



Securities and Futures Commission

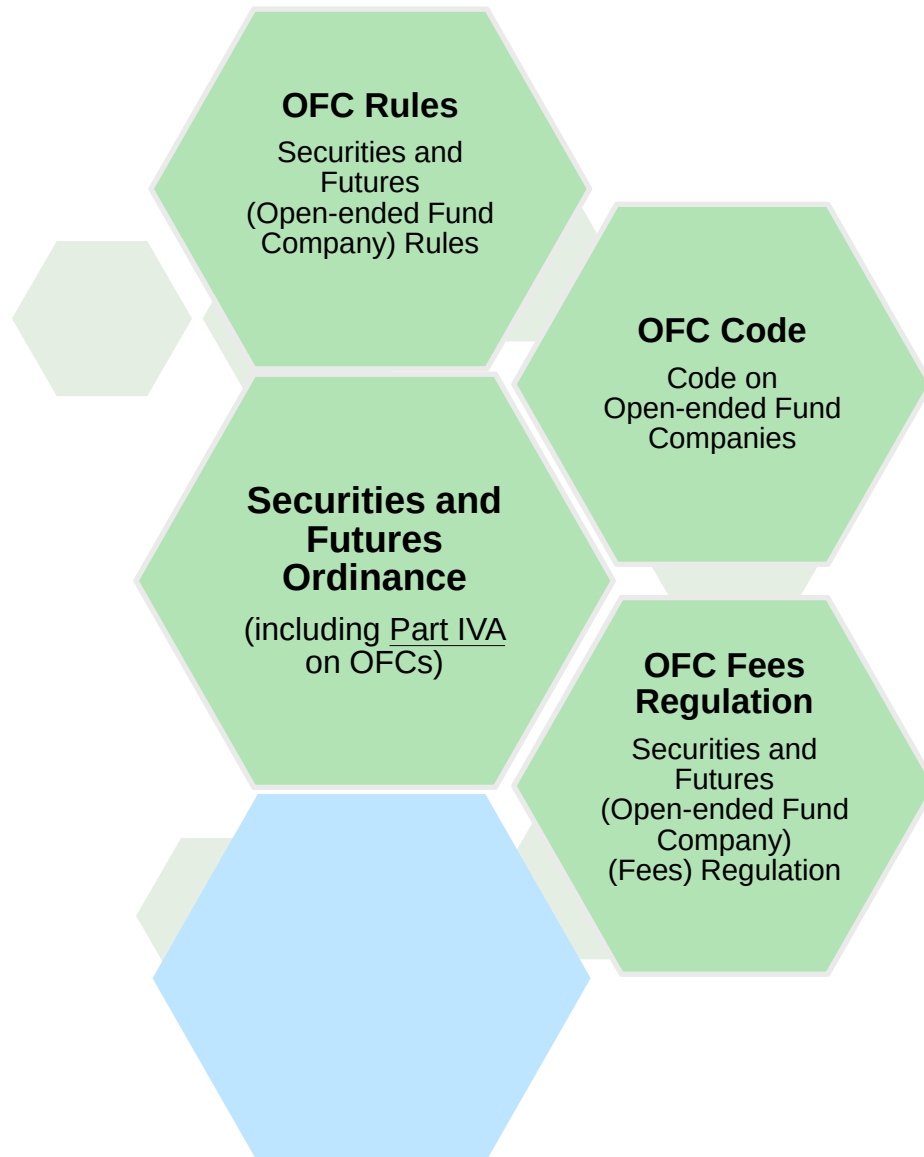
Open-ended Fund Companies (OFC) **– the Corporate Investment Fund Vehicle in** **Hong Kong**

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1. Legal and regulatory framework for OFC

