

**CODE ON INVESTMENT-LINKED ASSURANCE
SCHEMES**

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Explanatory Notes:

- (a) This Code establishes guidelines which will be applied by the Securities and Futures Commission for the authorization of investment-linked assurance schemes, pursuant to s.4(2)(g) of the Protection of Investors Ordinance (PIO).**
- (b) The Commission may review its authorization at any time and may modify, add to or withdraw such authorization, as it deems fit.**
- (c) The issue of an advertisement or invitation to the public in Hong Kong to invest in an unauthorized investment-linked assurance scheme may amount to an offence under s.4 of the PIO.**
- (d) This Code does not have the force of law.**

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PART I: GENERAL MATTERS

Chapter 1: Authorization Procedures

General

- 1.1 Investment-linked assurance schemes are expected to comply with the provisions of this Code in order to be authorized in Hong Kong.
- 1.2 Applications for authorization which seek waivers of any of these provisions must give detailed reasons why waivers are sought.

Documents to be supplied to the Commission

- 1.3 An applicant for authorization of a scheme should lodge with the Commission:
 - (a) The scheme's principal brochure and constitutive documents;
 - (b) Copies of any material contracts;
 - (c) All other sales literature, proposed advertisements and printed material intended to be issued in Hong Kong to prospective scheme participants;
 - (d) A checklist of compliance with the Code (see Appendix D);
 - (e) The latest audited report and corporate information in respect of the applicant company and other relevant parties, where applicable; and
 - (f) The application fee in the form of a cheque payable to the "Securities & Futures Commission". The current fee schedule is available on request from the Commission.

Chapter 2: Administrative Arrangements

- 2.1 The Commission has delegated to the Committee on Investment-Linked Assurance and Pooled Retirement Funds, to an Executive Director and to the Director (Investment Products), its power to authorize investment-linked assurance schemes and pooled retirement funds. Powers are normally exercised by the Committee when new management groups or new policy issues are considered; otherwise powers are normally exercised by the Director (Investment Products).
- 2.2 The Commission has established the Committee on Investment-Linked Assurance and Pooled Retirement Funds (ILAC) under s. 6(1) of the Securities and Futures Commission Ordinance (SFC Ordinance) for the purposes of:
- (a) assisting the Commission in the performance of its functions to ensure the effective regulation of the marketing of investment-linked assurance schemes and pooled retirement funds;
 - (b) authorizing investment-linked assurance schemes and pooled retirement funds pursuant to s. 4(2)(g) of the PIO;
 - (c) imposing conditions on the authorization of investment-linked assurance schemes and pooled retirement funds pursuant to s. 4(7) of the PIO;
 - (d) granting waivers from this Code; and
 - (e) considering whether there should be any amendments to the legislation relating to investment-linked assurance schemes and pooled retirement funds and to this Code and making recommendations to the Commission accordingly.

Constitution of Committee

- 2.3 The constitution of ILAC is:

Chairman

- (a) Any Executive Director of the SFC;

Members (11)

- (b) Non-executive Director of the SFC;
- (c) Director (Investment Products) of the Commission (ex-officio and deputises as Chairman in the absence of the Chairman);
- (d) Representative of the Commissioner of Insurance;
- (e) Representative of the Mandatory Provident Fund Schemes Authority;
- (f) Chairman of the Life Insurance Council (ex-officio);

- (g) Life assurance company member;
- (h) Retirement fund company member;
- (i) Person nominated by the Commission;
- (j) Actuary member;
- (k) Trustee member; and
- (l) Appointment (I) ad personam.

Alternate Members (4)

- (m) Alternate life assurance company member;
- (n) Alternate retirement fund company member;
- (o) Alternate actuary member; and
- (p) Alternate trustee member.

Quorum & Meetings

- 2.4 The quorum for any meeting of the Committee is four members, one of whom must be an Executive Director or Director of the Commission and one of whom must be employed by a life assurance or retirement fund company. ILAC has appointed a staff member of the SFC as Secretary. The Secretary attends ILAC's discussions but has no vote.
- 2.5 On request, the Commission will give reasons for decisions reached.
- 2.6 Under s.9(2)(a) of the SFC Ordinance, the Commission may concurrently perform any function, power or duty which it has delegated but the Commission does not intend to exercise this right by reviewing a decision of the Committee except where there has been:
 - (a) a manifest error;
 - (b) an application of defective procedures; or
 - (c) a manifest misinterpretation of this Code.

Procedure for Amendments to the Code

- 2.7 ILAC may make recommendations to the Commission whenever it considers that the provisions of this Code should be amended or extended. If the Commission accepts the Committee's recommendation, any such change or amendment will be made known to the industry and transitional periods for compliance will be allowed where necessary.

Data Privacy

- 2.8 The information requested under the Code may result in the applicant providing the Commission with personal data as defined in the Personal Data (Privacy) Ordinance. The

data supplied will only be used by the Commission to perform its functions, in the course of which it may match, compare, transfer or exchange personal data with data held or obtained by the Commission, government bodies, other regulatory authorities, corporations, organizations or individuals in Hong Kong or overseas for the purpose of verifying those data. Subject to the limits in s.59 and 59A of the SFC Ordinance, the Commission may disclose personal data to other regulatory bodies. You may be entitled under the Personal Data (Privacy) Ordinance to request access to or to request the correction of any data supplied to the Commission, in the manner and subject to the limitations prescribed. All enquiries should be directed to the Data Privacy Officer at the SFC.

