

Response to Consultation Paper on the Securities and Futures (Open-ended Fund Companies) Rules and Code on Open-ended Fund Companies

1. Do you have any comments on the suggested one-stop process for the establishment of an OFC? Please explain your view.

The one-stop approach is time-saving and efficient by avoiding the OFC applicant from having to submit separate documents to different authorities, especially if business registration (under the Business Registration Ordinance, Cap.310) is also included. In addition, Hong Kong should facilitate electronic filing processes. As with the incorporation of other companies under the Companies Ordinance (Cap. 622), detailed guidance should be provided on the websites of the SFC with checklists and examples, where appropriate, to demonstrate documentary requirements regarding scenarios such as establishment of an OFC, alteration of instrument of incorporation and change of directors.

2. With regards to the suggested factors as to whether a proposed OFC name is “misleading or otherwise undesirable”, are there other factors which you think should be taken into account? Please explain your view.

On the foundation of the factors set forth in the proposed code, the SFC can also prepare an OFC name registration guideline by adopting most of the principles of the Companies Registry’s guideline on registration of company names (http://www.cr.gov.hk/en/companies_ordinance/docs/Guide_RegCompName-e.pdf) to the extent applicable. As the name of an OFC should be approved by the SFC and such approval process will take some time, it is desirable to have a name-reservation system so that an applicant will be able to reserve a name pending the process and arrange for other matters (such as an office lease) in the meantime.

3. Do you have any views on the proposals regarding the instrument of incorporation and the legal capacity of an OFC?

One of the aim of the proposed OFC rules is to enhance market infrastructure to further develop Hong Kong as an international financial center and, in particular, an asset management center as well as a preferred fund domicile. It would be helpful for the SFC to provide specific guideline on issues relating to re-domiciling an overseas OFC to Hong Kong; for instance, there should be a statement that the laws of the jurisdiction from which the company is transferring permit, and does not prohibit, the transfer the domicile of the company to Hong Kong.

The “example” instrument of incorporation to be published by the SFC may include features to promote the status of Hong Kong as an international financial center in a cross-disciplinary manner. For instance, the “example” may include a Hong Kong mediation procedure for determining financial disputes regarding the fund to be facilitated by the Financial Dispute Resolution Centre (noting that arbitration may not be suitable for certain disputes regarding the fund, whereas the Centre can facilitate an ad hoc arbitration as appropriate, if mediation is not successful).

4. What are your views on the proposed General Principles in the draft OFC Code as outlined above? Are there any other areas which you think the General Principles should cover?

As an international financial center, the regulation and compliance of the proposed OFC in Hong Kong should be up to established international standards in order to maintain the faith of the investors in the fund market. The General Principles (and other applicable IOSCO standards) can be applied in particular to the valuation of fund assets.

5. Do you have any comments on the proposed requirements as to the eligibility, appointment and removal, and duties of the key operators of an OFC? Please explain your view.

Hong Kong as a reputable independent legal system. It is desirable to impose OFC requirements in such manner as to make full advantage of Hong Kong’s legal system and the public’s confidence in such system. One way is to require the company secretary or a director of a Hong Kong body corporate to be resident in Hong Kong. This will also enhance transparency in that, for instance, a Hong Kong resident’s legal status (and the fact that he/she is not bankrupt) can be ascertained readily by local searches. An OFC should preferably have a local “company secretary”. If the proposed OFC does not have the position of a “company secretary”, it would then be desirable to require at least one of the directors to be ordinarily resident in Hong Kong. This would enhance corporate governance because a resident officer would give the public confidence that, as a cardinal principle, a local officer will look after the corporate compliance matters of a Hong Kong body corporate.

6. What are your views on the proposed persons and entities which may serve as the process agent of an overseas director and overseas custodian of an OFC?
Perhaps a SFC licensed person can also be the process agent (so long as he/she is so licensed).

7. Do you have any views on the proposals concerning the shares, meetings and resolutions of an OFC discussed above?

The idea of proposing and introducing OFC into Hong Kong is to provide an alternative option for the fund market to choose, despite of setting up a trust fund, setting up funds in the form of a company. Such implementation should cater to both the requisites of a fund and those of Hong Kong corporation. For instance, to enhance corporate governance underlying Hong Kong shareholding principles, shareholder(s) with 10% or more of the entire voting rights of an OFC should be able to requisition a general meeting.

