



Hubbis Wealth Management Forum

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Agenda

- Hong Kong vs Singapore - does it matter?
- Regulatory “hot buttons”
- Accessing investors and capital
- What is the real PRC landscape?



Geo-politics

- Not a common market place
 - Different legal systems, regulators and languages
 - No degree of uniformity in regulation like EU
 - No real commonality of approach
 - No generally accepted existing definition of compliance
 - No single reference point for financial institution
- Regulatory convergence unlikely
 - Cultural and language differences
 - Disparity between emerging and developed economies
 - Legislation
 - Regulatory and firm infrastructure
 - Corruption

Hong Kong vs Singapore

- Hong Kong
 - Independent transparent securities regulator
 - Predictable licensing process with no exemptions
 - Very aggressive enforcement regime
 - Weaker bank secrecy rules
 - New AML rules
- Singapore
 - Central regulator with nation building agenda
 - Strong bank secrecy and AML rules
 - Difficult and opaque licensing process
 - New fund manager licensing regime
 - New predicate crime laws on tax
 - Better regime for external asset managers

Regulatory Radar

- Mis-selling
- Insider dealing and market abuse
- Risk management procedures
- Investor categorisation
- Fund authorisation
- AML
- Conflicts of interest
- Quality of product materials and disclosures

Hong Kong

Hong Kong Overview

10 Types of Regulated Activities	
Type 1	Dealing in securities
Type 2	Dealing in futures contracts
Type 3	Leveraged foreign exchange trading
Type 4	Advising on securities
Type 5	Advising on futures contracts
Type 6	Advising on corporate finance
Type 7	Automated trading services
Type 8	Securities margin financing
Type 9	Asset management
Type 10	Credit rating agencies

Hong Kong Overview

Types of Licences / Registrations	
Corporation	<ul style="list-style-type: none">• Full licence
Individual	<ul style="list-style-type: none">• Full licence• Provisional licence
Corporation / Individual (Types 1, 2, 4, 5, 6)	<ul style="list-style-type: none">• Temporary licence (< 3 months)
Registered institution	<ul style="list-style-type: none">• Certificate of registration

Banking Regulation

- HKMA
 - Banking regulator
 - Prudential / CAMEL supervision
- Banks undertaking SFC regulated activities
 - Require SFC licences
 - Appointed persons to hold SFC licences
 - Subject to SFC examinations / inspections
- Joint and separate enforcement powers
 - Lehman Brothers mis-selling cases jointly investigated
 - SFC more aggressive enforcement regulator

Hong Kong Overview

- Individual or corporation carrying on RA in Hong Kong must be licensed by SFC
 - Overseas firms actively marketing to Hong Kong investors need license
- Persons can be licensed for more than one RA
 - Must pass the Fit and Proper test to be licensed
- Corporation
 - 2 responsible officers and 1 must be executive director
 - 1 RO available at all times to supervise business
 - Capitalisation of HK\$150,000 upwards
 - Licensing conditions
 - On-going obligations (FRR, codes, annual returns and accounts,

Hong Kong Licences

- Type 9 – asset management
 - Managing a portfolio of securities and futures for another
- Type 1 – dealing in securities
 - Dealing in securities
 - Inducing someone to deal in securities
 - Attempting to induce someone to deal in securities
- Type 2 – trading in futures
- Type 4 and 5 – advising on securities / futures
 - Independent research
 - Remuneration from the advisory
 - No move YET to fees for advice

Insurance Issues

- Insurance companies regulated by Insurance Authority
- Sales of insurance products self regulated
- SFC and insurance linked savings schemes
 - Decided most are not a security
 - Now sold by unlicensed insurance agents
- Insurance component to wealth management
 - Require membership of insurance regulator
 - Poor compliance and poor oversight
- Problems with expat financial planners

Offering Fund Products

- Separate registration regime for funds to be sold in Hong Kong
 - Complex and lengthy process
 - SFC views on UCITS IV
- Full retail registration required unless offer within safe harbour
 - Private placement
 - High minimum subscription
 - Small offer
 - Wholesale offer only
- Hong Kong domiciled funds

