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Hon Jasper Tsang Yok-sing
President
Legislative Council
Room 101
Legislative Council Complex
1 Legislative Council Road
Central, Hong Kong

For the attention of all members of the Legislative Council

By Hand

29 November 2011

Dear Mr Tsang

Securities and Futures (Professional Investor)(Amendment) Rules 2011

We are writing on behalf of the group of banks (the “**Banks**”) listed in the Appendix to this letter in connection with developments we understand to be taking place in relation to the Securities and Futures (Professional Investor) (Amendment) Rules 2011 (“**Rules**”). We would be grateful if you would ensure that this letter is distributed to all members of the Legislative Council.

We understand that a motion may be put forward for consideration by the Legislative Council at the meeting to be held on 30 November 2011 for a proposal to amend the Rules. We understand that the proposal is to incorporate into the Rules some aspects of the professional investor requirements contained in the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission (“**Code**”) which require a qualitative assessment of an investor’s knowledge and expertise.

We have discussed this with the Banks who wish to express the very serious concerns about this development. The proposal, if implemented, would have disastrous implications for the private placement market in Hong Kong. The “professional investor” exemption is the most important private placement exemption from the securities offering restrictions in Hong Kong. Its significance has increased following the recent reforms to the offering restrictions which, as you will be aware, have had the effect of bringing all offerings of structured products under the Securities and Futures Ordinance. As a consequence of this, the professional investor exemption is now the only viable exemption for many product offerings and it is widely relied upon by market participants.

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Incorporating the Code requirements into the Rules would make the professional investor exemption extremely difficult to rely upon. The Code requirements are very stringent (e.g. the requirement that an investor has carried out 40 transactions per annum) and have been made even more so following the recent reforms to the Code (in particular, by requiring an investor's knowledge, expertise and investment experience to be assessed separately for each relevant product type and market for which the investor is characterised as a professional investor under the Code). For that reason, the professional investor classification under the Code is not widely relied upon by the industry. Most private banks for instance do not classify their clients as Code of Conduct professional investors and very few of their clients would actually satisfy the Code requirements. If the proposal were implemented, it is therefore likely that market participants would no longer be able to rely on the professional investor exemption to make private placements, thereby closing an important segment of the market.

This would have a number of highly undesirable consequences. It would for instance significantly restrict investor freedom of choice as the range of products available to the market would shrink significantly. Additionally, it would make Hong Kong uncompetitive relative to other markets all of which have a viable private placement exemption.

Furthermore, the change would not in result in any significant increase in investor protection. The key safeguards to protecting investors are the obligations on financial institutions to know their customers and to assess the suitability of an investment product for the customer on a transaction-by-transaction basis. It is critical to note that these obligations apply even when products are offered to professional investors in reliance on the private placement exemption unless the investor is also assessed as having substantial knowledge and experience in the relevant product, in accordance with the professional investor requirements set out in the Code. Only then may know your customer and suitability obligations be waived by an intermediary if the client consents to this on a fully informed basis. In other words, classification of an investor as a professional investor under the Rules only opens the gateway to offering of products on a private placement basis – it does not however deprive the investor of all of the investor protection safeguards in the Code including the requirement to ensure that the product is suitable for the investor and that the investor fully understands the risks associated with the product.

In light of the above, the Banks strongly urge the Legislative Council not to adopt this proposal, the costs of which in their view significantly outweigh the benefits. If the Legislative Council is nevertheless minded to consider the proposal, **then the Banks think it is of critical importance that the Government conducts a full market consultation to enable the industry to express their views.** This is of course the usual practice in relation to the making of rules by the Securities and Futures Commission ("**Commission**"). As you will be aware, the Commission is required to consult the market on proposed rules under section 398 of the Securities and Futures Ordinance. Any departure from this practice would in our view be very unfair to the industry which would be deprived of the opportunity to make representations in the usual way.

Please do keep us informed of any developments. Representatives from the Banks would be very happy to meet with members of the Legislative Council to elaborate on the issues if the Legislative Council considers that this may be helpful.

Yours sincerely



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Appendix

List of Banks on whose behalf this letter is written

Citigroup Global Markets Asia Limited
Deutsche Bank AG
Goldman Sachs (Asia) LLC
Hong Kong and Shanghai Banking Corporation Limited
Morgan Stanley Asia Limited
Nomura International (Hong Kong) Limited
UBS AG