Chapter 3: Interpretation

- 3.1 "applicant company" means the company which applies to the Commission, directly or through an authorized representative, to have its scheme authorized pursuant to this Code.
- 3.2 "broker managed fund" means an internal life or pension fund of an insurance company with an external fund manager, offered as an investment link to one or more of the company's insurance policies.
- 3.3 "Commission" or "SFC" means the Securities and Futures Commission established pursuant to the SFC Ordinance.
- 3.4 "connected person" in relation to a company means:
- (a) any person or company beneficially owning, directly or indirectly, 20% or more of the ordinary share capital of that company or able to exercise, directly or indirectly, 20% or more of the total votes in that company;
 - (b) any person or company controlled by a person who or which meets one or both of the descriptions given in (a);
 - (c) any member of the group of which that company forms part; or
 - (d) any director or officer of that company or of any of its connected persons as defined in (a), (b) or (c).
- 3.5 "constitutive documents" means the documents which establish and govern the existence and operation of a scheme and includes the policy document in the case of a scheme established pursuant to an insurance contract and the trust deed in the case of a scheme established under trust.
- 3.6 "insurance company" means a company authorized by the Insurance Authority under the Insurance Companies Ordinance to carry on a relevant class of insurance business in Hong Kong.
- 3.7 "investment-linked assurance scheme" means an insurance policy of the "linked long-term" class as defined in the Insurance Companies Ordinance, First Schedule, Part 2, other than a policy of which the predominant purpose is life assurance and not investment.
- 3.8 "investment-linked savings plan" means a unit-linked investment plan established under an investment contract where notional units linked to the performance of authorized funds or other financial instruments are issued to participants in return for their contributions.
- 3.9 "principal brochure" means that document, or documents issued together, issued by an applicant company, containing information on a scheme as stipulated in Appendix A.
- 3.10 "scheme participants" means the policy or contract owners and, upon the death of the

owner, the beneficiaries appointed by him/her under the scheme.

- 3.11 "substantial financial institution" means a licensed banking institution authorized under the Banking Ordinance, or financial institution with a minimum paid-up capital of HK\$150,000,000 or its equivalent in foreign currency.

PART II: AUTHORIZATION REQUIREMENTS

Chapter 4: Applicant Company

Regulatory Status of Applicant Company

- 4.1 No investment-linked assurance scheme will be authorized pursuant to this Code unless the applicant company is authorized under the Insurance Companies Ordinance to carry on the relevant class of insurance business in Hong Kong. If the applicant company ceases to be authorized by the Insurance Authority, any existing authorization of the scheme will normally lapse.

Responsibilities of Applicant Company

- 4.2 The applicant company will be responsible for observing all requirements of the Code and any conditions imposed by the Commission in granting authorization during the continued enjoyment of that authorization, except to the extent that the Commission grants waivers in writing.
- 4.3 The applicant company is responsible for whatever information is given to the Commission on its behalf and should use its best endeavors to ensure that statements of intention in printed matter are followed.
- 4.4 If a scheme contains a guaranteed investment option, such guarantee should be provided either by the applicant company or a substantial financial institution acceptable to the Commission.
- 4.5 The applicant company shall:
- (a) use its best endeavors to carry on and conduct its business in a proper and efficient manner and will ensure that any scheme to which the constitutive documents relate is conducted in a proper and efficient manner; and
 - (b) exercise best endeavours and due diligence to ensure that the marketing of the scheme is carried out professionally, honestly and fairly.

Chapter 5: Hong Kong Representative

Appointment of Representative

- 5.1 The applicant company will be required to appoint a representative in Hong Kong if it is not incorporated in and does not have a place of business in Hong Kong. The representative must be maintained throughout the period the scheme is authorized in Hong Kong.

Functions of a Representative

- 5.2 The representative is not required to take responsibility for the acts and omissions of the applicant company but must be empowered to:
- (a) act for the applicant company in all matters relating to the initial and continued authorization of the scheme, pursuant to the relevant legislation and this Code;
 - (b) accept service of any summons or writ on behalf of the applicant company;
 - (c) provide the Commission with such up-to-date principal brochure, constitutive documents or other documents relevant to the scheme as the Commission may from time to time request;
 - (d) receive notices from scheme participants in respect of the scheme;
 - (e) make available for public inspection in Hong Kong, free of charge, and offer for sale at a reasonable price to scheme participants, copies of all constitutive documents of the scheme;
 - (f) provide scheme participants with information on the scheme;
 - (g) represent the applicant company in relation to all matters in which any scheme participant in Hong Kong has a pecuniary interest; and
 - (h) exercise best endeavours and due diligence to ensure that the marketing of the scheme is carried out professionally, honestly and fairly.

Written Undertaking

- 5.3 The representative must provide the Commission with a written undertaking that it will perform the duties required of a representative under this Code.

Retirement or Dismissal of Representative

- 5.4 Should the representative retire or be dismissed, it must be replaced as soon as possible, by another representative whose appointment is subject to the approval of the Commission.

Hong Kong Representative Agreement

5.5 Details of all contracts between the representative and the applicant company must be supplied to the Commission. Any subsequent amendments of these contracts must be notified to the Commission.

Chapter 6: Operational Requirements

Scheme Documentation

Matters to be Disclosed in the Principal Brochure

- 6.1 An authorized scheme must issue an up-to-date principal brochure, which should contain the information necessary for prospective scheme participants to be able to make an informed judgment of the investment proposed to them, and in particular should contain the information listed in Appendix A.

English and Chinese Principal Brochure

- 6.2 Except as provided herein, the information required in Appendix A must be provided in the English and Chinese languages. The Commission may waive the requirement that the information be provided in both languages on a case-by-case basis where the applicant company satisfies the Commission that the scheme will only be offered to persons fully conversant in the language in which it is intended to publish the information.

Illustration Document

- 6.3 An illustration document must be prepared by the insurance company in conjunction with each proposed investment. Alternatively, the Commission may allow the provision of a standard illustration for each scheme, provided that the surrender values illustrated are for a contract with a term based on a maximum commission scale and a minimum premium requirement. This document must be provided to the scheme participant for his review and signature prior to signing of the application form.
- 6.4 The minimum requirements for the information to be included in the illustration document are set out below. Subject to the approval of the SFC, the insurance company may customize the document to include additional information provided that such additional information is not misleading and does not otherwise detract from the information disclosed in the minimum requirements.

(a) Surrender Values

The insurance company is required to illustrate, what the scheme participant would be expected to receive if he redeems at the end of each of the first 5 years of the contract, and for every fifth year thereafter until maturity, after deduction of all relevant charges. These expected surrender values should be based on 2 different assumptions on the rate of return, initially set at a low of not more than 5% and a high of not more than 11% p.a. respectively. [These rates may be subject to change by the Commission after consultation with the industry.]

(b) Prescribed Statements

The following statement should appear below the table of surrender values:

The rates of return shown here are for illustrative purposes and are not based on past performance. The actual return may be different.

The following statements should be clearly disclosed before the investor signature:

You should only invest in this product if you intend to pay the premium for the whole of your chosen premium payment term. Should you terminate this product early, you may suffer a loss as illustrated above.