SMP Funds

SFC Product Suitability

- Review of selling practices
- Complex funds
 - Incorrect assumptions about use of derivatives in funds
- Failures detected
 - Not all firms did due diligence on SFC authorised funds
 - Reviewed reputation, track record and financial standing of fund houses only
 - Diligence on funds limited to information on fund platform not independently checked
 - Use of risk ratings for funds from research company based on 3 year annualised volatility without independent due diligence
 - Inadequate records of assessments done

Management and Oversight

- Inadequate management oversight
 - Transactions involving risk mis match not detected by Head of Sales solely responsible for directly supervising selling activities of 70 sales staff
 - Detection failure attributable to inability of single supervisor to exercise effective supervision over large number of sales staff
- Inadequate documentation
 - No guidance to sales staff to document rationale underlying investment recommendations to clients
 - No written guidelines on how to conduct suitability assessments
 - Individual investment transactions subject to review and approval by supervisory staff but no clear guidance to them of approval criteria

RBC and Product Suitability

- RBC Investment Management fined HK\$4 million for investment advice to clients on non-SFC authorized funds from Nov 2006 - Jul 2008
 - Not provide adequate guidance to staff on conducting due diligence on funds before making investment recommendations
 - Relied on Singapore office to conduct due diligence on investment products but no record of due diligence & not aware of scope and extent
 - Not provide adequate practical guidance to RMs in providing investment advice or recommendations
 - Not have any measure for overall risk of investment products sold
 - RMs not ensure advice provided would best fulfill clients' investment objectives

RBC and Product Suitability

- RMs not record or document product suitability assessment undertaken to demonstrate that RBC was reasonably satisfied that investment products recommended suitable for client
 - Not adequate procedures requiring RMs to document investment advice and underlying rationale and provide copy to clients
 - RBC's supervision of RMs not effective in ensuring recommendations to clients suitable and reasonable
- Failed to ensure investment recommendations based on thorough analysis and reasonable in circumstances
 - RBC's breaches prejudicial to interest of investing public
 - Repurchase offer, fine and special reviewer appointed

CIC Investor Services

- CIC publicly reprimanded and fined \$4 million
- SFC identified that CIC failed:-
 - to evidence clients had met requisite requirements under Securities and Futures (Professional Investor) Rules
 - to adequately assess investment experience of its clients as required under Code of Conduct
 - to obtain signed declarations from clients who agreed to be treated as professional investors as required under Code of Conduct
 - to maintain adequate documentary records of investment advice given to clients

CIC Investor Services

- Specific issues in 420 clients:-
 - No custodial or accounting statements as to value of portfolios
 - < 50% of clients classed as PIs not meet HK\$8 million test
 - Treated clients as PIs in all products
 - Only 10 clients meet requirement to have 40 transactions p.a. in derivatives (in fact in any products)
 - <90% did not have 2 years of trading experience
 - Still classified clients as having “high” level of experience
- Letter to all clients seeking agreement to be treated as PI
 - CIC claims 184 clients responded
 - Only 4 documentary agreements located

Julius Baer Hong Kong

- SFC reprimands and fines Julius Baer HK\$3 million
- SFC investigation revealed that Julius Baer, which is licensed to provide services only to professional investors, failed to
 - Take adequate steps to identify clients as professional investors before treating them as such
 - Conduct an annual confirmation as to whether clients continued to fulfill PI requirements
 - Maintain adequate written records of investment advice given to clients

“The difference between professional investors and ordinary retail customers is a profoundly important one. Firms that do not classify customers properly, in strict compliance with the requirements, impose undue risks on those customers. The SFC will not hesitate to take deterrent action in these cases,” said Mark Steward

Inadequate Disclosure of Fees

- SFC reprimanded Société Générale for failings in internal controls in Wealth Management activities
- SG to reimburse affected customers full value of fee together with interest (US\$11 million)
- 3,000 transactions from 2003 – 2006
 - Customers paid or received different price for OTC products from actual price transacted for them by SG
 - Difference retained by SG as a fee
 - Fee variable and in some cases excessive
 - SG not disclose fee to customers
 - Fee not disclosed as commission in contract notes
 - Inadequate conflicts and internal control procedures

Singapore

Singapore Licences

- 2 relevant pieces legislation
 - Fund management - SFA
 - Advising on securities – FAA
 - Marketing CIS - FAA
- Need CMS licence for fund management
 - Retail LFMC or Accredited and Institutional Investor LFMC
- Registered Fund Management Company
 - Subject to business conduct regulations
 - Fall within regulatory purview and supervisory oversight of MAS
 - Not > 30 qualified investors (15 funds or LPs) AND total value of assets management not >\$250 million
- Financial adviser or exempt financial adviser
- CMS licence for dealing in securities

