

Public Consultation on Open-ended Fund Companies

Legislative Council
Panel on Financial Affairs
7 April 2014

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Hong Kong's Strengths in Developing Asset Management

Robust economic growth and wealth
creation in Asia

+

Increase in portfolio allocation into
Asian markets

+

Financial market liberalization in the
Mainland

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Continued Growth of Hong Kong's Fund Industry

As at 31 March 2013

- SFC-authorized unit trust and mutual funds: 1 847
- Total asset under management : USD 1,238 billion

As at 31 December 2013

- Total Number of Hong Kong-domiciled SFC-authorized funds
 - 343 (an increase of 61% from 2011-2013)
- Proportion of HK-domiciled SFC-authorized funds as a % of total SFC-authorized unit trust and mutual funds
 - 19% (an increase of 7.5% from 2011-2013)

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Policy Objectives

- Strengthen Hong Kong's position as a premier international asset management centre
- Attract more funds to base in Hong Kong to broaden the variety and scope of our fund business
- Expand the distribution network for Hong Kong's funds industry
- Promote product origination of funds
- Increase opportunities for fund administration and servicing work

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What is an OFC

- An **open-ended collective investment scheme** –
 - in corporate form
 - with limited liability
 - with variable share capital
- To serve as an **investment fund** and manage investments for the benefit of its shareholders
- An **additional legal structure** to complement the existing unit trust structure

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What is an OFC

- May be set up as a **public** or **private fund**
- OFC shareholders -
 - do not have day-to-day management rights or control over the underlying assets
 - have the right to participate in the income/profits arising from the management of and transactions in the fund property (via distributions)
- OFC shares are typically priced at net asset value

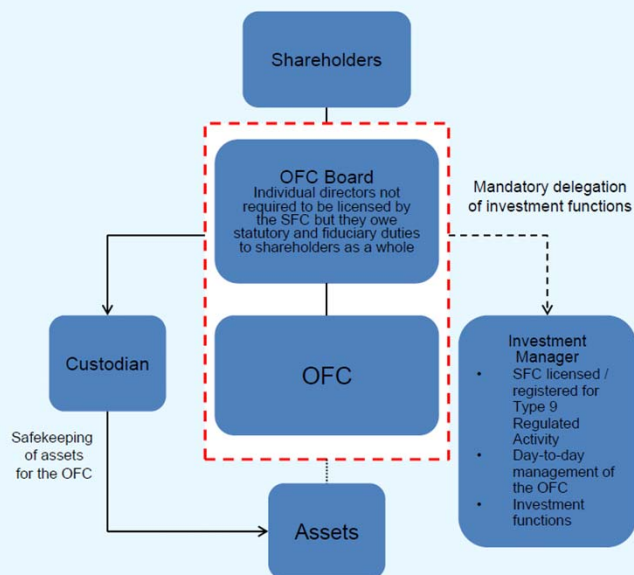
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Key Benefits of OFCs

- Variable share capital to meet shareholder application/redemption requests
- Corporate form with legal personality
- Shareholder liability will be limited to their shares in the OFC
- Streamlined procedures for termination
- Familiar structure to other fund jurisdictions, particularly those not familiar with trust law

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Proposed OFC Structure



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Investment Scope

- **Align with investment activities subject to licensing and regulation by SFC under the SFO** i.e. securities, futures (and over-the-counter derivatives)

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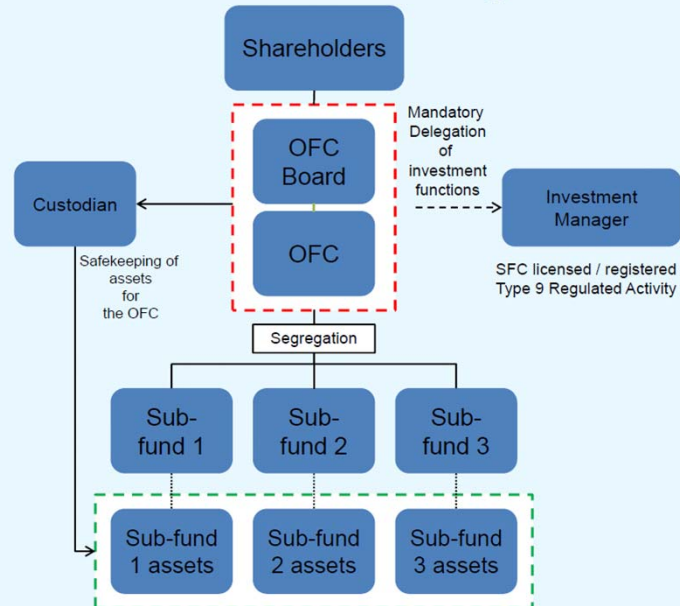
Fund Operation

OFCs will have more **flexibility** –

- to **vary its share capital** to meet shareholder redemption requests
- **may distribute out of share capital**, subject to solvency and disclosure requirements

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Protected Cell Regime



Legislative Framework

- Given that the OFCs are set up to function as an investment fund vehicle, it is proposed –
 - the **Securities and Futures Commission (SFC)** be the **primary regulator** for registration and regulation of OFCs under the **Securities and Futures Ordinance (SFO)**

Legislative Framework

- The **amended SFO** and the new **OFC subsidiary legislation**
 - the full scheme of OFC (creation and regulation of OFCs)
- **OFC Code** under the SFO
 - more detailed requirements and operation

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Registration & Authorization

- Setting up of OFCs
 - SFC would review applications and issue registration approval
 - Companies Registry would incorporate and register OFCs, and undertake statutory corporate filings functions
- Subject to post-registration monitoring and supervision. Publicly offered OFCs subject to all existing ongoing post-authorisation requirements under the SFC Handbook.

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Termination & Winding Up

- Termination of solvent OFCs
 - Streamlined procedures to facilitate termination of OFCs for commercial reasons
- Winding up of OFCs
 - In accordance with the requirements and procedures in the Companies (Winding up and Miscellaneous Provisions) Ordinance

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Key Investor Protection Measures

- Mandatory delegation of day-to-day management and investment functions to investment managers, subject to oversight by the OFC board
- Basic eligibility criteria applicable to the OFC board, investment manager and custodian
- Assets of OFCs to be entrusted to a separate, independent custodian for safekeeping
- Alignment of investment scope with those types of investment activities which are subject to licensing and regulation by the SFC under the SFO
- Properly overseeing OFCs and their activities
- Publicly offered OFCs required to seek SFC-authorization would also have to comply with the applicable requirements under the SFC Handbook, including disclosure requirements.

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Regulators

SFC

- Responsible for registration approval and regulation
- To approve appointment and replacement of key operators (e.g. custodian)
- To license/register investment managers
- Vested with enforcement powers

Companies Registry

- responsible for incorporation of OFCs and administering the relevant statutory corporate filings for public access

Official Receiver's Office

- responsible for administering compulsory winding-up procedures

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Tax Regime for OFCs

Publicly offered OFCs

- To be **exempted** from profits tax (same as for public funds)

Privately offered OFCs with central management and control (CMC) located outside Hong Kong

- To be **exempted** from profits tax under the existing regime for offshore funds

Privately offered OFCs with CMC located onshore

- We will consider carefully the exemption or the extent of exemption having regard to possible read-across implications

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Way Forward

- Three-month public consultation until **19 June 2014**
- FSTB, SFC and relevant departments will work on the details of the proposed OFC regime having regard to the comments received

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Thank You

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