I confirm having read and understood the information provided in this illustration and received the principal brochure.

A format for the illustration document is contained in Appendix B.

Application Form

- 6.5 The entitlement of the investor to the cooling-off period must be prominently displayed at the bottom of the application form immediately above the space for signature in these words:

”Cancellation Right and Refund of Premiums

I understand that I have the right to cancel and obtain a refund of any premium(s) paid less any market value adjustment, by giving written notice. Such notice must be signed by me and received directly by [name and address of insurance company Hong Kong registered office] within 21 days from the date of this application, or 14 days from the date of issue of the policy [or contract, as applicable] if later.”

- 6.6 No scheme application form may be provided to any member of the public unless it is accompanied by the principal brochure and the illustration document. To that end the application form should include a statement to the effect that it should only be issued in conjunction with the principal brochure and the illustration document.

Inclusion of Performance Data

- 6.7 If performance data or estimated yield is quoted, the Commission may require supporting documentation. No forecast or illustration of the scheme future performance may be made in authorized scheme documents except for the illustration of surrender values or where an investment return at a certain rate is guaranteed.

Naming of Unauthorized Unit Trusts

- 6.8 As a general principle any naming of unit trusts or mutual funds in authorized scheme documents should be restricted to those which are authorized by the Commission pursuant to section 15 of the Securities Ordinance.

Contents of Constitutive Documents

- 6.9 The constitutive documents of a scheme should contain the information listed in Appendix C.

- 6.10 Nothing in the constitutive documents may provide for the parties thereto to be exempted from any liability to scheme participants arising out of any breach of trust through fraud or culpable negligence or imposed on them under Hong Kong law or the law of the scheme's place of domicile, under any trust deed or under any contract entered into, nor to be indemnified against any such liability by scheme participants or at scheme participants' expense.

Cooling-off Period

- 6.11 A scheme must allow an investor to withdraw unconditionally within the cooling-off period, subject to a market value adjustment (MVA). This cooling-off period will extend to the later of 14 days after the date of issue of the new contract; or 21 days after the date on which the application for the new contract is signed.
- 6.12 Any such MVA must be calculated solely with reference to the loss the insurance company or contract issuer might make in realizing the value of any assets acquired through investment of the premiums made under the contract. It shall therefore not include any allowance for expenses or commissions in connection with the issuance of the contract.

Fees and Charges

- 6.13 Where a scheme proposes to invest in unit trusts, mutual funds or other pooled funds managed or distributed by the same company or group, all initial charges of the underlying funds must be waived but recurrent management fees and charges may be levied proportionate to the amount invested.
- 6.14 The level/basis of calculation of all costs and charges payable from the scheme property must be clearly stated, with percentages expressed on a per annum basis, where applicable. The aggregate level of fees for investment management or advisory functions should also be disclosed.
- 6.15 If a performance fee is levied, the fee can only be payable:
- (a) no more frequently than annually; and
 - (b) only if the net asset value per unit exceeds the net asset value per unit on which the performance fee was last calculated and paid (i.e. on a "high-on-high" basis).

In the case where a scheme or the fund(s) linked to the scheme is not unitized, a certificate from an actuary must be provided to the Commission on an annual basis to certify compliance with the foregoing except where:

- (a) there exists a year-on-year guarantee on investment return where the deficiency, if any, between the guaranteed return and the actual return is credited into the fund account not less frequently than annually; or
- (b) the scheme is a deposit administration policy in which investment returns may be declared by a company, in its discretion, at or above a stated minimum rate not less frequently than annually.

Chapter 7: Guaranteed Funds

The following criteria shall apply to a scheme which contains an investment fund in which a guaranteed amount will be paid to scheme participants at a specific date in the future.

Guarantor

- 7.1 If the guarantor is an entity other than the insurance company which issues the policy, it must be a substantial financial institution acceptable to the Commission.

Disclosure

- 7.2 The principal brochure of the scheme must contain:
- (a) the name of the guarantor (if other than the insurance company which issues the policy) and the terms of the guarantee;
 - (b) where applicable, a warning statement in relation to all material conditions which affect the scope or validity of the guarantee including, where relevant, the condition that the guarantee only applies to scheme participants who hold their investment until the date specified in the guarantee and that termination or withdrawal before such date are fully exposed to fluctuations in the value of the fund assets and/or subject to penalties; and
 - (c) an illustration or description to clearly demonstrate the guarantee mechanism.

Guaranteed Funds with Discretionary Benefits

- 7.3 In relation to an insurance arrangement, if it is stated that discretionary benefits will or may be paid to scheme participants in excess of the guaranteed amount, and the amounts of those benefits are determined at the discretion of the policy issuer, the principal brochure of the scheme must contain:
- (a) a statement to the effect that the [name of policy issuer], at its sole discretion, has the right to retain investment income of the [name of investment fund] in excess of that required to be set aside to meet the guaranteed benefits under the [name of investment fund];
 - (b) a readily comprehensible description of the methods of determining the discretionary benefits, including the following information, to the extent applicable:
 - (I) the reporting date; and
 - (II) **(i) for a participating product where the policy holder has a right to participate in profits from the long term fund of the policy issuer or any part of that fund :**
 - (i) details of the fund or part fund to which the right relates,

- (ii) the principles on which the distribution of profits among policy holders and shareholders is based and whether these principles are derived from the constitution of the policy issuer or otherwise,
 - (iii) the bonus rates declared immediately prior to the reporting date and for the four years previous, *and*
 - (iv) the proportion of total distributed profits that was distributed to shareholders immediately prior to the reporting date and for the four years previous;
- (ii) for an investment-linked product :**
- (i) a description of the method which will be used to calculate unit prices from time to time, *and*
 - (ii) the percentage changes in unit prices for the five yearly intervals immediately preceding the reporting date;
- (iii) for an investment account product -**
- (i) a description of the method which will be used to calculate the interest rate for each period, *and*
 - (ii) the rate of interest declared immediately prior to the reporting date and for the four years previous; and
- (c) a statement that past performance should not be taken as an indication of future performance.

Note: For investment funds with less than five years experience, figures for shorter periods may be shown, provided the date of commencement is shown.

