

Securities and Futures (Amendment) Bill 2016

Open-ended Fund Companies

23 February 2016



Continued Growth of Hong Kong's Fund Industry

As at 31 December 2015

- SFC-authorized unit trusts and mutual funds: 2 110
- Hong Kong-domiciled SFC-authorized funds: 636 (an increase of 47 % from December 2012)
- Proportion of Hong Kong-domiciled funds as percentage of total number of SFC-authorized unit trust and mutual funds: increase by 8% over the past 3 years (from 22% in December 2012 to 30% in December 2015)

As at December 2014

- Total Net Asset Value: US\$1,322 billion (an increase of 27% from December 2011)



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



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



What is an OFC

- Could be a **publicly offered** or **privately offered 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



Key Benefits of OFCs

- Corporate form with legal personality
- Variable share capital to meet shareholder redemption requests
- 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

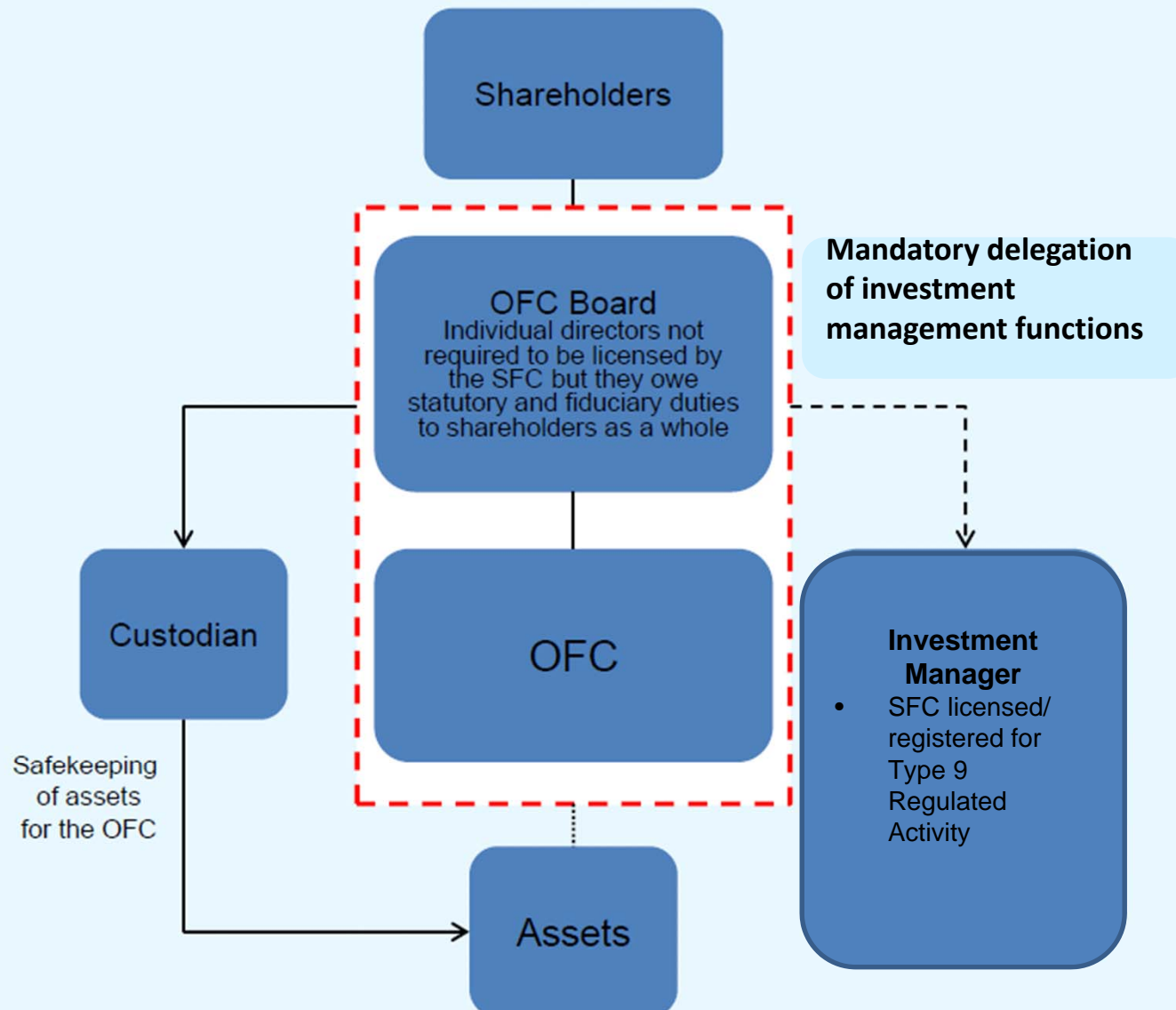


Key Benefits of OFCs

- More flexibility than conventional companies -
 - OFCs will not be bound by restrictions on the reduction of share capital, but will have the flexibility to **vary its share capital** in order to meet shareholder redemption requests
 - OFCs will not be bound by restrictions on the distribution out of share capital **but may distribute out of share capital**, subject to solvency and disclosure requirements
 - certain corporate filings requirements may not be applicable to OFCs or may be simplified in view of the nature of OFCs as investment funds



Proposed OFC Structure



