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Reminders for advertisements of authorised funds

Alwyn Li, Eve Leung and Lawrence Yeung

The SFC conducts surveillance on marketing materials of authorised funds. Fund managers are reminded of their obligations to ensure compliance with applicable SFC requirements, including but not limited to, the [Code on Unit Trusts and Mutual Funds](#), [Advertising Guidelines](#) and the SFC's [FAQ on Advertising Materials](#).

Below is a summary of some of the key compliance issues:

- 1) An advertisement of an authorised fund should contain an upfront risk disclosure box (**RDB**) highlighting all the key risks of the fund. The box must be presented upfront and prominently. The risk disclosures should be clearly seen and of appropriate prominence. The SFC pays particular attention to the presentation of benefits and returns in advertisements. In particular, returns and dividend yields should not be presented disproportionately larger than the risks of the fund. The SFC expects that the font size of the risk disclosures should be comparable to the main text. Unfortunately, the SFC does not provide any specific requirements or guidance in respect of appropriate font size and fund managers need to adopt a holistic approach to ensure that the risk disclosure, in terms of overall impression, is reader-friendly and “eye-catching”, especially for large items e.g., displays in the MTR.
- 2) For advertisements which highlight dividend payments or distribution features, the disclaimers regarding the payment of dividends out of capital should be disclosed in the RDB if applicable. If the fund does not offer a fixed dividend arrangement, the disclosed rate of dividend payments should be accompanied by the SFC-prescribed disclaimers that the amount of dividend or the rate of distribution is not guaranteed.
- 3) A substantiated prospective yield may only be allowed in an advertisement if the fund invests substantially in fixed income securities, money market instruments or other investments that provide regular and stable distributions.
- 4) For a newly launched fund which does not guarantee or make dividend payment at a fixed rate, it would generally not be acceptable for the fund to include prospective dividend yield in its advertisement unless the above condition is met.
- 5) Lucky draws, gifts and other non-fee related incentives are generally prohibited.

If the SFC has any concern about an advertisement of an authorised fund, the fund manager will likely be required to submit all the advertisements of the relevant fund during a specific period to the SFC for review. The fund manager may also be required to cease publication of the advertisement as soon as possible.

The SFC launches a new online e-IP system for investment products

Jack Hung and Eve Leung

On 29 July 2024, the SFC launched a new online application/submission system, namely e-IP, on its Web-based INteGrated Service (**WINGS**) portal to facilitate new product applications, post-authorisation/registration submissions and regulatory filings of investment products (**IP Submissions**) to the Investment Products Division (**IPD**). The e-IP system serves as a portal for IP Submissions of investment products including but not limited to unit trusts, mutual funds, open-ended fund companies, pooled retirement funds, mandatory provident fund (**MPF**) products and investment-linked assurance schemes.

There is a three-month transition period during which the SFC continues to accept IP Submissions via existing arrangements. Starting from 30 October 2024, all IP Submissions must be made via the e-IP system.

In order to utilise e-IP, all product issuers (which are e-IP Managing Companies) should activate their e-IP Managing Company Account set up by the IPD and nominate at least one e-IP Administrator to operate the account. New product issuers should contact the IPD for the establishment of their new accounts prior to making their first product applications.

With the implementation of e-IP, existing template application forms and filing forms for IP Submissions will be replaced by smart-forms, while other confirmations and annexures remain in the format of word documents. The SFC will issue take-up letters and authorisation letters via e-IP. However, any correspondence / communications with the IPD during the vetting process will continue to be done via the existing e-mail arrangements.

The e-IP Administrators can grant permission to their staff and/or external legal advisors to make IP Submissions on behalf of the e-IP Managing Company. Such delegation can be made at the company level or product level and can be changed from time to time.

The e-IP system provides flexible fee payment options in addition to cheque payments. It also provides more flexibility with the signing of documents. The relevant signatories can either sign by physical signature or e-signature on the PDF forms generated from e-IP. Alternatively, unsigned documents can be submitted via e-IP with online confirmations from the submitter that the documents / confirmations are true and accurate.

Product issuers should get familiar with the e-IP system and can refer to the user guides ([link](#)) and online demo clips ([link](#)) on the SFC website for more details. Product issuers should review and consider their internal procedures and controls in light of the e-IP implementation, in particular, how the delegation arrangements and/or granting of access rights on e-IP should be done.

