Vivien Teu & Co LLP
張慧雯律師事務所
有限法律責任合夥

Synopsis Series

Focus on Hong Kong Asset Management

Hong Kong has a well-established asset management and funds industry that has been successful under an open architecture framework. This spans from being accepting of fund managers' overseas qualifications and experiences of different markets to set up in Hong Kong, to being domicile-neutral on the funds that may be offered in Hong Kong on a private placement basis or which may be approved for retail public offer. It is this backdrop that has developed Hong Kong into a financial centre where many asset management firms are set up by international groups and in recent years Mainland China fund houses.

Recently the status quo has been shaken up amidst efforts to maintain and enhance Hong Kong's competitiveness as an international centre for funds, and also as it seeks to further capitalise and stay relevant as the gateway for Mainland China of the People's Republic. There are also developments in the context and environment of international regulatory and fiscal cooperation. In this article we focus on the key attributes and changes that are interesting for asset managers to consider Hong Kong under their global strategy.

Hong Kong investment managers

Conducting business in Hong Kong that engages in the services of asset management – including investment funds management – is subject to licensing and regulatory requirements. To obtain a license from the SFC for carrying on asset management business in Hong Kong, the applicant is required to be a Hong Kong-incorporated company or a non-Hong Kong company registered with the Companies Registry. The requirements and formalities for company incorporation and business registration are relatively minimal and straight-forward in Hong Kong. The most commonly used vehicles for doing business in Hong Kong are private limited companies structured as a company limited by shares. There is a minimum requirement of one shareholder and one director, respectively, but these do not have to be local companies or individuals. There are also no foreign ownership restrictions.

Hong Kong's tax regime operates under the territorial principle of taxation, and which primarily taxes Hong Kong sourced income. The applicable profits tax rate for incorporated businesses is 16.5%, although under current general concessionary incentive the profits tax rate is reduced to 8.25% on up to HK$ 2 million of the assessable profits. There is no general tax levied on dividend income (and no dividend withholding tax, as well as similarly no withholding tax on interest payments from Hong Kong), and no capital gains tax.

While there is no local resident director requirement for a Hong Kong company, it is a requirement for SFC licensed managers to have at least two responsible offers accepted and approved by the SFC as being fit and proper. At least one of the responsible officers should be available at all times to supervise the business (and hence expected to be Hong Kong-based). Further, at least one of the responsible officers of the Hong Kong licensed manager must be an executive director of the company.

In order to be considered as fit and proper to be approved as responsible officers, there are certain competency requirements that cover academic or industry qualifications, industry experience and management experience. Investment management or closely related experience gained in Hong Kong or elsewhere can be recognised to meet the requirements on industry experience, while recognised industry qualifications from jurisdictions such as the United States, United Kingdom, Australia, Canada, Japan and Mainland China are accepted. Managers from other jurisdictions may also qualify on the basis of academic qualifications in place of industry qualifications. It is therefore open for qualified and experienced investment managers from other jurisdictions or markets to apply for approval to become responsible officers. A key (local) qualification requirement that remains necessary to meet is to take the local regulatory framework examination papers to demonstrate a certain expected level of understanding of the Hong Kong legal and regulatory requirements applicable to investment management.

The substantial shareholder(s) of a Hong Kong licensed investment manager is also subject to prior regulatory approval, and the SFC would consider factors such as the financial status, qualifications, reputation and reliability of the proposed shareholder. However, there are no minimum requirements on capital, assets size or assets-under-management on the shareholders. It is this open framework that has enabled many investment management firms of varying background and sizes to set up in Hong Kong, and which allows both established global firms as well as entrepreneurial new managers to compete in this market to offer diverse investment services and products.

Upon becoming licensed Hong Kong managers, an investment manager can engage in investment management and/or fund management business that may take the form of managing segregated investment portfolios or managing private funds, usually domiciled in an offshore or tax efficient jurisdiction.

Group resources accepted for retail funds

In order to establish and manage retail funds that may be offered to the public in Hong Kong, managers are subject to further vetting by the SFC under the fund authorisation process and in this regard subject to the applicable requirements under the Code on Unit Trusts and Mutual Funds (UT Code). With effect from January 2019, the SFC has relaxed its requirement under the UT Code with respect to a proposed management company of an SFC authorised company or its investment delegate who belong to a well-established fund management group. Such management company or investment delegate can now rely on the experience and resources on a group basis to satisfy the requirement of having at least two key investment management personnel who possess at least five years investment experience in managing public funds, provided that the management company or the investment delegate on a group-wide basis is able to demonstrate that it possesses the requisite oversight, monitoring and supervision systems to administer public funds.

We consider the relaxation to be a welcomed development consistent with encouraging more investment management groups to set up investment management entities in Hong Kong, and such new managers may now be better placed to seek SFC authorisation of retail funds to be offered to the public. These would further strengthen Hong Kong's position as an asset management centre and, as we see below, also develop Hong Kong's role as a jurisdiction of choice for fund domicile.

Mutual Recognition of Funds

Under Hong Kong's open framework, the UT Code does not restrict the fund domicile of authorised funds, and the SFC also accepts funds that are approved in certain jurisdictions as 'recognised jurisdiction schemes'[1] that may be authorised by the SFC under a streamline process. Accordingly retail funds in Hong Kong has for a long time been mostly UCITS funds domiciled in Luxembourg or Ireland, with Hong Kong as well as Cayman-domiciled funds making up others.

