

**C L I F F O R D
C H A N C E**

CLIFFORD CHANCE
高偉紳律師行
29TH FLOOR, JARDINE HOUSE
ONE CONNAUGHT PLACE
HONG KONG
TEL +852 2825 8888
FAX +852 2825 8800
INTERCHANGE DX-009005 CENTRAL 1
www.cliffordchance.com

YOUR REFERENCE

IN REPLY PLEASE QUOTE
MGXS/RN

DATE
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DIRECT DIAL

SFC Professional Investor Rules
12/F, Edinburgh Tower
The Landmark
15 Queen's Road, Central
Hong Kong

Dear Sirs

The Draft Securities and Futures (Professional Investor) Rules (the “draft Rules”)

Thank you for giving us the opportunity to comment on the Securities and Futures Commission (“SFC”) proposed draft Rules made under clause 384 of the Securities and Futures Bill (the “Bill”). Generally we welcome the proposal by the SFC to broaden the definition of “professional investor”. We have now had the chance to review the draft Rules, and set out our comments below.

Specifically

Turning to consider the specific draft Rules on which the SFC has particularly expressed interest in receiving comments, we believe that a person who has a current certificate in writing signed by a licensed person to the effect that, that person is sufficiently knowledgeable to understand the risks associated with the investment should be included in the definition of “professional investor”. In the United Kingdom, Financial Services and Markets Act 2000 (Financial Promotion) Order 2001, these investors are classed as “certified sophisticated investors” and are exempted (under certain conditions) from financial promotion restrictions in respect of communications, in the course of business, of an invitation or inducement to engage in investment activity.

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PARTNERS

J.W. BAIRD
D.G. BROCK
A.Y.L. CHAN
C.S.K. CHAN
C.F.Y. CHOI
R.M. DENNY
I.P.D. HARDEE
J.E. JAMISON
H.R. JENKINS

P.F. KRUGER
W.W. LI
A. LINDSAY
A.S.H. LO
A.A. MACPHERSON
M.E. MATSON
P.S. O'CONNOR
M.D. ROGERS
S.J. ROITH

M.G. SHIPMAN
C.F.M. TANG
S.J. VALENTINE
J.A. WALKER
J.R. WALTER
S.K.K. WEBB
J.F. WREDE

FOREIGN LEGAL CONSULTANTS

E. CASDAGLI (ENGLAND AND WALES)
E.J. COHEN (USA)
GAO P.J. (PRC)
S.P. HARDER (USA)
J.R. LEWIS (USA)
J.M. MADDOX (USA)
N.C.H. STAMP (ENGLAND AND WALES)
J. ZONIS (USA)

CONSULTANT

R.L. CALDWELL

Generally

We would like to take this opportunity to raise a few related issues which we believe would be helpful to the market.

1. *The definition of "professional investor" in the Bill*

Under the definition of "professional investor" in the Bill, a scheme which is constituted under the law of any place outside Hong Kong, but constituted similarly to a collective investment scheme authorised under section 103 of the Bill, falls within the definition of a "professional investor". Perhaps the SFC could confirm that it is intended that this includes unregulated off shore schemes as well as schemes regulated under the law of the place of incorporation/establishment. If not, we would suggest that unregulated off shore schemes should be included in the definition of "professional investor" under the draft Rules.

2. *The limited persons "rule"*

The Companies Ordinance ("CO") and Part IV of the Bill refers to "offer to the public" and "invitation to the public" respectively, but as yet there is no definition of the term, the "public", either in the CO or the Bill (or any of the Codes issued by the regulators in Hong Kong). Also, case law in Hong Kong provides no guidance as to the number of persons constituting the "public".

In December 1991, the SFC stated that an invitation will not be deemed to be made to the public if, broadly, it involves a distribution of numbered documents up to a maximum of 50 named persons in Hong Kong; where each numbered copy is individually addressed to a named person, only that named person is entitled to take up the offer or invitation, and that person's acceptance of the offer cannot be transferred to another person (the so called "limited persons rule"). However, the SFC subsequently stated in December 1996 that this is not a hard and fast rule and that each offering must be considered on its specific facts.

In the United Kingdom, the Public Offers of Securities Regulations 1995 ("POS Regulations"), Part II (Unlisted Securities) states clearly that, an offer of securities shall be deemed not to be an offer to the public in the United Kingdom if, to the extent that the offer is made to persons in the United Kingdom, the securities are offered to no more than fifty persons.

It might be helpful if there could be similar guidance on what will otherwise remain a somewhat grey area under the Bill.

Also there is some doubt as to whether *the limited persons "rule"* and the "professional investor" exception can be combined. The conservative view is that they are separate exceptions and therefore what happens in practice should reflect the separate nature of the exceptions, and so possibly these exceptions may not be combinable. Again, it would be helpful if some guidance could be given on whether the *limited persons "rule"* and the "professional investor" exceptions are combinable. Under the United Kingdom's POS

Regulations, the “professional investor” exception and the “fifty persons” rule are combinable.

3. *The CO*

As you know, under the CO it is an offence for any person to issue, circulate or distribute in Hong Kong any document offering to the public, shares or debentures in an "oversea company" for subscription unless a prospectus is prepared, complying with the content requirements of the CO (including as to a Chinese translation), and registered on or before its date of publication with the Registrar of Companies in Hong Kong.

The prospectus requirements will therefore apply if:

- (i) there is an offering by the oversea company;
- (ii) of its shares "for subscription";
- (iii) by way of a document;
- (iv) to the public in Hong Kong.

However, for the purposes of determining whether the prospectus requirements under the CO apply to the proposed offering of shares in the company, it is necessary to consider whether there is an "offer to the public". In this respect, the CO specifically provides that an offer of shares in an oversea company for subscription or sale to "*any person whose ordinary business is to buy or sell shares or debentures, whether as principal or agent*" is not deemed to be an offer to the public.

In our view, it would be helpful if the so called “professional investor” exception under the CO could be brought in line with the “professional investor” exception mentioned in Part IV of the Bill in order to maintain consistency and reduce confusion. In addition, we would note that the so called “professional investor” exception under the CO is only available to Hong Kong incorporated companies to the extent permitted by section 3 of the Companies Ordinance (Exemption of Companies and Prospectuses from Compliance with Provisions) Notice (Cap. 32 sub. leg. L).

4. *Code of Conduct for Persons Registered with the SFC (the “Code”)*

Paragraph 15.2 of the Code specifies categories of “professional investors” which are more or less in line with the “professional investor” exception mentioned in Part IV of the Bill. In order to maintain consistency and reduce confusion, it would be helpful if the SFC could bring the “professional investor” exception under the Code and other relevant SFC codes where there are (or should be) exceptions for “professional investors” in line with the “professional investor” exception mentioned in the Bill, although we anticipate that this may already be in hand.

We hope these comments are helpful to you. Please feel free to contact us if you have any questions or would like to discuss any of these comments further. Again we appreciate the opportunity to comment on these provisions.

Yours faithfully,


Clifford Chance