least an annual evaluation of the appointed custodian and its services to ensure that the custodian has carried out its responsibilities with due care, skill and diligence.

10.10 The assessment referred to under paragraph 10.09(j) should include–

- (a) performance of custodial services by the custodian;
- (b) arrangements that the custodian has in place in custodising clients' assets;
- (c) adverse changes in the prevailing market conditions of the country that a custodian outside Malaysia is operating from, which may impact the undertaking of custodial function; and
- (d) custodian's compliance with Chapter 10 of these guidelines.

10.11 A fund management company must ensure that its written agreement with a custodian stipulates that the custodian–

- (a) maintains records that would enable identification of assets to respective clients;
- (b) conducts reconciliation of clients' accounts on daily basis against third-party records;
- (c) delivers clients' statement, which includes client's portfolio position and transactions during the period, at least on a quarterly basis, directly to the respective clients;

- (d) verifies any instructions to transfer assets and notifies the client of such transfer of assets; and
- (e) exercises due care to effect transfer in any apparent conflict-of-interest situation.

10.12 Where a custodian sub-delegates its custodial role, the fund management company must ensure that–

- (a) the sub-custodian is licensed or authorised to provide custodian services in their respective jurisdiction; and
- (b) such sub-delegation will not affect the custodian in carrying its obligations as provided for in paragraph 10.11.

### **Trust account**

10.13 All clients' trust accounts must carry the name of custodian or the name of fund management company (may be abbreviated but must be sufficiently distinctive) or both; and unique identifier of client which include–

- (a) full name of client; or
- (b) identity card number; or
- (c) passport number; or
- (d) company number if the client is a company; or
- (e) any unique identifiable and verifiable code.

10.14 Where the trust account is maintained under an omnibus structure, a fund management company must ensure that–

- (a) co-mingling of assets at custodian or the issuer of assets level is confined to clients of the same fund management company;
- (b) in terms of naming conventions as provided for in paragraph 10.13, '*clients' account*' or '*clients' trust account*' is maintained in substitution of the unique identifier of client; and
- (c) such arrangement will not affect the custodian in carrying its obligations as provided for in paragraph 10.11.

## Chapter 11

### MANAGING CONFLICTS OF INTEREST

#### General

11.01 A fund management company must establish, implement and maintain conflicts of interest policy and procedures that commensurate with the fund management company's business, which include:

- (a) identification of the specific services and activities carried out by or on behalf of the fund management company, and situations that give or may give rise to a conflict of interest;
- (b) measures to be adopted to manage the conflicts of interest identified in subparagraph (a) above;
- (c) appropriate internal structures and reporting lines to enable effective management of conflicts of interest; and
- (d) proper documentation and record keeping.

#### Conflicts of interest identification

11.02 A fund management company must take all reasonable steps to identify situations where conflicts of interest between:

- (a) the fund management company, including its directors, investment committees members (if any), employees and appointed representatives, or any person directly or indirectly related to them, and its client; and
- (b) its client and other clients;

arise or may arise in the course of the fund management company providing its services.

11.03 In identifying situations that give or may give rise to a conflict of interest, a fund management company must take into account whether the fund management company, including its directors, investment committees members (if any), employees and appointed representatives, or any person directly or indirectly related to the fund management company:

- (a) is likely to make a financial gain, or avoid a financial loss, at the expense of the client;
- (b) has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of the client, other than the client's interest in that outcome;

- (c) has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client;
- (d) carries on the same business as the client; or
- (e) receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monies, goods or services, other than the standard commission or fee for that service.

### **Conflicts of interest management**

11.04 A fund management company must ensure that it adopts measures to mitigate and manage, or avoid (where necessary) situations of conflict of interest referred to in paragraph 11.02. The measures adopted must include:

- (a) procedures to prevent or control the exchange of information between persons engaged in activities that give rise to a risk of a conflict of interest;
- (b) prevention or limitation of any person from exercising inappropriate influence over the way in which a relevant person carries out services or activities;
- (c) limitation or control of the involvement of personnel in separate services or activities where such involvement may impair the proper management of conflicts of interest;
- (d) monitoring procedures to ensure that any non-compliance with the conflicts of interest policy is identified, appropriately and timely acted upon; and
- (e) a revision of the conflicts of interest policy at least on an annual basis and, where necessary, updated to ensure that the arrangements are relevant and adequate to identify, assess, and evaluate the effectiveness of controls in place.

