

Hong Kong and Australia Sign Declaration to Allow Cross-Border Marketing of Retail Funds

On 7 July 2008, the Hong Kong Securities and Futures Commission (the "SFC") and the Australian Securities & Investments Commission (the "ASIC") signed a Declaration on Mutual Recognition of Cross-Border Offerings of Collective Investment Schemes (the "Declaration"). The Declaration may represent a considerable opportunity for funds based in and currently authorized/registered in either Hong Kong or Australia to source investors in the counterpart jurisdiction. However, the Declaration appears to be of limited utility to funds and managers that are SFC-authorized but based outside of Hong Kong (i.e., most UCITS and US funds offered in Hong Kong and their managers).

Overview

The Declaration seeks to facilitate the cross-border sale of retail funds in the Hong Kong and Australian markets by significantly streamlining the regulatory approval process in each jurisdiction with respect to funds from the other jurisdiction. Currently, both regulators are in the process of developing guidance to support the implementation of the Declaration. To assist Australian funds wishing to take advantage of the Declaration, the SFC issued a circular setting out practical guidelines and intends to issue a "checklist" for Australian funds seeking SFC authorization. Similarly, the ASIC is expected to soon issue a class order providing guidance with respect to its registration criteria for Hong Kong funds.

The Declaration will not apply to funds from either jurisdiction that are "principally aimed" or "marketed" to investors in the other jurisdiction. This requirement, which is borrowed from presently effective Australian regulations, is meant to prevent funds from engaging in regulatory forum shopping. Specifically, neither regulator will permit the streamlined authorization/registration of a fund from the

other jurisdiction if their domestic investors account for more than 30% of the value of the foreign fund. In order to maintain competitive parity, the Declaration provides each jurisdiction with flexibility to adjust this amount should the other jurisdiction impose (or change) limits on the extent of ownership interests that investors in its jurisdiction may have in a foreign fund. The Declaration also provides that fund managers will be responsible for monitoring and ensuring compliance with this restriction, which may be operationally challenging (especially to small managers).

With respect to post-authorization compliance matters, the Declaration clearly provides that each regulator has "unfettered powers and discretion" to regulate marketing and dealing (including requiring that distributors and other intermediaries be licensed in their respective jurisdictions), to issue stop orders and to request documentation and information from funds and their managers.

Implementation

Under the initial framework of the Declaration, the SFC intends to expedite the authorization process for an Australian retail fund if the fund, among other things, is: (i) managed by an ASIC-licensed manager; (ii) registered with the ASIC; (iii) meets certain disclosure, operational and reporting requirements; and (iv) is not principally marketed to investors in Hong Kong. Likewise, the ASIC intends to expedite the registration of a Hong Kong-based retail fund for distribution in Australia if the fund is: (i) “primarily regulated by the SFC and not subject to regulatory concessions applicable because of [its] regulation outside Hong Kong;” (ii) managed by an entity licensed with and primarily regulated by the SFC; and (iii) not principally marketed in Australia.

Over 2,000 SFC-authorized funds are available for investment in Hong Kong. However, the prerequisites applicable to the registration of funds in Australia indicate that managers and funds that are SFC-authorized, but based outside of Hong Kong, may not be able to avail themselves of the Declaration’s accelerated review and registration process in Australia. Most UCITS and US funds that are authorized by the SFC would not appear to qualify for expedited review and registration because they generally are not “primarily regulated by” the

SFC and may be subject to regulatory concessions due to their primary regulation by other regulatory regimes. In addition, managers of these funds often do not hold applicable SFC licenses, nor are they “primarily regulated” by the SFC, as fund authorization in Hong Kong does not, by itself, require licensing of the fund manager. Accordingly, while subsequent regulatory guidance may provide more flexibility to non-Hong Kong based advisers and their funds, a plain reading of the Declaration indicates it is largely intended to be utilized by funds and managers that are resident in Hong Kong and primarily regulated by the SFC.

Dechert LLP will continue to monitor guidance released by the SFC and ASIC with respect to the Declaration, and will inform you as to any significant developments.

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