As a legal advisor, we have established an e-IP Advisory Firm Account in WINGS to provide assistance to product issuers, and we have already made IP Submissions (e.g. making new fund applications and filing of notices and offering documents) on behalf of our clients via e-IP.

The SFC's Asset and Wealth Management Activities Survey 2023

Taylor Hui and Isabella Wong

On 12 July 2024, Hong Kong's Securities and Futures Commission (**SFC**) published the findings of its annual Asset and Wealth Management Activities Survey for 2023 (**Survey**).

Overall, the asset and wealth management industry in Hong Kong saw positive growth in 2023, with a 2.1% year-on-year increase in its assets under management (**AUM**) to HK\$31,193 billion. This was driven by a 342% surge in net fund inflows to HK\$389 billion. Specifically:

- The AUM of Mainland headquartered licensed corporations (**LCs**) and registered institutions (**RIs**) in Hong Kong increased 4% year-on-year to HK\$2,678 billion, a 50% rise since 2019. Their net fund inflows grew 16% to HK\$153 billion.
- The net asset value of Hong Kong-domiciled funds authorised by the SFC rose 5% to HK\$1,351 billion, with net fund inflows up 93% to HK\$83 billion. The number of registered open-ended fund companies (**OFCs**) also increased 118% to 244.
- Hong Kong remained the world's largest offshore renminbi deposit pool, with Renminbi (**RMB**) deposits totalling RMB1,134 billion as at June 2024, a 135% increase from 2022.

The Survey also highlighted recent developments to facilitate cross-border transactions and strengthen cooperation between the Mainland and Hong Kong financial markets. Such developments include:

- The cross-boundary Wealth Management Connect (**WMC**) scheme was enhanced to expand the scope of products and participants. This will allow Hong Kong-licensed brokers (other than banks) who wish to distribute eligible investment products, i.e. (i) Hong Kong domiciled funds authorised by the SFC and assessed as “non-complex” in accordance with Hong Kong regulations and “low risk to medium risk” by the Hong Kong bank distributing such funds; (ii) bonds assessed as “low” risk to “medium” risk and “non-complex” by Hong Kong banks distributing such bonds; and (iii) RMB, Hong Kong dollar and foreign currency deposits, through the enhanced WMC scheme, but the brokers will need to identify a partner broker in the Mainland. The partnership agreement must clearly define the parties' respective obligations and operational arrangements. Additionally, existing investment account terms and conditions will need to be supplemented with provisions specific to the WMC scheme, such as investor undertakings and the onboarding process. Asset management firms can also expand the range of products offered to Mainland investors. The increased investment quota and eligible product scope will better meet investors' demand for diversified investments, presenting new opportunities for Hong Kong-based fund managers. For details of the enhanced WMC scheme, please refer to our [client alert of 2 February 2024](#).
- The China Securities Regulatory Commission (**CSRC**) announced initiatives to increase capital market cooperation with Hong Kong and improved the Mainland-Hong Kong Mutual Recognition of Funds (**MRF**) scheme. The CSRC has published a public consultation paper on proposed rule amendments to enhance the MRF scheme. The key draft proposals include: (i) Relaxing sales restrictions for recognized Hong Kong funds in the Mainland. Currently, the value of units sold to investors in the host market is capped at 50% of the fund's total assets. This cap will be increased to 80%. (ii) Allowing delegation of investment management functions for recognized Hong Kong funds. Currently, such functions cannot be delegated to a firm outside the home market. After the enhancement, recognized Hong Kong funds can delegate these functions to an overseas entity within the same group, located in a jurisdiction that has a regulatory cooperation agreement with the CSRC. In a reciprocal move, the SFC will also relax the relevant restrictions on recognized Mainland funds accordingly. For detail of the CSRC's proposed amendments, please refer [here](#).

Severe weather trading on HKEX – key issues for fund managers

Ming Chiu Li

On 18 June 2024, the Securities and Futures Commission (**SFC**) issued a circular on the updated arrangements concerning severe weather trading (**SWT**) on the Hong Kong securities and derivatives markets. Effective 23 September 2024 (the “effective date”), on a day with severe weather (**SWT day**), the Hong Kong Exchanges and Clearing Limited (**HKEX**) will maintain normal operations to the greatest extent possible with trading, clearing and settlement services and operations continuing in both the securities and derivatives markets.