Investment Scope

- Publicly offered OFCs - investing in asset classes in accordance with the SFC product code requirements and authorization conditions. On par with the existing regime for publicly offered SFC-authorized funds.
- Privately offered OFCs - the investment scope should still align with Type 9 (asset management) regulated activity, with a 10% de-minimis exemption for other asset classes. Cash deposits and currencies would be permissible asset classes not subject to the 10% de minimis limit.



Key Operators

- **Directors, Custodian and Investment Manager**
 - **Board of directors:** at least 2 natural-person directors; not required to be licensed with the SFC
 - **Custodian:** OFCs may appoint an overseas custodian provided that (a) it meets eligibility requirements generally referable to those under the SFC Handbook and (b) it has a place of business or a process agent in HK to accept service.
 - **Investment Manager:** The investment management functions of an OFC should be delegated to an investment manager licensed or registered with the SFC to carry out Type 9 (asset management) regulated activity.



Legislative Framework

- Given that the OFCs are set up to function as an investment fund vehicle, it is proposed that –
 - the **Securities and Futures Commission (SFC)** be the **primary regulator** under the **Securities and Futures Ordinance (SFO)**
 - the SFC be empowered to make subsidiary legislation (OFC rules) to provide for detailed registration, incorporation requirements, etc, and publish codes and guidelines (OFC Code) to provide guidance
- The enabling provisions are set out in the Bill; detailed operational and procedural matters in OFC rules and OFC Code