The OFC regime came into effect on 30 July 2018



1. Legal and regulatory framework for OFC

OFC Rules

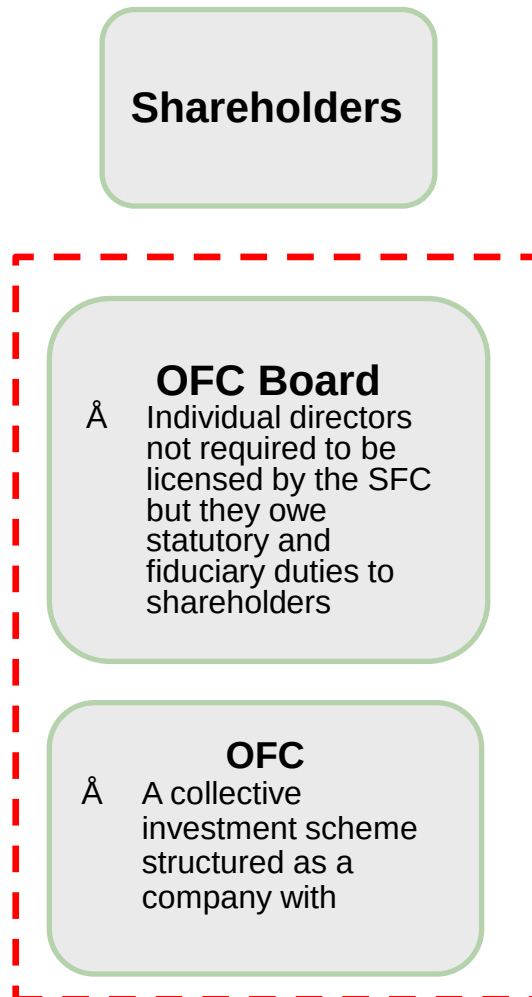
- Å Subsidiary legislation
- Å Relevant Companies Ordinance (Cap. 622) provisions directly set out in the OFC Rules
- Å Voluntary winding up of OFCs
(note: court winding-up of OFCs falls under the C(WUMP)O)

OFC Code

A non-statutory code issued by the SFC

- Å Provides guidelines relating to the registration and post-registration matters

2. OFC structure



3. Public OFCs and Private OFCs



Public OFCs: OFCs which are offered to the public

- ï Compliance with essentially the same requirements under the UT Code as existing SFC-authorised unit trusts

Private OFCs: OFCs which are privately offered

- ï Key regulatory focus:

Key operators -

4. Establishment of an OFC

4.2 Application documents

Registration of OFC / approval of establishment of sub-fund

Application Form

- separate forms to be used for public and private OFCs
- to be signed by proposed director/ senior executive of proposed investment manager, duly authorised by the applicant

Information Checklist

- separate forms to be used for public and private OFCs

Instrument of Incorporation

- to be signed by all of the first directors
- templates for both private and public OFCs available on SFC website for reference

SFC's Fees

- registration fee for private OFCs
- application for authorisation fee for public OFCs (no separate fee for registration of public OFCs)

4.2 Application documents

For incorporation by CR and business registration by IRD

Incorporation form (Form OFCNC1(SFC))(to be signed by any director of the OFC)

A copy of the Instrument of Incorporation

Notice to Business Registration Office (IRBR3)

Cheque for incorporation fees, business registration fee and levy payable to CR

“One-stop” workflow

Documents to be submitted to SFC prior to issuance of notice of registration

SFC to send to CR together with notice of registration

4.4 Instrument of incorporation

Contents

- i Must include the mandatory provisions under the SFO and comply with the OFC Rules and OFC Code, and SFC Products Handbook (for public OFCs), e.g.

Objects of the OFC must include a statement on its operation as a collective investment scheme

The kinds of properties in which the OFC invests

Corporate administrative matters of the OFC, eg. procedures and notices for holding meetings, creation of shares and the rights attached to them

A statement that the company is an open-ended fund company with variable share capital

Indicative templates (including the mandatory and optional provisions) are available on SFC's website for reference

- i The indicative template provides the baseline contents. An OFC may include other provisions provided that they do not contradict the required contents

4.5 Key operators – Directors

An OFC must have at least two directors, who must be

- ï natural persons
- ï aged 18 or above
- ï not an undischarged bankrupt unless with the leave of the court

At least one of the directors must be an independent director

- ï OFC Code: independent director must not be a director or employee of the custodian

Directors must delegate investment management functions to the investment manager by an investment management agreement