Chapter 8: Broker Managed Funds

General

- 8.1 A Broker Managed Fund (BMF) is generally an internal life or pension fund of an insurance company with an external fund manager, offered as an investment link to one or more of the company's insurance policies. The BMF's investment or asset mix is usually determined on the advice or instructions of a financial intermediary (the broker). The BMF is in most cases restricted to the clients of the broker who thus performs the dual function of selling agent and investment manager. The following criteria are *in addition* to the general requirements, where applicable, of this Code.
- 8.2 The Commission takes the view that BMFs can have the potential to offer a service of value to investors. However, given the extra expense involved and the uncertainty of any commensurate benefit to the investor, the Commission considers that the service would seem only to be justified if the fund:
- (a) is expected to consistently outperform comparable funds being offered by the insurance company by more than the investment management charge, or;
 - (b) offers a better service or other advantage.
- 8.3 The Commission's main concern is therefore that prospective scheme participants are fully informed of the nature and costs of the service they are being offered and that suitable protective measures are present.

Agreement between Insurance Company and Broker

- 8.4 The respective roles of the insurance company and the broker should be clearly set out in a formal agreement between the insurance company and intermediary, to be submitted to the Commission. In particular, the use of third parties by the broker should not be allowed to cloud the lines of responsibility.

Broker Expertise

- 8.5 The Commission will require to be satisfied that the insurance company has closely examined the caliber of brokers, their financial circumstances and previous investment management knowledge and experience prior to appointment. Insurance companies must have satisfied themselves as to the fitness of those they appoint as BMF managers. In addition the investment manager of a BMF must hold a license, where appropriate, under the Securities Ordinance.

Control Procedures

- 8.6 The Commission expects that on-going control procedures will be in place and, in principle, include:

(a) *Dealing*

only "forward" or "spot" pricing being permitted for BMFs when dealing within an insurance company's internal funds; i.e. BMFs should not be allowed to deal with the benefit of hindsight;

(b) *Switching*

where warranted, the insurance company imposing daily switching limits on BMFs dealing within the insurance company's internal funds, in order to protect scheme participants from any significant price swings;

(c) *Performance*

the insurance company ensuring that the stated investment objective of the BMF is matched by employed strategy - e.g. a stated low risk objective should not be matched by a high risk strategy;

(d) *Investment Objective*

the insurance company actively monitoring the BMF investment performance and introducing guidelines for when consideration to terminate the BMF should be made. Any decisions taken should be documented and promptly conveyed to scheme participants and to the Commission in writing. These guidelines should be disclosed in the principal brochure and the constitutive documents of the BMF.

(e) *Charges*

the insurance company not allowing the BMF to invest large percentages of the fund in the insurance company's managed, with-profits or cash funds while enjoying an unjustified investment management fee.

Additional Disclosure Requirements of the Principal Brochure

- 8.7 It must be made clear that investors will incur higher charges than on some other contracts i.e. the investment management charge paid to the broker. As this charge is generally borne by the scheme participant out of the fund, it can lack the visibility and impact of fees charged direct. The Commission will therefore expect a high level of clarity in any marketing brochure and will not accept, for example, the use of terminology which disguises charges or confuses the scheme participant e.g. charges being quoted on a weekly basis.
- 8.8 The principal brochure must make it clear that the essence of the BMF is the replacement, either partly or completely, of an insurance company's investment expertise for that of the broker at an extra cost to the scheme participant. The scheme participant must be adequately informed that he is opting for a service which in investment terms may, or may not, benefit him. Potential scheme participants should then be in a position to assess whether the service being offered is worthwhile to them.
- 8.9 The Commission will expect the following to be clearly disclosed in the principal

brochure:

(a) *Charges*

All charges payable, and to whom they are accruing, (including any commissions on dealing in the property of the BMF e.g. unit trust commission) and the extent of the brokers' financial interest in selling the fund. Appropriate statements would be;

"to the extent that [the broker] sells units in the [BMF], [the broker] will receive commission from [the insurance company] in addition to their annual management charge." and;

"where [the BMF] invests in unit trusts the cost of buying such unit trusts will be borne by the fund. Neither [the broker] nor [the insurance company] will receive commission from the unit trust group."

(b) *Investment Objectives*

The investment objectives of the BMF, together with the strategy adopted to attain those objectives and any inherent risks involved. The insurance company should also disclose the benchmark(s) against which the performance of the BMF would be measured and results documented.

(c) *Nature of Investment*

The nature of the relationship between all parties involved and the responsibilities of each. For example, that:

- (i) the insurance company has full responsibility for the administration of the fund;
- (ii) investment returns and the quality of the service are entirely dependent upon the expertise of the broker;
- (iii) the broker has full discretion to advise on the investment content of the fund.

(d) *Experience and Expertise*

The extent of the broker's qualification and experience in managing and operating similar types of products.

(e) *Policy*

The nature and choice of insurance policy being recommended or being available to the scheme participant in conjunction with the BMF.

(f) *Termination*

The conditions and procedures applicable to termination of the fund e.g. whether

the insurance company will switch scheme participants into their own managed fund on a bid basis.

(g) *Switching and Dealing*

All the relevant terms of switching and dealing.

(h) *Responsibility Statement*

A responsibility statement to be placed in the principal brochure or supplied to the Commission in the form of an undertaking to the effect that:

"[The insurance company] accepts responsibility for the accuracy of statements contained in [this] brochure and that no material facts have been omitted from the information provided to the best of [the insurance company's] knowledge."

Post-Authorization Requirements

- 8.10 The Commission also requires that appropriate and timely on-going information is provided to scheme participants regarding the progress of their investment. As a minimum requirement, a quarterly investment report should be provided to scheme participants, and to the Commission, showing, inter alia, performance statistics alongside benchmark(s) described in 8.9(b) above. There should also be regular publishing of BMF prices.

Chapter 9: Investment-Linked Savings Plans

General

- 9.1 An Investment-Linked Savings Plan (ILSP) is generally a unit-linked investment plan established under an investment contract where notional units linked to the performance of authorized funds or other financial instruments are issued to participants in return for their contributions. The investment or asset mix of a participant portfolio under the ILSP is usually determined by the participant or his appointed investment advisor.
- 9.2 An ILSP is usually, though not exclusively, promoted by an overseas insurance company that is not authorized to carry out insurance business in Hong Kong. In the absence of prudential supervision by the Insurance Authority, the Commission takes the view that additional structural and operational requirements should be imposed on ILSPs to afford appropriate protection to participants. Further, the applicant company must be authorized by or subject to the requirements of a supervisory authority in Hong Kong or any other authority which is acceptable to the Commission. The following criteria are *in addition* to the general requirements, where applicable, of this Code.