- 2 directors with 5 years experience
 - At least 1 executive director resident in Singapore
 - Nominee directors not sufficient
 - 1 director to be nominated as CEO
 - CEO of LFMC must declare 5 years fund management experience
- Relevant professionals
 - At least 2 with 5 years experience
 - Directors, CEO and representatives
- Assess relevance of experience in context of role
 - Director / CEO to have managerial / supervisory experience
- Not cumulative
 - Same 2 persons can perform all roles if competent

Base Capital

- 3 base capital levels
 - Managing retail CIS – S\$1,000,000
 - Retail fund management (non CIS) – S\$500,000
 - Other fund management – S\$250,000
 - MAS recommends buffer is held – no guidance on amount
- Maintain base capital above minimum at all times
 - Demonstration typically by maintenance of monthly management account
 - Budgets to be produced to predict any losses that may arise
- Ordinary shares + irredeemable and non-cumulative preference shares - unappropriated losses (or + profits) -dividend declared - interim loss.

Risk Capital

- LPMC's maintain financial resources of at least 120% of risk based capital requirement at all times
- RBC is greater of:
 - S\$100,000;
 - 10% of “annual average adjusted gross income” for past 3 years;
 - 5% of “annual average gross income” for past 3 years.
- Consultation Paper on Regulatory Capital Framework
 - Calculate TRR as sum of counterparty / position / operational / large exposure / underwriting / firm-specific risk
 - Applicable to FCM if average adjusted assets in each quarter of year > lower of 10 times minimum base capital requirement or 5 times total positive financial resources

Compliance

- CEO and directors ultimately responsible for compliance
- Retail LFMC
 - Independent dedicated compliance function in Singapore
 - Combine with non competing role – in house legal
- A/I LFMC >S\$1 billion AUM
 - Only engaged in research / advisory
 - Compliance support from holdco or overseas affiliate
- A/I FMC <\$1 billion AUM / RFMC
 - Compliance independent from front office eg COO / CFO or holdco / affiliate
 - No group compliance – competent compliance consultant & knows Singapore rules
- CO – ten year employment history

Risk Management

- Framework must identify, address and monitor risks associated with customer assets it manages
- MAS Guidelines on Risk Management Practices
 - ols
- At a minimum framework to cover
 - **Governance, independence competency risk management function**
 - **Measurement of risks associated with customer assets**
 - **Timely monitoring and reporting of risks to management**
 - **Documentation of risk policies, procedures, reports**

- External audit For LFMC and RFMC
- Financial audit
- Compliance audit component where auditor to report on FMC's compliance with
 - Restrictions in clientele and AUM
 - Minimum base capital requirement
 - Key business conduct rules such as independent custody, valuation of clients' assets and client reporting
 - Implementation of risk management framework
- Internal audit or independent review annually

Fund Offering in Singapore

- Full fund registration
 - Luxembourg and Dublin UCITS funds
 - Requires substantive physical local fund management operation
- Restricted fund registration
 - Any foreign fund where manager is suitably licensed
 - Offer to unlimited number of accredited investors
 - Private banking model
- Private placement
 - High minimum subscription
 - Small offering
- New FAIR dealing consultation paper – MiFID equivalent

Investors

Professional Investors

- Means test
 - Not specify acceptable method to establish investor worth
 - Not rule out self certification but only when occasion is appropriate
- Person to meet requirements at relevant date
 - Date of document issue vs call made vs offer made
- Do you have to establish worth prior to marketing?
 - Contractual question as to when offer is made
- For firms restricted to dealing with professionals
 - Do regulators look through to investor education efforts etc
- Client opt in / opt out provisions

Hong Kong PI Issues

- Assess and reasonably satisfied person is knowledgeable and sufficient expertise in product and market
 - Type of product person has traded
 - Frequency and size of trades (PI trade not < 40 transactions in year)
 - Dealing experience (PI active in relevant market for at least 2 years)
 - Knowledge & experience in product
 - Awareness of risks involved in trading product / market
 - Separate assessment required for different products / markets
 - Annual confirmation
- Firm to assess extent fund product uses derivatives
 - Investor not an expert in derivatives not automatically mean investment in fund using derivatives not suitable
 - SFC approval not make product automatically suitable