A non-resident director (i.e. a director whose usual residential address is outside Hong Kong) must appoint a process agent to receive any process or notice

- ï an individual whose usual residential address is in Hong Kong;
- ï a company; or
- ï a firm of solicitors or certified public accountants (practising)

4.5 Key operators – Directors

Eligibility:

- ï The experience and expertise of the persons appointed as directors, taken

4.6 Key operators – Investment manager

Eligibility:

- ï Must be registered or licensed for Type 9 (asset management) regulated activity
- ï Must be and remain fit and proper, at and after the registration of the OFC

The investment manager is expected to:

- ï Have sufficient experience, expertise and competence in managing the asset types in which the OFC will invest
- ï Carry out investment management functions of the OFC in accordance with the instrument of incorporation and investment management agreement
- ï Fulfill the duties and functions in compliance with applicable laws and regulations (including the Fund Manager Code of Conduct the Code of Conduct for Persons Licensed by or Registered with the SFC, the Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the Securities and Futures Commission, the Guideline on Anti-Money Laundering and Counter-Financing of Terrorism (For Licensed Corporations) and the Guideline on Anti-Money Laundering and Counter-Financing of Terrorism (For Authorized Institutions))

Documents to support the appointment application:

- ï Information in relation to the applicant having registered or licensed for Type 9 (asset management) regulated activity
- ï Information in relation to the applicant who is in the process of applying for a registration or licence for Type 9 (asset management) regulated activity, for example when the application is made

4.7 Key operators – Custodian

Eligibility

- For public OFCs, same requirements as to the type of entities and capital requirements as those under the UT Code; and
- For private OFCs, (i) same requirements as to the type of entities and capital requirements as those under the UT Code; or (ii) a licensed corporation or registered institution licensed or registered for Type 1 regulated activity which meets eligibility criteria under 7.1(b)(ii) of the OFC Code

Duties of custodian

- Statutory duty to take reasonable care, skill and diligence to ensure the safe keeping of the scheme property of the OFC that is entrusted to it (same for sub-custodian)
- Proper segregation of assets
- Safe-keeping and record keeping of assets
- Sufficient experience, expertise and competence in safekeeping the asset types in which the OFC invests
- Exercise due care in the selection, appointment and ongoing monitoring of its delegates, including sub-custodians
- Internal controls:
 - Public OFC – same as those under the UT Code
 - Private OFC – OFC directors to review the adequacy of the custodian's internal controls which should be commensurate with the OFC's nature, scale, complexity and underlying investments - audit certificate not mandatory

A non-Hong Kong custodian (i.e. a custodian incorporated outside Hong Kong) must have a process agent to receive any process or notice

- Exception: a non-Hong Kong custodian that is a "registered non-Hong Kong company" as defined in the CO, since the CO already provides for a local authorised representative for service of documents

4.8 Offering documents

Public and private OFCs:

Must comply with baseline disclosure requirements in the OFC Code, for example:

General Principles: disclosure should be clear, concise and effective; ongoing disclosure of information shall be disseminated in a timely and efficient manner

Whether the OFC is a private OFC or a public OFC

Its nature as an OFC with variable capital with limited liability

For an umbrella OFC, statement on the segregated liability between sub-funds and warning regarding the enforceability of such segregation in foreign courts

Circumstances for cessation of office of key operators and removal procedures

Custody arrangements of the OFC's property and associated material risks

Termination: summary of circumstances for termination, party who may apply and any shareholders' approval required

Manner in which shareholders may obtain the OFC's information and make enquiries

Public OFCs

Must also comply with the SFC Products Handbook

Private OFCs:

Must also disclose the investment scope and restrictions

Must contain clear disclosures on all material risks specific to the type and nature of assets in which the OFC is invested, in particular where the OFC invests 10% or more of the GAV of the OFC in non-financial or other less common asset class(es)

OFC to send the offering document to SFC for filing as soon as practicable following issuance by the OFC

In the case of changes to the offering documents, should be filed with the SFC within 17 7 days from date of issuance of the revised offering documents