Appointment of Trustee

- 9.3 A trustee acceptable to the Commission must be appointed for the scheme. The trustee must be either:
- (a) a bank licensed under Section 16 of the Banking Ordinance;
 - (b) a trust company which is a subsidiary of such a bank;
 - (c) a trust company registered under Part VIII of the Trustee Ordinance; or
 - (d) a banking institution or trust company incorporated outside Hong Kong which is acceptable to the Commission.
- 9.4 A trustee must be independently audited and have minimum issued and paid-up capital and non-distributable capital reserves of HK\$10 million or its equivalent in foreign currency.
- 9.5 Notwithstanding 9.4 above, the trustee's paid-up capital and non-distributable capital reserves may be less than HK\$10 million if the trustee is a wholly-owned subsidiary of a substantial financial institution (the holding company); and
- (a) the holding company issues a standing commitment to subscribe sufficient additional capital up to the required amount, if so required by the Commission; or
 - (b) the holding company undertakes that it would not let its wholly-owned subsidiary default and would not, without prior approval of the Commission, voluntarily dispose of or permit the disposal or issue of any share capital of the trustee such that it ceases to be a wholly-owned subsidiary of the holding company.

General Obligations of Trustee

9.6 The trustee must:

- (a)
 - (i) take into its custody or under its control all the property of the scheme and hold it in trust for the scheme participants in accordance with the provisions of the constitutive documents;
 - (ii) register cash and registrable assets in the name of or to the order of the trustee; where borrowing is undertaken, such assets may be registered in the lender name or in that of a nominee appointed by the lender; and
 - (iii) be liable for the acts and omissions of its nominees and agents in relation to assets forming part of the property of the scheme;
- (b) take reasonable care to ensure that the issue and cancellation of units effected by the scheme are carried out in accordance with the provisions of the constitutive documents;
- (c) take reasonable care to ensure that the methods adopted by the applicant company in calculating the value of units are adequate to ensure that the issue and cancellation prices are calculated in accordance with the provisions of the constitutive documents;
- (d) carry out the instructions of the applicant company in respect of investments unless they are in conflict with the provisions of the offering or constitutive documents; and
- (e) take reasonable care to ensure that the investment and borrowing limitations set out in the offering or constitutive documents and the conditions under which the scheme was authorized are complied with.

Retirement of Trustee

9.7 The trustee may not retire except upon the appointment of a new trustee and subject to the prior approval of the Commission. The retirement of the trustee should take effect at the same time as the new trustee takes up office.

Independence of Trustee and the Applicant Company

9.8 The trustee and the applicant company must be persons who are independent of each other.

9.9 Notwithstanding 9.8 above, if the trustee and the applicant company are both bodies corporate having the same ultimate holding company, whether incorporated in Hong Kong or outside Hong Kong, the trustee and the applicant company are deemed to be independent of each other if:

- (a) they are both subsidiaries of a substantial financial institution;

- (b) neither the trustee nor the applicant company is a subsidiary of the other;
- (c) no person is a director of both the trustee and the applicant company; and
- (d) both the trustee and the applicant company sign an undertaking that they will act independently of each other in their dealings with the scheme.

Appointment of Auditor

- 9.10 The applicant company shall, at the outset and upon any vacancy, appoint an auditor for the scheme, subject to the approval of the trustee.
- 9.11 The auditor must be independent of the applicant company and the trustee.

Obligations of the Applicant Company

- 9.12 The applicant company shall:
 - (a) use its best endeavors to ensure that the scheme is conducted in a proper and efficient manner;
 - (b) make available for inspection by the trustee and auditor all books and accounts of the applicant company in relation to the scheme; and
 - (c) give to the trustee and auditor such oral and written information as they require with respect to all matters relating to the scheme.

Additional Disclosure Requirements for Scheme Documentation

- 9.13 The constitutive documents should disclose details of the functions, duties and obligations of the trustee, auditor and applicant company. There should also be detailed provisions for the appointment, retirement and removal of the trustee and auditor.
- 9.14 The following warning statements must appear on the front page of the principal brochure (as applicable, in the case of an insurance company not authorized in Hong Kong):

"Investors should note that this product may only be sold through registered or exempt securities dealers and investment advisers. This investment-linked savings plan is NOT a unit trust or contract of insurance."

"[The applicant company] is not authorized by the Insurance Authority in Hong Kong to carry out insurance business."

Additional Requirements for Hong Kong Representative

- 9.15 The Hong Kong Representative must provide the Commission with a written undertaking that they would only allow the ILSP to be sold through registered (or exempt) securities dealers and investment advisers and that authorized scheme documents would only be provided to same for distribution to the public.

PART III: POST-AUTHORIZATION REQUIREMENTS

Chapter 10: Post-authorization Requirements

Changes to Documentation

- 10.1 All proposed alterations or additions to the principal brochure and constitutive documents must be submitted to the Commission for prior approval. The Commission will determine whether scheme participants should be notified and the period of notice (if any) that should be applied before the changes are to take effect. Such notice period would not normally exceed three months, but individual cases will be considered on their merits.
- 10.2 The constitutive documents may be altered without consulting scheme participants provided that the proposed alteration:
- (a) is necessary to make possible compliance with fiscal or other statutory or official requirements; or
 - (b) does not materially prejudice scheme participants' interest, does not to any extent release the parties from any liability to participants and does not increase the costs and charges payable under the scheme.
- 10.3 The Commission may accept undertakings from an applicant company to delay making a required amendment to a document until an opportune time, but in such cases the Commission may impose a reasonable time limit for carrying out the required amendment, and require a written undertaking from an applicant company to comply, in the interim period, with the substance of the requirement.

Increase in Fees

- 10.4 In respect of any increase of the fees and charges from the current level as stated in the principal brochure up to the maximum level permitted by the constitutive documents, at least three months prior notice must be given to all scheme participants.