In accordance with the SFC's circular, management companies of listed funds will be required to ensure normal operations as far as possible on a SWT day. They should ensure the operational readiness of all relevant fund service providers, closely monitor the funds' operations and activities, and keep investors informed of any material information

concerning the funds as a result of SWT. In view of the SWT arrangement, we note that operators of listed funds have started to conduct system testing to ensure that SWT can be implemented from the effective date.

Fund documentation, particularly definitions concerning business day and dealing day, should be reviewed and amended if necessary, and notification should be given to holders to inform them of related changes. For Hong Kong domiciled funds, a business day is often defined with reference to days on which banks in Hong Kong are open for normal banking business. As bank branches will remain closed on any SWT day, the relevant definition in the fund documents will likely need to be amended, to clearly stipulate the days on which dealing may be conducted going forward.

For unlisted funds, operation on an SWT day is voluntary and should be based on the company's business needs and operational readiness. If the management company chooses to offer dealing on a SWT day, it should amend fund documents and provide notification to investors. A further consideration for unlisted funds is that they are offered through distributors (mainly banks), and therefore management companies should also have regard to the practice of different distributors (both in relation to the transmission of dealing orders and arrangement for settlement of proceeds). Proper disclosure should be made in fund documents to keep investors informed of the arrangements in relation to dealing on a SWT day.

Hong Kong SFC licensing and compliance hints – Financial resources management and compliance with the Securities and Futures (Financial Resources) Rules (FRR)

Elaine Ho

On 3 July 2024, the Hong Kong's Securities and Futures Commission (**SFC**) issued a circular (**Circular**) regarding the governance and internal control standards of licensed corporations (**LCs**) for monitoring the adequacy of financial resources and compliance with the FRR.

The Circular outlines the expected FRR compliance standards.

Required liquid capital deficit incident report

Clients should note the following two changes as set out in the Circular:

1. Expected FRR compliance standards – prescriptive internal control measures

The SFC has set out the following prescriptive internal control measures in relation to the expected FRR compliance standards:

- (a) sound accounting policies and procedures, including month-end and year-end closing procedures, for timely and proper recognition of revenues, accruals and provisions;
- (b) a maker and checker mechanism for the calculation, monitoring and reporting of liquid capital;
- (c) effective processes for ongoing liquid capital monitoring commensurate with the nature, scope, size and complexity of the LC's business activities and operations;
- (d) regular liquid capital projections for preparing and maintaining a sufficient liquid capital buffer;
- (e) a liquidity management framework for handling thin excess liquid capital situations that entails effective alerts, relevant mitigation measures and escalation procedures with clear steps and timelines;
- (f) procedures for ensuring compliance with all relevant notification requirements; and;
- (g) where applicable, clear allocation of scope, roles and responsibilities between the LC and its external service providers regarding outsourced accounting and FRR compliance functions.

2. Reporting deficiency in minimum required liquid capital using prescribed form within three weeks

An LC that incurs a deficit in the minimum required liquid capital (**RLC deficit**) is now expected to submit an incident report to the SFC in the prescribed form (as set out in Appendix B of the Circular) within three weeks from the date of first identifying the RLC deficit.

For the avoidance of doubt, the submission of the incident report in the new prescribed form is not a substitute for the need to notify the SFC of the RLC deficit before the report is submitted. The LC is still expected to notify the SFC of the RLC as soon as practicable, and subsequently submit the incident report to the SFC within three weeks. Furthermore, the LC should immediately cease carrying on the regulated activity for which it is licensed and should notify its clients of the same as soon as practicable.

In addition, the existing requirements to notify the SFC if the liquid capital falls below 120% of the required minimum amount or 50% of the liquid capital stated in its last submitted return still remain the same at “*as soon as practicable and in any event within one business day of becoming aware*” and in writing. There is no prescribed form for the aforementioned notifications.

How can Deacons help?

LC clients are reminded that their “liquid” capital must always exceed its “required” liquid capital under the FRR. Furthermore, LC clients are reminded to abide with the relevant notification requirements to the SFC in relation to liquid capital as applicable.

Deacons regularly advises LC clients on regulatory issues and assists them in implementing internal control measures in relation to financial resources requirements and compliance with the FRR, including the preparation and review of policies and procedures, compliance health-checks and preparation for SFC routine inspections.