5. Post-establishment of an OFC

5.1 Changes requiring SFC's approval

All OFCs

- (A) Change of name of an OFC or its sub-fund**
- (B) Appointment of key operators (directors, investment manager and custodian):**
 - ï early consultation with SFC regarding change of key operators is encouraged
 - ï for directors, early consultation is especially encouraged where a change may impact on the OFC's compliance with the requirement to have at least 2 directors including at least 1 independent director
- (C) Establishment of sub-funds**
- (D) Termination of the OFC or its sub-fund**

Public OFCs

Compliance with the Code on Unit Trusts and Mutual Funds as well

5.4 Auditor and financial reports

Eligibility and cessation of office requirements: largely similar to those under the CO

- ï Only ãpractice unit under the Professional Accountants Ordinance (Cap. 50) is eligible for appointment
- ï Outgoing auditor must give a statement of circumstances connected with the resignation that should be brought to the attention of shareholders or creditors, or if there are no such circumstances, a statement to that effect

The OFC must prepare an audited annual report for each financial year

- ï On application by an OFC, the SFC may exempt the directors of the OFC from such requirement if it has not been launched and has no investor (see OFC FAQs Question 21A)

Accounting standards under the OFC Code:

- ï All accounts must be prepared in a manner compliant with Hong Kong Financial Reporting Standards or International Financial Reporting Standards
- ï Other accounting standards may be considered on a case-by-case basis

Guidance on contents required for financial reports of private OFCs are set out in the OFC Code (*Note: public OFCs to comply with the UT Code*)

Interim report not a mandatory requirement for private OFCs

5.6 Termination by application to the SFC

Key steps

Submit a termination proposal with an explanation of the proposed arrangements with:
 a solvency statement approved by the board of directors confirming ability of OFC to
 meet liabilities within following 12 months
 OFC must **make a termination notice to shareholders** (Share applications only required for
 public OFC according to the UT Code), following which the OFC should no longer be
 marketed and shall not accept new subscriptions

After realization of assets, settlement of liabilities and distribution of proceeds to
 shareholders, an OFC may **make an application to the SFC for cancellation of
 registration** enclosing:

the final accounts of the OFC accompanied by the auditor's report;

a declaration signed by the OFC (guard and the investment manager) confirming completion of
 realization of assets and distribution of proceeds

5.7 SFC filings

Various filings have to be made with the SFC:

- Annual report
- Interim report (if any)
- Offering documents
- Details of process agent appointed by an overseas director or custodian
- Notice to SFC of a resolution to remove a director
- Cessation of investment manager or custodian
- Alteration of instrument of incorporation
- Statement of circumstances issued by auditor or custodian
- Winding up notifications

Public OFCs have to comply with the requirements in the UT Code

5.8 Corporate filings



Various changes of OFCs are required to be reported to the CR, for example:

- ï Change of company name
- ï Change of address of registered office
- ï

7. Practical tips and common misconceptions

Investment managers

Q: Can an OFC have an offshore investment manager which sub-delegates the investment management functions to a Type 9 licensed corporation?

- i The investment manager of an OFC must be an intermediary licensed / registered for Type 9 regulated activity
- i The investment management functions can be further sub-delegated to an offshore investment manager
- i The investment manager shall exercise due care in the selection, appointment and ongoing monitoring of its delegate

7. Practical tips and common misconceptions

Investment managers

Q: Can the investment manager of an OFC be an OFC director?

- ï The OFC must have at least two individual directors, with at least one independent director, who must not be a director or employee of the custodian
- ï Directors / responsible officers of the investment manager can be OFC directors

Q: Can the investment manager of an OFC also act as the custodian?

- ï The custodian must be a separate legal entity from the investment

7. Practical tips and common misconceptions

Investment managers

Q: Is it more onerous for investment managers to operate private OFCs than offshore fund structures as private OFCs are regulated?

7. Practical tips and common misconceptions

Custodians

Q: Can multiple sub-custodians be appointed?

