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14 March 2016 By Post & Email: ofc@fstb.gov.hk

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

Dear Sirs

The Securities and Futures (Amendment) Bill 2016 (the "Bill")

We thank you for the opportunity to provide comments on the above Bill published by the Financial Services and the Treasury Bureau ("FSTB") in January 2016.

The Hong Kong Association of Banks ("HKAB") believes that the Bill captures most of the essential elements of an open-ended fund company ("OFC") and acknowledges the need for different treatment towards private and public OFCs.

Whilst the consultation conclusions issued by the FSTB in January 2016 clarified several enquires in our comments provided in December 2015, we are of the view that further distinction should be drawn between the regulatory framework of private and public OFCs, particularly in their formation, termination and corporate administration. Insofar as public funds are concerned, HKAB reiterates that the rules should be consistent with existing requirements under the Code on Unit Trusts and Mutual Funds.

We enclose members' views in the appendix for your consideration. We look forward to receiving further details in the subsidiary legislation and the relevant OFC Code.

For any enquiries, please contact our Manager Ms. Florence Ng at 2537 3220.

Yours faithfully

Doris Ma
Secretary

Enc.

Financial Services and the Treasury Bureau

The Securities and Futures (Amendment) Bill 2016

Submission of The Hong Kong Association of Banks

14 March 2016

Introduction

Further to the submission of The Hong Kong Association of Banks ("**HKAB**") provided in December 2015, this paper sets out HKAB's views in relation to the legislative proposals for open-ended fund companies ("**OFCs**"), as put forward in the Securities and Futures (Amendment) Bill 2016 (the "**Bill**") issued by the Financial Services and the Treasury Bureau ("**FSTB**") in January 2016. We have also had regard to the consultation conclusions ("**Consultation Conclusions**") and the Legislative Council Brief issued by the FSTB in January 2016 (the "**Legislative Council Brief**").

Assisted by King & Wood Mallesons, this submission sets out HKAB's response to the legislative proposal. We continue to await for further details in the subsidiary legislation and the relevant "OFC Code".

We look forward to an ongoing dialogue with the FSTB in relation to the proposed OFC regime.

Terms that are defined in the Bill have the same meaning when used in our response.

HKAB's Comments

1. Overarching principles for OFCs

HKAB continues to support the overarching principles for OFCs and reiterates that they will allow greater flexibility in the choice of legal fund structure and ensure that OFCs and their key operators will comply with proper governance and conduct requirement in order to protect the interests of shareholders and build confidence of investors.

We welcome that the Bill continues to capture most of the essential elements of an OFC and acknowledge the need for different treatment towards private and public OFCs. Whilst the Consultation Conclusions clarified several enquires in our comments provided in December 2015, HKAB is of the view that further distinction should be drawn between the regulatory framework of private and public OFCs, particularly in their formation, termination and corporate administration.

Insofar as public funds are concerned, HKAB reiterates that the rules should be consistent with existing requirements under the Code on Unit Trusts and Mutual Funds ("**UT Code**").

2. Regulatory oversight

Distinction between public and private OFCs

HKAB reiterates that the Bill does not draw clear distinction between private and public OFCs in the regulatory framework. We recognise that the Consultation Conclusions indicate that the OFC Rules and OFC Code will be made subject to further public consultation. We look forward to providing our comments as part of this consultation.

To the extent that private OFCs may be subject to registration requirements and other requirements under the OFC Code, this would create disparity with private funds taking other forms, such as private or non-authorised unit trusts domiciled in Hong Kong, and collective investment schemes domiciled in other jurisdictions. Consequently, this could undermine the attractiveness of the proposed OFC regime and hamper its growth.

We continue to anticipate that the overall regulation of public OFCs under the subsidiary legislation, OFC Code and the UT Code should be consistent with the regulation over existing public unit trusts or mutual funds domiciled in other jurisdictions but authorised for sale in Hong Kong under the existing UT Code.

Termination process

Under the Bill, streamlined termination remains subject to prior approval of the SFC. HKAB reiterates that the termination of private OFCs can be administered in a more cost effective and expedient manner by way of notification or filing to the SFC and CR instead. Since the Bill does not specify the detailed process of termination, we continue to anticipate that they will be included in subsidiary legislation and the OFC Code and look forward to being part of the consultation in respect of these.

3. Legal structure

Director criteria

HKAB welcomes the removal of the requirement for at least one Hong Kong-resident OFC director. However, the Bill does not specify the eligibility criteria for directors. As the board of directors would bear fiduciary duties for the OFCs under the legislative the Bill, we anticipate that the OFC Code or subsidiary legislation will include a clear and succinct description of the eligibility criteria.

Licensing of investment manager

As set out in previous responses, HKAB maintains that the licensing requirement for public OFCs should be aligned with paragraph 5.6 of the UT Code. This provides that whether the investment manager is required to be licensed by or registered with the SFC should depend on the functions which are actually performed by the investment manager in Hong Kong as opposed to being mandatory.