8. Do you agree with the proposed approach with regards to the filings with the CR? Please explain your view.

The proposed OFC code suggests a one-stop approach which divide the filings into Type 1 and Type 2. In general, Type 1 filing would be submitted to the SFC and Type 2 filing would be submitted to the Companies Registry. Type 1 and Type 2 filings are mutually exclusive, which means whatever that is required to be submitted to the SFC for approval would be passed to the Companies Registry by the SFC. By virtue of the one-stop approach, the OFC would not be required to submit an identical document to the Companies Registry on its own again.

The one-stop approach is time-saving and very efficient by avoiding the OFC to submit duplicated documents to different authorities. The new OFC rules should also be proposed with a clear guideline as to the definition and classification of Type 1 filing and Type 2 filing. Such guideline should be comprehensive and includes common scenarios such as submission in relation to change in directors and change of company biography.

On the filing of a notice of removal of the auditor (as opposed to a notice of resignation of the auditor), we suggest that the SFC should provide more oversight by requiring the notice of removal of the auditor to be Type 1 filing (i.e. make the scrutiny by the SFC a pre-requisite). It would be unusual for an OFC to remove its auditor and the SFC is justified to sanction it upon submitted circumstances (and further enquiry, if necessary).

9. Do you have any views on the proposed eligibility, appointment and removal, and

rights and powers of the auditors in the draft OFC Rules?

The removal of the auditor of an OFC prior to the expiration of the auditor's term of service should be subject to approval at a general meeting (not just by a resolution of the directors).

10. Do you agree with the proposed requirements regarding the financial reports of an OFC? Please explain your view

The SFC should have power to approve the use of other financial reporting standard on a case by case basis, while providing guidelines.

11. Do you have any comments on the proposed provisions for the segregated liability of sub-funds and cross sub-fund investments? Please explain your view.

The resources of the sub-fund should be segregated from the OFC's general resources and other sub-funds' resources in the case of an umbrella and sub-fund structure. Yet, in some circumstances, where the sub-fund assets are insufficient to satisfy certain liability, it might in particular circumstances be appropriate for a party contracting with the OFC to have access to the OFC's general assets. Such access, if allowed, should be subject to constitution of the OFC, and indeed, the constitution of an OFC should set forth such details as regards the segregation of the liabilities and assets of different sub-funds or sub-portfolios.

12. Do you have any comments on the proposed draft OFC Rules regarding arrangements and compromises? Please explain your view.

Since the proposed OFC is in the nature of a company incorporated in Hong Kong, the rules in relation to arrangements and compromises may adopt, with modifications, the current regime under the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32).

13. What are your views on the proposed requirements and steps for termination by application to the SFC?

For an umbrella fund, the OFC should disclose in its Instrument of Incorporation the details as regards the segregation of the liabilities and assets of different sub-funds or sub-portfolios and the circumstances, if any, under which general assets of the fund may be available for distribution to shareholders or creditors of a sub-fund.

14. Do you agree with the proposed approach to applying the C(WUMP)O's winding up regime to OFCs and the modifications suggested in the draft OFC Rules when

applying the winding-up regime? Are there any other modifications which you think should be included? Please explain your view.

The C(WUMP)O's winding up regime should not be entirely applicable to an OFC because of the difference in nature of an OFC from other companies. Such regime should be modified to involve the regulation by the SFC to protect the interests of creditors and investors upon insolvency. Consider the one-stop approach that has been taken for the OFC code and rules, the SFC should have a supervisory role in the winding-up process. For instance, the SFC should have the authority and discretion to reject an application for simplified (or fast-track) winding-up of the OFC in appropriate cases.

15. Do you have any comments on the wording in the proposed OFC Code in respect of the investment scope of private OFCs? Please explain your view.

We have no comments on the proposed investment scope of private OFCs.

16. Do you agree with the proposed approach and basic requirements concerning fund operations and disclosure by a private OFC? Do you think that there are other requirements that should be included in the proposed OFC Code? Please explain your view.

The requirements to be imposed on a private OFC should be less complicated and be more flexible comparing to a public OFC. Yet, some basic requirements such as the General Principles should be maintained as a minimum threshold and disclosure of the material affairs of a private OFC should also be made to the shareholders of the OFC from time to time.

17. Do you have any views on the proposed approach to the different types of scheme changes of a private OFC?

Under Chapter 12 of the OFC Code, it should additionally be provided that, where any material change calls for the approval of shareholders or the SFC, separate notice should be sent to the shareholders upon the approval of the material change.

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