- ï Custodians can delegate their custody tasks to one or more sub-custodians ï i.e. appointment of multiple sub-custodians is permitted
- ï A custodian shall exercise due care in the selection, appointment and ongoing monitoring of its delegate(s)

7. Practical tips and common misconceptions

Custodians

Q: Can overseas prime brokers act as custodians for private OFCs?

- ï These entities are already currently eligible to act as custodians for private OFCs if they meet the requirements in 4.2(d) of the UT Code

Structure

Q: Can a public umbrella OFC house a private sub-fund?

- ï A public umbrella OFC may have both publicly-offered and privately-offered sub-funds

Q: Can a closed-ended fund adopt an OFC structure?

- ï A "closed-ended" fund (ie funds which are subject to redemption restrictions) may use an OFC structure
- ï SFO enables an OFC to have variable capital and does not preclude an OFC from imposing redemption restrictions

7. Practical tips and common misconceptions

OFC application

Q: Whether an OFC application must be submitted by a solicitor or law firm?

- ï There is no requirement that an application for registration of OFC must be submitted by a solicitor or law firm

8. Appeal and benefits of the OFC regime

Cost-savings over offshore structure

- ï Saves management time and costs by dealing with one jurisdiction instead of two
- ï Avoid extra offshore layer of service providers
- ï Public OFCs: No new fees ï only the existing fees for public funds
- ï Private OFCs: Basic registration and post-registration fees on per change basis

Caters for different types of funds

- ï The OFC can be used for public, private, open-ended, closed-ended, listed or unlisted funds

Tax incentives

- ï Public OFCs: enjoy same profits tax exemption as other SFC-authorised public funds
- ï Private OFCs: enjoy profits tax exemption since roll out of the regime in July 2018, enhanced tax exemption regime commenced on 1 April 2019 (**see Appendix**)

8. Appeal and benefits of the OFC regime

Facilitates international fund distribution

- ï Corporate funds are more popular with investors internationally

Mutual recognition of funds

- ï OFCs eligible under the scope of MRF arrangements

8. Appeal and benefits of the OFC regime

Fast set-up

- ï One-stop approach: submit establishment documents to SFC only, no need to submit separately to the CR or Inland Revenue Department
- ï

8. Appeal and benefits of the OFC regime

9. Re-domiciliation mechanism

Background

To create a commercially viable and facilitating mechanism with legal and tax certainty for foreign corporate funds to re-locate to Hong Kong

Further develop fund administration and ancillary services to bring more jobs and business opportunities to the local fund and professional services industries

Conversion from unit trusts to OFCs already possible with no restriction on the restructuring of unit trusts into OFCs

The legislative framework for re-domiciliation came into operation in November 2021

9. Re-domiciliation mechanism

Benefits of re-domiciliation to Hong Kong

Existing corporate identity, continuity and track record can be preserved

OECD economic substance requirements i higher costs for offshore funds

Saves management time and costs i avoid extra offshore layer of service providers

Stamp duty savings and profit tax treatment

- i No stamp duty will arise

- i Same profits tax position as newly formed OFCs

Strong community of investors and professional service providers, proximity to Mainland China and active IPO market

9. Re-domiciliation mechanism

Registration by way of re-domiciliation process

Same key registration requirements as those for registering a newly-established OFC under the SFO and the OFC Rules