Overturning of the US SEC’s Private Fund Adviser Rules

Ethan W. Johnson of Morgan, Lewis & Bockius LLP

The decision

In a unanimous decision published on 5 June 2024, the US Court of Appeals for the Fifth Circuit vacated the entire set of Private Fund Adviser regulations, including amendments to existing rules (collectively, the **Private Fund Adviser Rules**) that had been adopted with great fanfare by the US Securities and Exchange Commission in August 2023. The Private Fund Adviser Rules would have substantially overhauled the US private investment fund industry. The court’s ruling is a welcome result for many private fund advisers in the US who have been preparing for months for the complex and burdensome set of requirements. For private fund advisers with no place of business in the US, even if registered with the SEC, the impact of the Private Fund Adviser Rules and now of their demise has less impact on them because the Private fund Adviser Rules had been interpreted as only applying to US-based private fund advisers.

What's next?

There are two avenues for the SEC to pursue further appellate review: first, the SEC can seek a rehearing before the Fifth Circuit; second, the SEC could seek review by the US Supreme Court within 90 days of the final ruling, which would require the Solicitor General of the United States to petition for a hearing on the SEC’s behalf. As an alternative to pursuing further appeals, the SEC could repropose some or all of the Rules under different legal authority, although that could be challenging in light of the court’s interpretation of the SEC’s authority under the Investment Advisers Act.

Potential for a lasting impact

Although vacated by the Fifth Circuit, the Private Fund Adviser Rules and their underlying principles may nonetheless continue to impact the private fund industry. For example, certain aspects of the Private Fund Adviser Rules and their proposing and adopting releases could serve as instructive guidelines for US and non-US advisers and investors as private fund advisers navigate interpretive issues under the Investment Advisers Act, or—perhaps more likely—could presage attempts by the SEC to regulate through an aggressive approach to examination and enforcement.

Recent publications

[Hong Kong relaxes requirements for Specialist Technology Companies and De-SPAC Transactions for 3 years from 1 September 2024](#)

[AI copyright law reform – data mining exception proposed](#)

[Hong Kong Stock Exchange proposes to further expand the paperless listing regime](#)

[Court finds no apparent bias on arbitrator's part](#)

[No extension of time to set aside order for enforcement of Mainland award](#)

[Court refuses enforcement of Mainland awards in Hong Kong](#)

[Court refuses to stay enforcement of award pending outcome of 2nd arbitration](#)

[Soleh Guidelines continue to apply in RHC O.73, r.10A applications](#)

[Loan agreement arbitration clause did not confer jurisdiction on tribunal to determine dispute regarding related promissory note](#)

[Award set aside due to incompatible appointment procedures in multi-contract dispute](#)

[Thinking inside the \(patent\) box](#)

[Delivery up of documents of insolvent companies to liquidators by former solicitors](#)

[FamilyFocus@Deacons: Series on mental capacity and financial issues – Financial planning for families with special needs children](#)

[Hong Kong Court upholds SPA and rejects attempt to void sale based on s.60 of the Conveyancing and Property Ordinance](#)

[Hong Kong Court of Appeal confirms applicability of Re Guy Lam principles to arbitration clauses and cross-claims subject to arbitration agreement](#)

[The Passage of Deposit Protection Scheme \(Amendment\) Bill 2024](#)

[Adjustments to the Fees in the Second Schedule to the Banking Ordinance](#)

[Revised Core Principles for effective banking supervision](#)

[International Conference on Central Bank Digital Currencies and Payment Systems](#)

[HKMA launches Phase 2 of the e-HKD Pilot Programme](#)

[Enhancements to the Code of Practice on Person-to-Person Marketing Calls](#)

[Refinements to property mortgage lending requirements](#)

[Deposit Protection Scheme \(Amendment\) Bill 2024 gazetted on 3 May 2024](#)

[Anti-Scam Consumer Protection Charter 2.0](#)

[Protecting data when using AI systems – Hong Kong Privacy Commissioner issues new guidelines](#)

[Hong Kong Stock Exchange proposes enhancements to corporate governance requirements for listed issuers](#)

[Art diligence: the key to making informed art investments](#)

[New Requirements on Beneficial Owner Filings in China](#)

[Is your advertising campaign fit for the summer games?](#)

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