11.05 Where the fund management company carries out a combination of regulated activities, it must take reasonable steps to minimise and manage any conflict of interest that may arise in carrying out such activities.

### **Disclosure of conflicts of interest**

11.06 Conflicts of interest and the policies in handling such conflicts must be disclosed to clients.

11.07 The disclosure must be timely, prominent, specific and meaningful to the client to enable the client to make an informed assessment of whether such conflicts are managed appropriately and not detrimental to the client's interest.

### **Proprietary transactions**

- 11.08 In order to avoid conflict of interest between the fund management company's proprietary transactions and clients' transactions, it must–
- (a) establish information barriers or firewalls; and
  - (b) closely supervise internal communication to prevent flow of information.
- 11.09 A fund management company must ensure that the CMSRL holder conducting its proprietary transactions does not manage clients' assets.

### **Receipt or provision of benefits**

- 11.10 A fund management company must establish, maintain and implement written policies and procedures including, but not limited to, monetary limits, pertaining to any acceptance or giving of gifts or any benefits by the fund management company or its employees.
- 11.11 A fund management company must not offer or accept any gifts or benefits which conflicts with the interest of or the duties owed to the clients.
- 11.12 A fund management company must maintain a register of gifts or benefits received or given.

### **Rebates and soft commission arrangements**

- 11.13 A fund management company must not accept or receive any rebates arising from transactions or orders on behalf of clients. Any rebates received must be directed to the account of the relevant clients.
- 11.14 In accepting or receiving soft commission arising from transactions or orders on behalf of a client, a fund management company–
- (a) must not utilise the soft commission for the purpose of defraying costs relating to the establishment or maintenance of its infrastructure, framework or systems; and
  - (b) must ensure that the:
    - (i) client's prior consent has been obtained; and
    - (ii) goods and services are in the form of research and advisory services that assist in the decision-making process relating to the client's investments.
- 11.15 A fund management company must disclose to the client details of any soft commission received as soon as practicable upon accepting or receiving the soft commission.

- 11.16 A fund management company must maintain a register of any soft commission accepted or received.
- 11.17 A compliance officer must verify that any soft commission accepted or received by the fund management company complies with the requirement provided in paragraph 11.14.

### **Order allocation**

- 11.18 A fund management company must establish, maintain and implement written policies and procedures to ensure fair and equitable allocation of orders among clients.
- 11.19 Where a fund management company uses block trades, allocation of securities should be conducted on a pro-rata basis and using an average price.
- 11.20 Where a fund management company undertakes proprietary trading, the selection method in determining the securities to be transacted for the fund management company's proprietary account and the clients' accounts must be disclosed to clients.
- 11.21 The fund management company must ensure that trades are not directed to benefit its proprietary account or any preferential clients.
- 11.22 A fund management company must ensure that the amount of commission or management fee earned from any particular clients or transaction must not be the determining factor in the allocation of orders.

### **Best execution**

- 11.23 A fund management company must establish, maintain and implement written policies and procedures to ensure best execution of trades for its clients.
- 11.24 Prior to executing any investments for a client, a fund management company must ensure that–
- (a) the investment transaction is carried out in accordance with the client's mandate and within limits prescribed in the IMA; and
  - (b) the relevant account has sufficient assets to meet the obligations of the transaction.
- 11.25 A fund management company must ensure that the use of any dealer or financial institution for the execution of its trades must not exceed 50% of the total dealings in value in any one financial year.
- 11.26 Investment transactions carried out on behalf of a related corporation must be at arm's length and consistent with best execution standards.