In recent years, Hong Kong domiciled unit trusts are preferred by Hong Kong managers setting up retail funds, largely due to the mutual recognition of funds arrangement between Mainland China and Hong Kong introduced in summer 2015. This is a groundbreaking initiative that enables Hong Kong authorised funds meeting relevant requirements (including being Hong Kong domiciled and managed by a Hong Kong licensed manager) to be registered for offer directly to the public in Mainland China.

Besides Mainland China, the SFC has entered into similar arrangements with Switzerland, France, United Kingdom, Luxembourg, and most recently the Netherlands[2] that opens up distribution opportunities for Hong Kong funds in these jurisdictions, and the list may further expand. Currently, for Hong Kong funds that seek to be recognised in Mainland China, the delegation of investment management by the Hong Kong manager is not permitted, whereas delegation is possible without affecting the eligibility for recognition in the other jurisdictions, as illustrated in Table 1.

Table 1. Investment management delegation by the Hong Kong manager of a "recognised Hong Kong fund"

Mainland China	Switzerland	France	United Kingdom	Luxembourg	Netherlands
Not permitted	Delegation permitted provided such delegation accepted under Hong Kong laws	Delegation to an entity operating in an "acceptable inspection regime" permitted	Delegation permitted provided such delegation accepted under Hong Kong laws and regulations	Delegation to an entity operating in an "acceptable inspection regime" permitted	Delegation permitted provided such delegation accepted under Hong Kong laws and regulations

"Acceptable inspection regimes" are currently Australia, France, Germany, Ireland, Luxembourg, Malaysia (for Islamic collective investment schemes), Switzerland, Taiwan, United Kingdom and United States. Outside this list, the SFC may accept delegation subject to meeting certain requirements and on a case-by-case basis. To-date, non-AIR delegation has been accepted for jurisdictions such as Belgium, Canada, Japan, Korea, Netherlands and Singapore.

Open-ended Fund Company Structure

While encouraging Hong Kong as a fund domicile of choice, new law has been introduced to provide an additional option for fund structuring and create a more flexible business environment for fund managers in choosing the legal entity or investment fund vehicle.

[1] "Recognised jurisdiction schemes" are qualifying retail funds from jurisdictions such as Australia, France, Germany, Guernsey, Ireland, Isle of Man, Jersey, Luxembourg, Malaysia (for Islamic collective investment schemes), Switzerland, Taiwan (for exchange-traded funds), United Kingdom and United States.

[2] The SFC and the Dutch Authority for Financial Markets entered into an Memorandum of Understanding for the Mutual Recognition of Funds arrangement on 15 May 2019

Previously, Hong Kong domiciled funds would take the form of unit trusts, and corporate form open-ended funds were not possible due to capital reduction restrictions under the Companies Ordinance. Relevant amendments to the Securities and Futures Ordinance have come into effect in July 2018, allowing Hong Kong licensed managers to set up a Hong Kong open-ended investment fund in the corporate form with legal personality and limited liability. Specifically, the legislation provides the flexibility to vary share capital and the creation and cancellation of shares in order to meet investors' requests for subscriptions for and withdrawals of capital from the fund, subject to its instrument of incorporation. Legislation also provides for segregation of liability between sub-funds that may be established within an open-ended fund company.

Besides the potential of adopting the open-ended fund company structure for retail funds, in the private funds space, profits tax exemptions have been introduced for Hong Kong open-ended funds alongside existing exemptions that are available for offshore funds (subject to meeting relevant conditions). Furthermore, effective April 2019 Hong Kong tax law has been amended to provide for the profits tax exemption to be applicable to funds overall resulting in a level playing field for offshore and domestic funds, removing ring-fencing features due to pressure from the international tax community. Going forward, regardless of their location of central management and control, their size or the purpose that they serve, all funds operating in Hong Kong may potentially enjoy profits tax exemption for transactions in specified assets subject to meeting certain conditions. In principle, such fund can also enjoy profits tax exemption from its investment in both overseas and local private companies.

Hong Kong can be an attractive option for fund managers as a jurisdiction where commercial and operational presence for fund management business is established, also in the context of the economic substance legislation enacted by various offshore jurisdictions (including the Cayman Islands and the British Virgin Islands) effective 1 January 2019. Under an environment where there may be a review and preference for onshore versus offshore jurisdictions as a choice of domicile, tax residency and place of business, Hong Kong has a growing list of double tax agreements (currently around 40) and has updated its tax legislation to be more in line with current international fiscal policies.

With the open and dynamic framework that Hong Kong continues to offer, there are many opportunities for Hong Kong to feature in investment managers' strategic business plans for funds and distribution, and its role would likely expand.

This article was first published in the Corporate LiveWire "Expert Guide – Investment funds 2019", with necessary updates.

Contact Details

If you like to know more information about the subjects covered in this publication, please feel free to contact the following people or your usual contact at our firm.

Vivien Teu **Managing Partner** **Vivien Teu & Co LLP** Tel: (852) 2969 5316 vivien.teu@vteu.co	**Christina Suen** **Counsel** **Vivien Teu & Co LLP** Tel: (852) 2969 5362 christina.suen@vteu.co	**Kenneth Yim** **Consultant, Tax*** **Vivien Teu & Co LLP** Tel: (852) 2969 5318 kenneth.yim@vteu.co