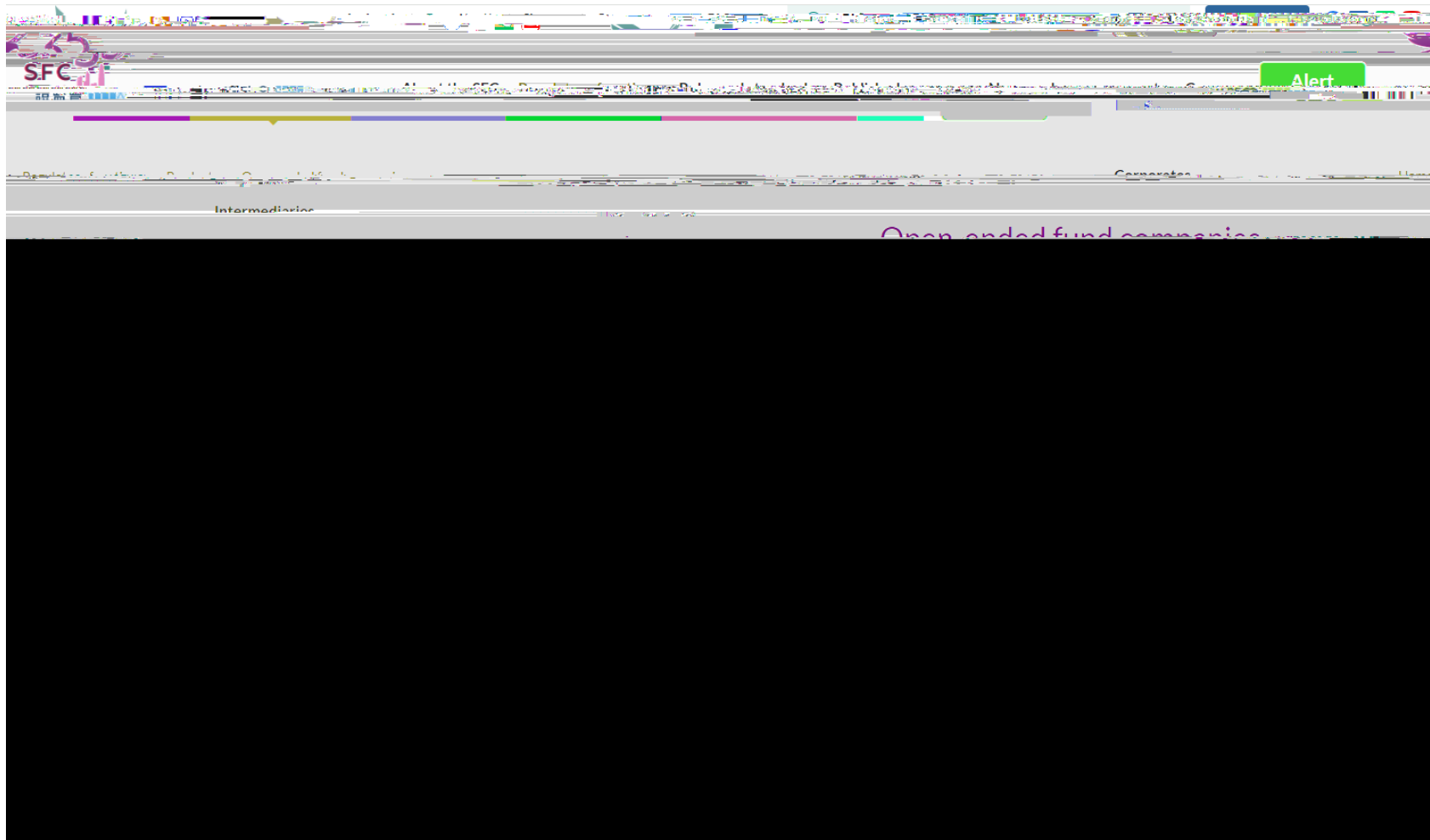
All documents to be submitted to SFC, for example:

- ï copy of certificate of incorporation
- ï constitutive document
- ï directors' confirmation of certain matters (eg solvency of fund)

The fund must de-register in its place of incorporation within 60 days after issue of the certificate of re-domiciliation

10. Further information

Dedicated webpage for OFCs on SFC's website:



Laws and Regulations

- İ SFO (see Part IVA on OFC)
- İ OFC Rules
- İ OFC Code
- İ Products Handbook

11. Appendix: enhanced tax exemption conditions for private funds (effective since 1 April 2019)



Profits tax exemption available for onshore and offshore funds alike

Enhanced profits tax exemption for OFC:

- ï No more “non-closely held” test (i.e. minimum number of corporate and individual investors)
- ï Expanded classes of transactions that are exempted from profits tax
- ï Clearer conditions for exemption regarding investment in private companies

Major breakthrough: profits tax exemption applies regardless of the domicile, structure, capital and size of the private fund

Profits tax exemption eligibility for profits generated from investment in private companies by private funds broadbrush overview



No