## **Cross-trades**

- 11.27 A fund management company must establish, implement and maintain written policies and procedures governing cross trades between clients' accounts.
- 11.28 Subject to paragraph 11.29, prior consent from clients must be obtained in documented form or details of the fund management company's policy on cross-trades must be disclosed in a fund's offering document (whichever is applicable), and cross trades can only be undertaken provided that the–
- (a) sale and purchase decisions are in the best interest of both clients;
  - (b) reason for such transactions is documented prior to execution of the trades;
  - (c) transactions are executed through a dealer or a financial institution on an arm's length and fair value basis; and
  - (d) cross trade transactions are disclosed to both clients.
- 11.29 Cross-trades between–
- (a) employee of the fund management company and the clients; or
  - (b) the fund management company for its proprietary trading and its clients,
- are prohibited.
- 11.30 A compliance officer must verify that any cross trade undertaken by the fund management company complies with the requirement provided in paragraph 11.28.

## **Chapter 12**

### **RECORD KEEPING**

#### **Accuracy of records**

- 12.01 A fund management company must ensure that records are accurate, properly secured and retained.
- 12.02 A fund management company must immediately carry out reconciliation of its records against third-party records to ensure accuracy of records.
- 12.03 A fund management company must maintain comprehensive records of its–
- (a) proprietary trading and accounting records; and
  - (b) clients' accounts and transactions.
- 12.04 A fund management company must ensure that the internal audit and compliance officers have access to such records at all times.
- 12.05 A fund management company must authorise its external auditor to obtain statements and confirmation from custodians on the accounts that contain clients' assets.
- 12.06 A fund management company must prepare and maintain its financial statements in accordance with approved accounting standards.

#### **Retention of records**

- 12.07 A fund management company must take reasonable care to retain adequate records of all matters including all transactions, dealings, accounting records and compliance review in accordance with the requirements of the law and these guidelines.
- 12.08 A compliance officer must ensure that the fund management company maintains and keeps such records in an easily accessible place for at least seven years after the last transaction was executed.

## Chapter 13

### ADDITIONAL REQUIREMENTS RELATING TO A DIGITAL INVESTMENT MANAGEMENT COMPANY

#### General

13.01 This chapter sets out the additional requirements applicable to a fund management company carrying on the business as a digital investment management company.

#### The Board's responsibilities

13.02 In addition to paragraph 4.02, the Board of Directors must ensure-

- (a) that the digital investment management company has technology capabilities and support to undertake the digital investment management business. The digital investment management company must -
  - (i) have sufficient understanding of the rationale, risks and rules behind the algorithm underpinning the digital investment management business;
  - (ii) at all times, ensure the outcomes produced by the algorithm in the above subparagraph (i)-
    - (A) are consistent with the digital investment management company's investment strategies;
    - (B) commensurate with the risk profile of the investor; and
    - (C) complies with securities laws and relevant guidelines;
  - (iii) have the system to support the digital investment management business which includes maintaining a secure environment pursuant to the *Guidelines on Management of Cyber Risk* and other relevant guidelines;
- (b) that it conducts at least an annual review on the effectiveness of the governance and supervision of the technology and algorithm underpinning the digital investment management business.

#### Compliance officer's responsibility

13.03 In addition to paragraph 4.04(g), a compliance officer's responsibility includes establishing a compliance programme which takes into consideration the unique and specific aspects of the digital investment management's business model.

## **Risk management**

13.04 In addition to paragraph 5.06, a digital investment management company's risk management framework must also include any other risks related to the digital investment management business.

## **Disclosure to clients**

13.05 In addition to paragraph 8.03, a digital investment management company must disclose and display prominently on its platform, any relevant information relating to the digital investment management company, including–

- (a) that an algorithm is used;
- (b) the function of the algorithm used;
- (c) the assumption and limitation of the algorithm;
- (d) the risks inherent in the use of technology;
- (e) the direct and indirect fees, charges and other remunerations related to services provided;
- (f) the investment strategies used and any future changes to the strategy; and
- (g) information about complaints handling or dispute resolution and its procedures.

13.06 Presentation and substance of the key disclosures must be clear and effective in a manner that is easily understood to enable clients to make informed investment decisions.

## **Algorithm design and oversight**

13.07 A digital investment management company must establish, maintain and implement written policies and procedures which include ensuring:

- (a) the algorithm is monitored and tested to ensure it is fit for purpose at all times;
- (b) access to and the ability to make changes to the algorithm is limited to authorised personnel only; and
- (c) ongoing due diligence on any third party that develops, owns or manages the technology and algorithm utilised by the digital investment management company.