MAS PI Issues

- A/I FMC only deal with Qualified Investors
 - Fund offered only to accredited investors
 - Look through fund to prove investors are accredited
- A/I LFMCs and RFMCs not target retail investors through investment structures circumvent clientele class restrictions
 - Mean managers of CIS authorised in Singapore need to be retail FMCs even if only deal with distributors?
- Employees of A/I LFMCs and RFMCs to meet definition of accredited investor or cannot participate in fund

PRC

PRC QDII and QFII

- QDII programme
 - Formal mechanism for institutional investment outside PRC
 - First obtain QDII licence from relevant agency then quota from SAFE
 - Considering new programme for HNWI to buy Hong Kong stocks
 - At March 2012 96 QDII licences with total quota US\$75.25 billion
- QFII programme
 - Foreign investors to obtain access to PRC capital markets
 - December 2012 investment quotas totaling \$37.44 billion to 169 foreign entities
 - Criteria including \$5 billion in AUM but thresholds being lowered and hedge funds /PE funds to be allowed
- Qualified individuals
 - Programme to be revived to allow PRC citizens to invest in HK

PRC QDII and QFII

■ RQFII

- Hong Kong funds regulated by SFC denominated in RMB
- At October 2012 21 institutions received RMB48 billion in quotas
- RMB22 billion quota unclaimed but increase to RMB270 billion

■ QDLP programme

- Shanghai pilot programme
- Allow domestic LPs to invest into offshore funds as feeders
- Primarily PE and hedge funds at this stage

■ China “sunshine” funds

- PRC manager / offshore adviser RMB pools set up by trust companies
- HWNI over RMB 1 million

■ Off balance sheet bank wealth management pools

Permitted Offshore Investment

Commercial banks	Overseas fixed-income products (e.g. bonds, notes), structured and derivative products and certain equity products (e.g. stocks, public funds), but they cannot invest in commodity derivatives, hedge funds and securities below 'BBB' level.
Security companies and funds managers	Overseas stocks, bonds, depository receipt, real estate investment trust, public funds, structured products and other financial derivatives.
Insurance companies	Invest foreign exchange funds in overseas money market products(e.g. bank bills ,negotiable certificates of deposit), fixed income products, depository receipt, and certain equity products (e.g. stocks, stock funds)
Trust companies	Overseas money market products (e.g. bank deposits, depository receipt), bonds and financial derivative products permitted by CBRC.

Fund Offering in PRC

- Potentially private placement of funds
 - CSRC guidance only
 - Not more than 200 persons
 - Marketing materials in English only
 - Primarily used for PE funds



PRC – Opportunities

- Average Daily Trade Volumes
 - Hong Kong - USD7 billion
 - Shanghai / Shenzhen - USD30 billion
 - NYSE/NASDAQ – USD200 billion
- Velocity
 - Hong Kong – 60%
 - Shanghai – 170% (higher than NYSE)
 - Shenzhen – 400% (NASDAQ at 350%)
- Separate liquidity pools – onshore and offshore via HK
 - 50% Hong Kong trades are institutional international
 - 12-20% unofficial China money
- Projections for 2015
 - Currently 5 largest banks control 80% of financial liquidity
 - Corporate bonds to increase in value to RMB 15 billion
 - Equity Capital Market – RMB 66 billion (doubling)
 - Total FUM – RMB 9 trillion (tripling)
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PRC – Challenges & Initiatives

■ Challenges

- Lack of disintermediation and lack of investable products
- Not yet full currency convertibility
- Accumulation of 10% CGT and unclear on legal status
- Impact of turnover tax – 5% on each transaction

■ Initiatives

- HK RMB products
- Dual listings in HK in RMB to achieve full fungibility
- SFC added China Futures Exchange to list of recognised exchanges
- Use of HK as domicile for LPs to invest in China RMB onshore funds
- New CSRC rules for sponsors of domestic listings to improve their DD process
- Favourable DTA between Hong Kong and PRC
- CIRC new rules allowing investment of 5 – 10% in alternative managers
- Introduction of index futures and short selling programme

■ Changes to QDII programme

- More local asset managers and brokers to be permitted

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