De-authorization

- 10.5 Following the authorization of a scheme, the applicant company should give at least three months' notice to scheme participants of any intention not to maintain such authorization. Such notice should be submitted to the Commission for prior approval and contain reasons for the de-authorization and the alternatives available to scheme participants in the event of de-authorization.

Termination

- 10.6 Where a scheme or a fund linked to the scheme is to be terminated, in addition to

following any procedures set out in the constitutive documents or governing law, notice shall be given to scheme participants. Such notice should be submitted to the Commission for prior approval and shall contain reasons for the termination, the alternatives available to participants (including, if possible, a right to switch without charge into another authorized scheme or fund), the estimated costs of the termination and who is expected to bear these.

Advertising and Public Announcements

- 10.7 Advertisements and other invitations to invest in a scheme, including public announcements, must be submitted for authorization prior to their issue or publication in Hong Kong. Authorization may be varied or withdrawn by the Commission as it deems fit. The criteria for authorization of advertisements are set out in Appendix E.
- 10.8 No radio, television or cinema advertising of a scheme is permitted in Hong Kong.
- 10.9 If a scheme is described as having been authorized by the Commission, it must be stated that authorization does not imply official approval or recommendation.

Appendix A

Information to be disclosed in the Principal Brochure

The principal brochure, preferably in one single document, should contain the information necessary for prospective scheme participants to be able to make an informed judgment of the scheme and in particular should contain the following:

(a) *Name and Type of Scheme*

The name and description of the scheme must not be misleading to potential scheme participants and should be an accurate reflection of the type of scheme and its objectives.

(b) *Parties Involved*

The names and registered address of all parties involved in the operation of the scheme with a brief description of the applicant company.

(c) *Investment Returns*

Details of how the investment return of the scheme is determined. Except where the scheme's investment returns are subject to a non-variable guarantee, a warning should be stated to the effect that investment involves risks.

**See Chapter 7 for additional disclosure requirements for Guaranteed Funds.*

If the nature of the investment policy so dictates, a warning should be given that investment in the scheme or fund linked to a scheme is subject to abnormal risks, together with a description of the risks involved.

(d) *Fees and Charges*

Explanations of fees and charges may be abbreviated, but should be clearly identified to include;

(i) the level of all fees and charges payable by a scheme participant, including all charges levied on subscription, redemption and switching;

(ii) the level of all fees and charges payable by the scheme or a fund linked to the scheme;

(iii) details of whether charges are subject to change and the relevant notice period.

A summary of all fees and charges in tabular form should be provided to give scheme participants an overview of the fees structure at a glance. Where complex calculations are required to disclose fees and charges, illustrative examples should be given for clarity.

(e) *Investment Objectives and Restrictions*

Summary of investment objective of the scheme or fund(s) linked to a scheme, including, where applicable:

- (i) the types of intended investments, and their relative proportions in the portfolio;
- (ii) the geographical distribution of the intended investments;
- (iii) the investment and borrowing restrictions; and
- (iv) if the nature of the investment policy so dictates, a warning that investment in the scheme is subject to abnormal risks, and a description of the risks involved.

(f) *Borrowing Powers*

The circumstances under which the scheme or fund(s) linked to a scheme may have outstanding borrowings and the purpose for which such outstanding borrowings were incurred.

(g) *Summary of Provisions in Constitutive Documents*

A summary of the provisions described in paragraphs (d), (f), (g), (h) and (k) of Appendix C with respect to:

- Valuation of Property and Pricing
- Characteristics of Premiums/Contributions
- Benefits
- Maturity and Early Surrender Values
- Conditions of Termination

(h) *Application and Surrender Procedures*

A summary of procedures for application and surrender.

(i) *Cooling-off Period*

A summary of the provisions described in 6.11 and 6.12 with respect to the cooling-off period.

(j) *Governing Law*

The governing law of the scheme should be disclosed and an acknowledgment that the parties involved have the right to bring legal action in a Hong Kong court as well as in any court elsewhere which has a relevant connection with the scheme.

(k) *Taxation*

Where the likely tax benefits to be enjoyed by scheme participants are described, the principal brochure should also briefly explain the applicant company's understanding of

the tax implications for Hong Kong scheme participants, based on expert advice received by the applicant company.

Scheme participants should also be advised to seek professional advice regarding their own particular tax circumstances.

(l) *Date of publication of the principal brochure*

All facts and figures in the principal brochure should be as reasonably up to date as possible.

(m) *Responsibility Statement*

A statement that the applicant company accepts responsibility for the accuracy of the information contained in the brochure.

(n) *Authorization Statement*

If a scheme is described as having been authorized by the Commission it must be stated that authorization does not imply official approval or recommendation.

Appendix B

Information to be disclosed in the Illustration Document

| | |
|----------------------------|-----------------------------|
| Name of Product: | [Name of Product] |
| Name of Insurance Company: | [Name of Insurance Company] |

The following table illustrates the amount [you, if personalized / *a policy/contract holder, if standard*] would receive, after deduction of fees and charges, based on the following assumptions:

| | |
|------------------------|--|
| Contract Term: | [Actual Contract Term, if personalized / <i>Contract Term based on a maximum commission scale, if standard</i>] |
| [Premium Payment Term: | (if different from Contract Term)] |
| Premium: | [Actual Premium, if personalized / <i>Minimum premium requirement, if standard</i>] |
| Return: | Illustrated at [11%] and [5%] p.a.* |

| Table Projected Surrender Values for a [Regular/Single] Premium [Name of Product] with Contributions of [\$ XXX] for [XXX Periods] | | | |
|---|--|---|--|
| Number of Years after Policy Issuance | Total Premium Paid since Start of Policy | Surrender Value Assuming Net Rate of Return of [11%p.a.]* | Surrender Value Assuming Net Rate of Return of [5%p.a.]* |
| 1 | | | |
| 2 | | | |
| 3 | | | |
| 4 | | | |
| 5 | | | |
| 10 | | | |
| XX | | | |

* *The rates of return shown here are for illustrative purposes and are not based on past performance.
The actual return may be different.*

You should only invest in this product if you intend to pay the premium for the whole of your chosen premium payment term. Should you terminate this product early, you may suffer a loss as illustrated above.

Declaration

I confirm having read and understood the information provided in this illustration and received the principal brochure.

signed & dated: _____

Applicant

Appendix C

Contents of the Constitutive Documents

The constitutive documents should incorporate the detailed terms and conditions of the scheme. The paragraphs which follow illustrate the details which the Commission will look for although it is prepared to be flexible in determining which criteria should apply.

