



香港財經分析師學會

THE HONG KONG SOCIETY OF FINANCIAL ANALYSTS

19th June 2014

Sent by Email and by Post

Financial Services Branch
Financial Services and the Treasury Bureau
24/F Central Government Offices
2 Tim Mei Avenue, Tamar
Hong Kong

Dear Sirs/Madams,

Re: Consultation Paper on Open-ended Fund Companies

The Hong Kong Society of Financial Analysts (“HKSFA”) is pleased to comment on the consultation concerning the open-ended fund companies. The HKSFA is basically supportive of the introduction of a new open-ended fund company structure to expand Hong Kong’s legal structure for investment fund vehicles and further open up Hong Kong’s capacity for asset management activities though we believe publicly and privately offered open-ended fund companies (“OFCs”) should be treated differently in order to give more flexibility for privately offered funds to pursue their investment strategies in terms of the regulatory requirements and legislative framework. In addition, we believe that profits tax exemption for public and privately offered funds should be treated consistently to encourage the setup of funds in Hong Kong.

Based on our positions, we state our comments to the specific questions set out in this Consultation Paper as follows :

Q1. Do you agree with the overarching principles with Open Ended Fund Companies (OFCs)?

- Yes, for publicly offered OFCs. We agree that these funds should be subject to the same regulatory requirements applicable to existing publicly offered funds.
- No, for privately offered OFCs. These funds should be given flexibility to pursue their own investment strategies. They should be allowed to invest in any asset class and subject only to its own restrictions contained in their constitutional documents.

Q2. Do you consider it agreeable to set out the legislative framework for OFC in the SFO and the relevant subsidiary legislation in the proposed manner?

- Yes, for publicly offered OFCs.
- No, for privately offered OFCs.

Q3. Do you think the proposed scope of the code and guidelines could adequately cater for the OFC regime? If not, what other essential features should the codes and guidelines include?

Yes, agree.

Q4. Do you agree with the proposal that the SFC should be the primary regulator of OFCs?

Yes, agree.

Q5. Do you agree with the proposed role and functions of CR in the OFC regime?

Yes, agree.

- Q6. Do you agree with the proposed role of ORO and SFC in respect of proposed termination and winding up arrangements for OFCs?

Yes, agree.

- Q7. Do you think the proposed features comprise the essential features of an OFC? If not, what other essential features should an OFC possess?

Under the proposed regulations, all public or private OFCs need to be registered with the SFC. For public funds, we agree that the proposed features comprise the essential features of an OFC. However, private funds are currently not subject to any registration requirements – this new requirement may create barriers for entry for smaller private funds.

The proposed requirement that the investment and management functions of the OFC must be delegated to an investment manager with Type 9 license may reduce the appeal of OFCs to international fund companies that do not want to incorporate a Hong Kong licensed manager. A possible consideration would be for the day to day management and investment functions of the OFC to be delegated to an investment manager with a comparable license from other jurisdictions.

- Q8. Do you agree with the proposed features for the Board of Directors? Do you think the proposed structure of the Board and the proposed criteria of directors will be able to render adequate investor protection to those investing in OFCs? Or do you think the proposed structure is too onerous, and would hinder the development of OFCs in Hong Kong?

Yes, we agree with the proposed features for the Board of Directors and the proposed structure and criteria of directors will be able to provide adequate investor protection.

- Q9. Do you agree that the OFC board must delegate the day to day management and investment functions of the OFC to an investment manager who is licensed or registered with the SFC to carry out Type 9 (asset management activity) regulated activity?

See response under Q7.

- Q10. Do you think the proposal to require a custodian in the OFC structure could foster the protection of investors in an OFC? Do you consider the proposed requirements and duties for a custodian adequate to meet this objective?

We agree with the proposal for an independent custodian to foster the protection of investors in an OFC. However, we query the need for requiring the custodian to be incorporated in Hong Kong. In practice, most funds will appoint a global custodian and the global custodian appoints a local sub-custodian for the local market they invest in. Given different areas of expertise/support across global custodians as well as different support requirements from investment managers, it may be difficult for funds to appoint only custodians that are incorporated in Hong Kong. There is currently no similar requirement for custodians under the Code on Unit Trusts and Mutual Funds.