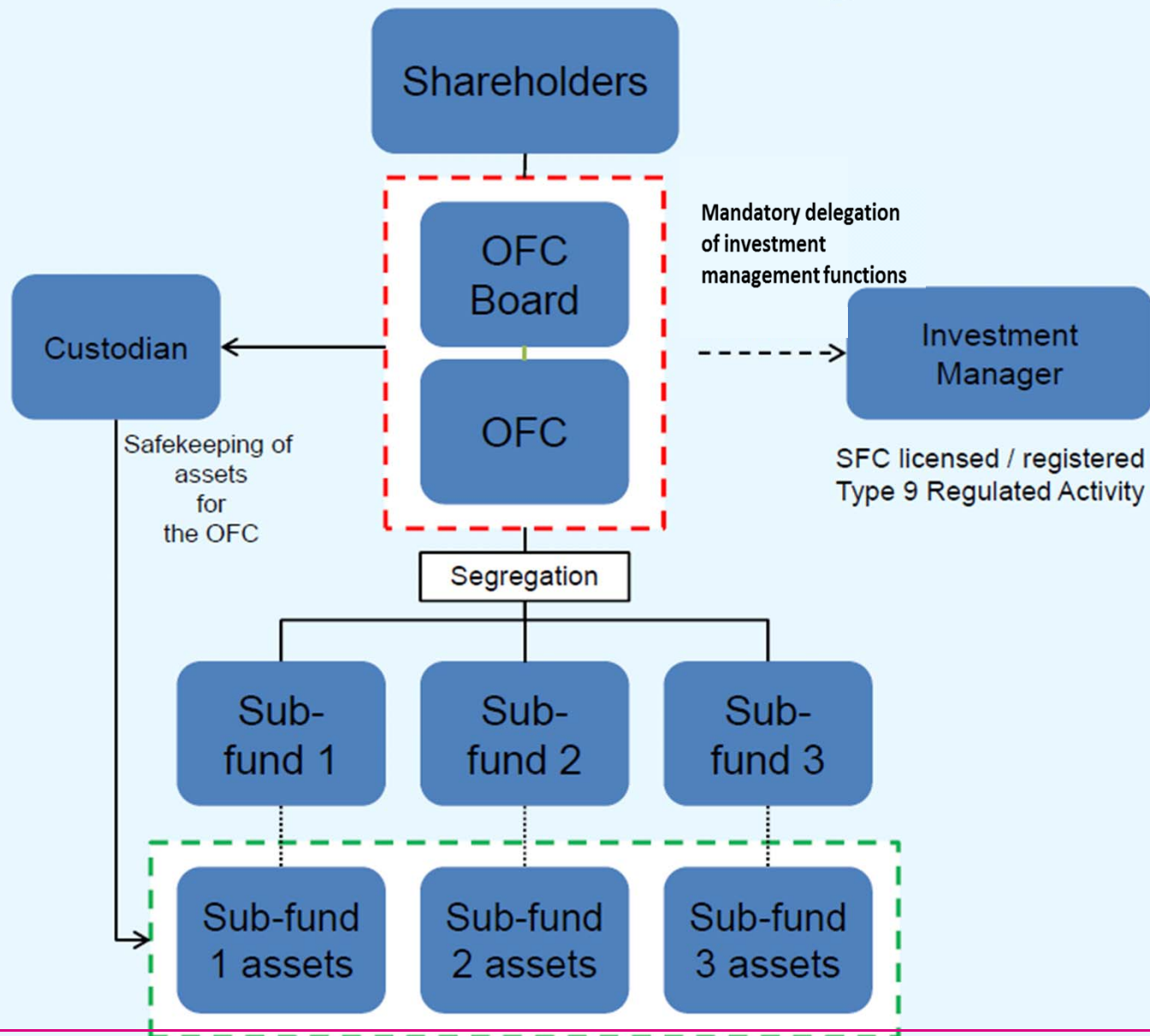
Legislative framework

Incorporation and registration of an OFC

- Setting up of OFCs
 - SFC will review applications and issue notice of registration to the Registrar of Companies (CR) once it is satisfied that the registration requirements are met
 - CR will incorporate OFCs and administer statutory corporate filings
 - CR will also issue first business registration certificate on behalf of the Commissioner of Inland Revenue simultaneously together with the certificate of incorporation
- Basic registration requirements and requirements relating to directors, investment manager and custodian are specified in the Bill



Protected Cell Regime



Legislative framework

Termination and winding up

- Termination of solvent OFCs
 - Streamlined procedures to facilitate termination of OFCs for commercial reasons
 - OFCs may apply to SFC for cancellation of registration voluntarily

- Winding up of OFCs
 - In accordance with the requirements and procedures in the Companies (Winding up and Miscellaneous Provisions) Ordinance, to be incorporated into the OFC rules with appropriate modifications



Key Investor Protection Measures

- Mandatory delegation of investment management 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
- 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.



Way Forward

- Upon the passage of the primary legislation, to formulate the subsidiary legislation and OFC Code, with a view to implementing the OFC regime as soon as practicable



Thank You