(a) *Name and type of Scheme*

A statement to specify the parties involved including, as applicable, the applicant company, the management company, the guarantor, the trustee and the auditor, giving full particulars of their functions, duties and obligations.

(b) *Parties Involved*

(c) *Investment Returns*

A detailed description of how the investment returns of the scheme is determined, for example, with reference to;

- (i) a fund or funds of assets held in the name of the policy issuer;
- (ii) any notional fund (with its basis stated); or
- (iii) a rate determined at the discretion of the policy issuer.

(d) *Valuation of Property and Pricing*

- (i) For schemes linked to unitized funds;
 - the method of determining the value of the assets and liabilities of the property of the scheme;
 - the method of calculating the issue and redemption prices;
 - how frequently prices are established;
 - the lead times for the allocation of premiums to units and the realization of units; and
 - the circumstances under which the above might change; or
- (ii) For schemes linked to funds which are not unitized;

- how and when the fund is valued;
- how and when the investment return is calculated and distributed amongst the scheme participants; and
- the circumstances under which the above might change.

(e) *Guarantee*

Whether investment performance or capital is guaranteed and if so details of:

- (i) the rate or amount guaranteed;
- (ii) the conditions under which the rate or amount may be altered or discontinued;
- (iii) the nature of the guarantee, e.g. a flat guarantee, year on year, or compounded;
- (iv) how and when the guarantee is invoked or revoked;
- (v) any charges or consideration for the guarantee;
- (vi) the date of expiry of the guarantee;
- (vii) if the guarantor is an entity other than the policy issuer, the provisions for appointment, retirement or removal;
- (viii) where applicable, the methods of determining the discretionary benefits to be paid to scheme participants in excess of the guaranteed amount; and
- (ix) where applicable, the extent to which, and the basis on which, the policy issuer may set up a reserve, by whatever name called, so as to smooth the progression of unit prices or rates of return.

(f) *Premiums and Contributions*

- (i) The full amount to be paid.
- (ii) The currency of payment.
- (iii) To whom and where paid.
- (iv) How paid and the options if any for payment.
- (v) The frequency, due dates and for what periods premiums must be paid.
- (vi) If there are fixed due dates, the grace period and penalties if any for late payment.
- (vii) The proportion or amount of the premiums paid which will be applied for investment purposes and if these proportions change as the scheme progresses, the stages at which these changes occur and the manner in which they change.
- (viii) The consequences and options if any should payment of premiums be discontinued at any time.

(g) *Benefits*

The currency, dates and places of payment of benefits.

(h) *Maturity and Early Surrender Value*

- (i) The maturity value.
- (ii) The methods of calculation of full surrender value, partial surrender value and death benefit.
- (iii) Any notice periods for full or partial surrenders.
- (iv) Other settlement options or rights.
- (v) The circumstances under which payment of benefits may be deferred or suspended.
- (vi) The maximum interval between the receipt of a properly documented request for surrender and the date of payment.
- (vii) Whether interest is payable in respect of the period between the effective date of claim and the date of payment.

(i) *Fees and Charges*

- (i) All specific fees and charges under the scheme whether calculated by way of an amount, percentage or otherwise.
- (ii) All indeterminable fees and charges.
- (iii) Information as to when and on what event the fees and charges will fall due.
- (iv) Any taxes and expenses charged to the scheme or levied against fund(s) linked to the scheme on a basis deemed fair and reasonable by an actuary or other person of professional standing.
- (v) Any fees payable to, as applicable, the applicant company, management company, trustee, guarantor or any other party.

(j) *Investment and Borrowing Restrictions*

The restrictions on the investment of the scheme or fund(s) linked to a scheme (if any) and borrowing restrictions.

(Note: The maximum borrowing limit of the scheme or any fund linked to a scheme should not exceed 25% of net asset value, inclusive of short-term borrowings to cover redemptions or other special situations.)

(k) *Termination of the Scheme*

The circumstances in which a class of scheme or a fund linked to a scheme may be

terminated and the relevant notice to be given to scheme participants.

(l) *Governing Law*

The governing law of the scheme must be specified.

(m) *Cooling-off Period*

The detailed provision of a cooling-off period, as in 6.11 and 6.12, within which an investor may withdraw unconditionally, subject to a market value adjustment, if any.

Appendix D

Compliance Checklist

The compliance checklist is to assist applicants in preparing an application. It should be completed and submitted to the Commission together with the other documents required for an application (see 1.3). References to the document(s) should be noted in the right-hand column.

| Information to be disclosed in the Principal Brochure | Where Found (Document/Page/Para) |
|--|-------------------------------------|
| <i>(a) Name and Type of Scheme</i> | |
| <i>(b) Parties Involved</i> | |
| <i>(c) Investment returns</i> | |
| <i>(d) Fees and Charges (i)</i> | |
| <i>(ii)</i> | |
| <i>(iii)</i> | |
| <i>(e) Investment Objectives and Restrictions (i)</i> | |
| <i>(ii) etc.</i> | |
| <i>(f) Borrowing Powers</i> | |
| <i>(g) Summary of Provisions in Constitutive Documents</i> | |
| - Valuation of Property and Pricing | |
| - Characteristics of Premiums/Contributions | |
| - Benefits | |
| - Maturity and Early Surrender Values | |
| - Conditions of Termination | |
| <i>(h) Application and Surrender Procedures</i> | |
| <i>(i) Cooling-off Period</i> | |

| | |
|--|--|
| <i>(j) Governing Law</i> | |
| <i>(k) Taxation</i> | |
| <i>(l) Date of publication of the Principal Brochure</i> | |
| <i>(m) Responsibility Statement</i> | |
| <i>(n) Authorization Statement</i> | |

Additional disclosure requirements for Broker Managed Funds

Please locate information with respect to 8.7-8.9 of this Code.

