Subcommittee on Three Pieces of Subsidiary Legislation Related to the Open-ended Fund Company Regime and Gazetted on 18 May 2018

Response to follow-up actions arising from the discussion at the meeting on 12 June 2018

This paper sets out the responses of the Government and the Securities and Futures Commission ("SFC") to the issues raised by Members in relation to the open-ended fund company ("OFC") regime at the meeting of the Subcommittee on 12 June 2018.

Registration of privately offered OFCs

2. Private investment funds may be set up in different forms, including limited partnership, unit trust or corporate form. Without any legislative amendments, if an investment fund opts to be established in corporate form in Hong Kong, it can only be set up under the Companies Ordinance (Cap. 622) ("CO") and be subject to various restrictions which are in practice unviable for investment funds. These include, for example, the CO's constraints on capital reduction and distributions out of capital, which would restrict an investment fund from conducting redemptions and making pay-outs in line with common fund industry practices.

3. In view of these constraints under the CO and having considered the regulatory framework in other major overseas fund jurisdictions (such as the UK, Ireland and Luxembourg) whereby the securities regulator primarily oversees the establishment of such corporate investment fund vehicles, it was decided that the framework for the new OFC structure in Hong Kong would be housed under the Securities and Futures Ordinance (Cap. 571) ("SFO").

4. Following a public consultation exercise in 2014, the Securities and Futures (Amendment) Bill 2016 was introduced and passed in 2016 to enable the registration and regulation of all OFCs (both publicly and privately offered) by the SFC under the new Part IVA of the SFO.

5. In formulating the legal framework for OFCs, the OFC's "limited company" nature had to be accounted for. Accordingly, relevant elements from the CO and the conventional company winding-up regime that are applicable to the OFC are replicated in the SFO and the Securities and Futures (Open-ended Fund Companies) Rules ("the OFC Rules").

These include, for example, CO provisions on company capacity, share capital and share transfer, incorporation and filings with the Company Registry ("CR"), directors' duties, requirements as to meetings, resolutions, register maintenance, financial statements and auditors.

6. These requirements for an OFC dovetail the CO requirements and are no more onerous than those applicable to a conventional limited company incorporated under the CO. Such requirements are in fact simplified where applicable. For example, no filings with CR on share allotments and redemptions are required.

7. The other provisions in the OFC legal and regulatory regime mainly revolves around the necessary key operators of an OFC due to its investment fund nature. These include, for example, requirements concerning (a) a custodian to whom the OFC's assets are to be segregated and entrusted and (b) an investment manager licensed or registered with the SFC for Type 9 (asset management) regulated activity.

8. The imposition of basic requirements on a corporate investment fund is consistent with the practices in other major overseas fund jurisdictions. These basic requirements are also necessary to ensure Hong Kong's regime under the SFO is compliant with the fundamental principles laid down by the International Organisation of Securities Commissions.

9. As noted in the 2014 and 2017 public consultations, it has always been the intention when devising the regime to allow privately offered OFCs the flexibility to pursue their own investment strategies as set out in their instrument of incorporation and offering documents, as long as they meet the basic requirements imposed. Accordingly, privately offered OFCs are subject to much more streamlined requirements than publicly offered OFCs. For example, unlike publicly offered OFCs, the SFC's prior approval will not be required for (a) the offering documents, (b) the instrument of incorporation, and (c) the scheme changes of privately offered OFCs.

10. Following the commencement of the OFC regime, the SFC will continue to keep in view the OFC's legal and regulatory requirements having regard to international developments, including overseas regulatory practices concerning private corporate investment funds.

Common law privilege against self-incrimination

11. Rule 46 of the OFC Rules provides that the Registrar of Companies ("the Registrar") may enquire into whether a person has knowingly or recklessly made a false, misleading or deceptive statement in a document delivered to the Registrar, i.e. the offence under rule 195(1). Rule 48 provides for the offences for failing to comply with the requirements made by the Registrar under rule 46. Rule 49 provides for the limitation on the use of incriminating evidence obtained under rule 46 in criminal proceedings.

12. Under rule 46, the Registrar can exercise power to enquire with a person other than the subject person of an enquiry to provide the necessary record, document, information or explanation. The information or explanation so provided is not admissible in evidence against the person in criminal proceedings relating to an offence for false statement under rule 195(1). However, it is admissible in evidence against the person in criminal proceedings in which the person is charged with an offence in respect of the information or explanation under (a) rule 48(4), (5) or (6), (b) Part V of the Crimes Ordinance (Cap. 200), or (c) for perjury.

Financial Services and the Treasury Bureau
Securities and Futures Commission
Companies Registry
19 June 2018