- Q11. Do you agree with the proposed arrangements in relation to the incorporation of OFC?

Yes, agree.

- Q12. Do you consider the proposed naming convention provides sufficient level of clarity to investors?

Yes.

Q13. Do you agree that the proposed Articles are adequate? What features should the Articles include?

Yes, we agree that the proposed Articles are adequate.

Q14. Do you consider the proposed investment scope and strategies could provide a competitive framework for OFCs in Hong Kong with sufficient safeguards for investor protection?

- Yes, for public OFCs.
- The proposed investment scope of an OFC for private funds does not provide a competitive framework for OFCs in Hong Kong. Private funds should be given flexibility to pursue their own investment strategies. They should be allowed to invest in any asset class and subject only to its own restrictions contained in their constitutional documents.

Q15. Do you agree with the proposed arrangements in relation to the offer of OFC shares?

Yes.

Q16. Do you agree with the proposed arrangements regarding corporate administration?

Yes, as not all corporate filings for companies should be applicable to OFCs.

Q17. Do you agree with the proposed arrangements in relation to fund operation? Are the proposed principles and arrangements adequate to cater for the practical operation for OFCs?

Yes.

Q18. Do you agree with the proposed arrangements in relation to protected cells?

Yes, we believe this will enhance the competitiveness of the Hong Kong asset management industry by protecting investors in sub-funds within an umbrella company in the event of a collapse.

Q19. Do you think the proposed termination procedures are adequate to provide an expedient way for terminating a solvent OFC?

Yes.

Q21. Do you consider the proposed powers are essential and proportionate?

Yes.

Q22. Do you think the existing profits tax exemption regimes for public funds authorized under section 104 of the SFO/bona fide widely held regulated funds and offshore funds are adequate to cater for OFCs?

Yes, the existing profits tax exemption for public funds is adequate to cater for OFCs. However, in order to qualify for the exemption, the central management of an OFC has to be located outside of Hong Kong. It is equally important that the government also consider tax incentives to encourage set up within Hong Kong to promote Hong Kong as a fund management centre.

However, for non-public investment entities, such as private companies managing its own investments, and family offices, we believe the lack of profits tax exemptions for privately offered OFCs is not consistent with the exemptions being proposed for the public OFCs.

- i) Please provide explanations on the "possible read-across implications", preferably with example cases. Our lack of thorough understanding on this issue may be the reason of our comments below.
- ii) It drives non-public investment entities to remain using offshore companies as preferred vehicles. This may be fine for any other region or country, but not for Hong Kong, which is clearly striving to become an asset management hub in the region.
- iii) Giving tax exemption to assets that are managed outside of HK, while not offering the same for private OFCs makes no sense at all, and works against the objectives of promoting asset management in Hong Kong. Effectively, we would be encouraging the main value-add of the asset management work to be located outside of Hong Kong. In that case, the OFC rules would make Hong Kong worse.
- iv) The objectives should be to encourage assets to be held in HK, traded in Hong Kong, managed in Hong Kong. Breaking any one of the links would be a failure to achieving the goal.
- v) Tax exemption should be considered in the context of the global investment environment. By levying taxes in Hong Kong, often no new tax revenue is gained, but instead assets are driven away. Similar, by giving tax exemption for asset management in HK, it is likely that no loss in tax revenue is resulted, but that more assets may be in custodies and kept in Hong Kong along with the asset manager.
- vi) In order to invite more asset management firms, especially new start-ups and local start-ups which can become the future asset management powerhouses, we need to make the system simple for the company management in order for the managers to focus their time on managing assets, instead of avoiding taxes.

Q23. Do you consider that the proposed stamp duty treatment on sale and transfer of sales in OFCs can cater for the market needs?

We recommend a stamp duty waiver for OFCs similar to the recent stamp duty waiver proposed for Hong Kong ETFs where transfers of ETFs instruments are not stampable if the value of Hong Kong stocks does not exceed 40% of the aggregate value of underlying portfolio – this would be particularly relevant for regional or global funds set up as OFCs.

The HK SFA appreciates the opportunity to comment on consultation paper concerning open-ended fund companies. We trust you find our comments useful and constructive.

Yours sincerely,
For and on behalf of
The Hong Kong Society of Financial Analysts

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Chair, Advocacy Committee

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