Additional disclosure requirements for Investment-linked Savings Plans

Please locate information with respect to 9.14 of this Code.

| Contents of the Constitutive Documents | Where Found (Document/Page/Para) |
|--|---|
| <i>(a) Name and type of Scheme</i> | |
| <i>(b) Parties Involved</i> | |
| <i>(c) Investment Returns (i)</i> | |
| <i>(ii)</i> | |
| <i>(iii)</i> | |
| <i>(d) Valuation of Property and Pricing (i)</i> | |
| <i>(ii)...etc</i> | |
| <i>(e) Guarantee</i> | |
| <i>(f) Premiums and Contributions</i> | |
| <i>(g) Benefits</i> | |
| <i>(h) Maturity and Early Surrender Value</i> | |

| | |
|--|--|
| <i>(i) Fees and Charges</i> | |
| <i>(j) Investment and Borrowing Restrictions</i> | |
| <i>(k) Termination of the Scheme</i> | |
| <i>(l) Governing Law</i> | |
| <i>(m) Cooling-off Period</i> | |

Additional disclosure requirements for Investment-linked Savings Plans

Please locate information with respect to 9.13 of this Code.

Appendix E

Advertising Guidelines

As a general principle, every advertisement for a scheme must have the prior authorization of the SFC. This requirement is derived from the Protection of Investors Ordinance (PIO), and is a provision of this Code. The issue of an unauthorized advertisement may be an offence under s.4 of the PIO. These guidelines should be interpreted as guidance rather than rigid rules, and issuers are expected to be guided by their spirit, as well as the content.

These guidelines are intended to apply to all forms of advertising, including print media, brochures, brochures, direct marketing, "fax on demand" services, posters in public places and advertising of authorized schemes on the Internet. In the latter case, a hard copy of the relevant pages of the Internet website should be submitted to the SFC.

To facilitate efficient processing of advertisements, it is recommended that a management company nominate one person, based in Hong Kong, to liaise with the SFC.

Authorization may be varied or withdrawn by the SFC as it deems fit. Once authorized, the advertisement may be used for as long as the information it contains remains current.

Corporate Advertisements

A corporate advertisement, which only advertises the expertise of or services offered by the applicant company without referring to any particular product, does not generally require authorization, unless it can be construed as a product advertisement.

Newsletters/Updates

Newsletters, monthly updates or fact sheets may be sent to existing investors on a regular basis. Where such materials are issued in a standard format, there is no need to submit every issue once the standard format has been approved. Any subsequent changes in the format should be submitted.

CONTENT OF ADVERTISEMENTS

1. **The general principle is that no advertisement can be made that is false, biased, misleading or deceptive.** The following statements are designed to illustrate this general principle.
2. Advertisements may not refer to any unauthorized scheme, except as permitted in para. 14.

Language & Graphics

3. A statement of opinion regarding a scheme or applicant company's level of performance must be reasonable.
4. An advertisement should not contain words or phrases that may give investors the impression that they cannot lose money or that profits are guaranteed, unless they

actually are guaranteed.

5. An advertisement should not focus on the potential return of a scheme without some balancing reference to the risks involved. An advertisement should not give the impression that an investor could profit without risk.
6. An advertisement should not contain language, artwork or graphics that is inaccurate or inconsistent with its principal brochure and other documents.
7. An advertisement should not seek to denigrate a scheme's competitors in such a way as might lower the reputation of the industry, or use language or artwork that would be considered by a reasonable person to be in poor taste.

Statistics/Performance Figures

8. If performance data (including charts, graphs, tables, and reference to awards and rankings) or estimated yield is quoted in a principal brochure or advertisement, supporting documents should be submitted to the SFC to substantiate the data or the calculation. The computation basis should be stated e.g. offer-to-offer or NAV-to-NAV. No forecast of the scheme's performance can be made. The publication of a prospective yield does not constitute a forecast of performance.
9. Performance statistics should, where possible, be quoted from an internationally recognised statistical source. All performance data should be referenced to the source and dated.
10. Performance figures shown must be actual rather than simulated results. Hypothetical figures may be permitted for schemes with complicated mechanisms for the purpose of explaining those mechanisms to investors, in which case such figures must be conservative, and it must be clearly stated to the effect that the figures used are for illustrative purposes only and not indicative of the actual return likely to be achieved by the investor. Annualized returns are generally only acceptable if the actual returns for all the individual years are shown in addition.
11. A comparison of performance figures should be fair, accurate and relevant, comparing "like with like".
12. If graphs are shown, they should be clearly presented without distortion. If different sets of data are plotted on the same graph, the same axis should be used.
13. If non-US\$/HK\$ denominated returns are shown, the advertisement should also show the returns in US\$/HK\$ terms. Alternatively, the advertisement should include a statement to alert investors to the effect that *the investment returns are denominated in [foreign currency]. US/HK dollar-based investors are therefore exposed to fluctuations in the US/HK dollar/ [foreign currency] exchange rate?*
14. Reference to past performance of an unauthorized scheme to indicate the fund manager's past track record can only be used in the following circumstances:
 - (a) the authorized scheme is newly launched with short or no past track record;

- (b) the investment objectives of the unauthorized scheme are substantially the same as the authorized scheme, managed by the same management team with similar investment policies and strategies;
- (c) the advertisement makes clear that the performance figures quoted are **not** those of the authorized scheme and that the unauthorized scheme is not authorized in Hong Kong and not available to Hong Kong residents.

Warning Statements

15. Warning statements are required on advertisements:

- (a) to the effect that investment involves risks, and that the principal brochure should be read for further details; and
- (b) (where past performance is quoted) the past performance figures shown are not indicative of future performance.

The text may be varied but the message should be clear and not disguised. If a scheme is described as having been authorized by the Commission it must be stated that authorization does not imply official approval or recommendation.

16. Warning statements should if possible be printed in type of the same size as the rest of the text in the advertisement, and in any event must be capable of being read with reasonable ease by anyone scanning the advertisement.

17. Warning requirements for advertisements of specialized schemes are as follows:

Guaranteed funds

The advertisement must disclose:

- (a) all material conditions which affect the scope or validity of the guarantee including, the warning, where relevant, that the guarantee only applies to investors who hold their investment until the date specified in the guarantee and that termination or withdrawal before such date are fully exposed to fluctuations in the value of the scheme assets and/or subject to penalties; and
- (b) the name of the guarantor (if other than the policy issuer) and refer investors to the principal brochure for more information.

Mortgage schemes

A warning statement to the effect that value of the plan will be insufficient to repay the mortgage if the return on the funds produces an average annual growth rate less than the assumed rate.