We reiterate that such mandatory licensing requirement would create disparity with private funds taking other forms, such as private or non-authorised unit trust domiciled in Hong Kong, and collective investment schemes domiciled in other jurisdictions.

Therefore, we respectfully request that the requirement that an investment manager of an OFC must be licensed or registered for Type 9 regulated activity is removed from the Bill.

Sub-custodians

HKAB welcomes the clarification in the Consultation Conclusions that the OFC board is permitted to appoint different investment managers and/or custodians for each sub-fund on a case-by-case basis. We anticipate that these details will be reflected in subsidiary legislation and the OFC Code.

For private OFCs, we welcome the confirmation in the Consultation Conclusions that brokers or prime brokers can act as custodians on a case-by-case basis as long as they fulfil the eligibility requirements and that the SFC may consider appointing multiple custodians on a case-by-case basis. We anticipate that the OFC Code or subsidiary legislation will expressly reflect these details to align with business practices of private OFCs and provide certainty that such appointment can be made.

Further, HKAB repeats our suggestion that the regime should provide for scenarios where custodians may disclaim liabilities for investment instruments that cannot be safekept by them, such as bilateral private deals, non-listed derivatives, non-tradable instruments and so forth.

4. Formation & Incorporation

Application process

HKAB anticipates that further details of the application process will be provided in subsidiary legislation and the OFC Code. HKAB repeats our comments provided in December 2015 that there should be an indicative timeframe for approval and registration of investment vehicles and suggests that the SFC should not require the production of documentary evidence for review and vetting for certain eligibility criteria in order to save time and cost.

Incorporation requirements and governance

The Consultation Conclusions clarify that for public OFCs, changes in the provisions of the instrument of incorporation should observe applicable requirements under the UT Code. For private OFCs, immaterial changes to non-core provisions in the instrument of incorporation will not require shareholders' approval. HKAB welcomes the relaxation in approval requirement for private OFCs. We anticipate that the OFC Code or subsidiary legislation will expressly reflect the distinction between public and private OFCs.

Investment scope and strategies

The Consultation Conclusions provide that publicly offered OFCs may invest in assets classes in accordance with the SFC's product code requirements and authorisation conditions, that is, mainly in securities, futures and OTC derivatives. For privately offered OFCs, the Consultation Conclusions state that the investment scope should align with Type 9 (asset management) regulated activity, with a 10% de minimis exemption for other asset classes).

The Consultation Conclusions note that private OFC investment managers are not subject to restrictions in the SFC Handbook on Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Products and may have the flexibility to pursue their own investment strategies provided that basic governance principles are complied with.

Whilst HKAB welcomes the different treatment for public and private OFCs, we repeat our previous comments that, given private OFCs are generally designed for professional investors, the licensing regime under the SFO should not be a contributing factor to defining the investment scope for private OFCs. The 10% de minimis limit would restrict investment in other asset classes such as commodities and real property.

5. Administration and Operation

HKAB welcomes the clarification in the Consultation Conclusions that the Hong Kong Financial Reporting Standards ("**HKFRS**") and the International Financial Reporting Standards ("**IFRS**") may be accepted for the purpose of preparing accounts. Further, HKAB agrees that the requirement of 10% voting rights held for requisitioning an EGM is consistent with existing practice of unit trusts and should be adopted for OFCs.

HKAB anticipates that these details will be reflected in subsidiary legislation and the OFC Code.

6. Termination and Winding Up

HKAB welcomes the clarification in the Consultation Conclusions that the SFC and the custodian are entitled to petition for winding up. We anticipate that the details will be provided in the subsidiary legislation and the OFC Code.

7. Tax and Other Issues

HKAB welcomes clarification in the Consultation Conclusions that OFCs will be exempt from profits tax. However, it remains unclear whether there is segregated tax liability. We respectfully request confirmation that in cases where one of the sub-funds of an offshore OFC does not comply with the requirements for offshore fund tax exemption, for example due to conducting transaction that is not "specified transaction", the non-eligibility to the tax exemption should only be restricted to that particular sub-fund and not taint the eligibility of other sub-funds of the offshore OFC so long as they comply with the relevant requirements.

HKAC welcomes the clarification in the Consultation Conclusions that unit trusts chargeable to profits tax need to file tax returns each year but that the Inland Revenue Department may not require the OFC to complete tax return if it is exempt from profits tax or is in a loss position. We anticipate such clarification to be reflected in subsidiary legislation and the OFC Code.

HKAB and its members look forward to working with the FSTB and the SFC in relation to the finalisation of the proposed OFCs regulatory framework – HKAB is keen to be closely involved in consultations in respect of subsidiary legislation and the OFC Code.

Please contact us if you have any queries in relation to the comments raised in this response. Equally, we would also welcome ongoing updates about the progress of implementation in Hong Kong, including timing.