

Oversight

September 2003

Revisions to Chapter 20 of the Listing Rules in respect of authorised funds issued 1 September 2003

Listing Funds in Hong Kong

The Securities and Futures Commission (SFC) has acknowledged in the past that the listing of authorised funds on The Stock Exchange of Hong Kong Limited (SEHK) has not been a great success. Indeed to date only one such fund (other than *TraHKs*) has been successfully launched – the index ETF *iShares MSCI China Tracker*, for which Simmons & Simmons acted.

Setting aside market considerations, an historic deterrent to authorised funds seeking a listing on the SEHK

has been the relative lack of clarity as to the listing process and requirements set out under Chapter 20 (Investment Vehicles) of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Ltd. (Listing Rules). In particular, it has long been felt that the respective roles of the SFC and SEHK were not clear.

Regulatory Changes

Although the revisions to Chapter 20 were indeed long overdue, two recent events prompted the SFC and SEHK to expedite the review and consequent changes to the Listing Rules applicable to authorised funds.

The first was the entry into force of the Securities and Futures Ordinance (SFO) on 1 April this year. Under the SFO, for the first time, the term “collective investment scheme” (CIS) has been defined. The phrase CIS is wide, covering all sorts of fund vehicles (both closed-end and open-ended), and has replaced the outdated “unit trust” and “mutual fund corporation” terminology in the old securities laws. Under Section 104 of the SFO, the SFC may authorise any sort of CIS for sale to the public – Chapter 20 previously did not anticipate this and reflected the narrower power of the SFC merely to authorise unit trusts and mutual fund

corporations under Section 15 of the now repealed Securities Ordinance.

The second event was the issuance by the SFC of its Code on Real Estate Investment Trusts (REITs Code) on 15 August – see the last edition of *Oversight* (August). Under the REITs Code, the SFC will authorise closed-end unit trusts which invest in Hong Kong real estate for sale to the public on condition these CIS are listed on the SEHK. In line with the comments of many market participants (including this firm) during the draft REITs Code’s consultation period, the SFC recognised the need, given its conclusion that all “HK-REITs” be listed, to amend Chapter 20 to facilitate a successful market for HK-REITs. The changes to Chapter 20 are not, however, restricted to HK-REITs and should assist future ETF launches and other CIS listings.

Stated Purpose

The SEHK and SFC have now agreed revisions to Chapter 20 of the Listing Rules, effective 1 September 2003, in respect of collective investment schemes (CIS). In its announcement dated 26 August 2003, the SEHK stated that the purpose of the revision was to:

- create a listing platform for all CIS authorised by the SFC;



- clarify the respective roles of the SFC vs the SEHK; and
- streamline the listing process generally for CIS.

The Old Chapter 20

Under the pre-1 September Chapter 20, Rule 20.01 specified that only unit trusts, mutual funds or other collective investment schemes authorised by the SFC under the Code on Unit Trusts and Mutual Funds (Mutual Fund Code) could be considered under Chapter 20. Accordingly references were made throughout Chapter 20 to “authorised schemes”, “units or redeemable shares (or their functional equivalent)” and to the Mutual Fund Code. This drafting has been tidied up and the term “Collective Investment Schemes” is now uniformly applied (bearing the same meaning as provided under the SFO). Corresponding references are also now made to “interests” in CIS. Previous references to the Mutual Fund Code have been removed, with the effect (as specified in the new Note i) to Rule 20.01), that any type of CIS authorised by the SFC “in accordance with the requirements of the respective codes” issued by the SFC from time to time may seek listing under Chapter 20. Accordingly, as indicated, HK-REITs may now be listed in accordance with the new Chapter 20 requirements.

Generally, as described in Note ii) to the new Rule 20.01 of the Listing Rules, the SEHK’s role is now limited to vetting documentation “in respect of listing issues not covered” by the SFC’s codes and to supervising the actual listing process. Whilst the SEHK retains responsibility for monitoring compliance with the Listing Rules on a continuing basis, these requirements are minimal.

Overall the new rules for listing SFC authorised collective investment schemes continue to be structured in the same way as, and to follow, the old Chapter 20. Some (minor) rules have been repealed completely rather than revised:

- Rule 20.09, by which the SEHK may refuse a booking for a listing date if there are too many existing reservations in the relevant period;
- Rule 20.10, by which revised documentation after submission must be marked up in the margin (against the Mutual Fund Code, if relevant). This change is procedural but will ease the application process given the new timing requirements (see below); and
- Rule 20.11, by which no material amendment was permitted to be made to the listing document without the consent of the SEHK. Again this should facilitate a smoother listing process, as the SFC will have primary responsibility for the contents and approval of the offering document.

The Listing Agreement

In addition to the changes to Chapter 20 of the Listing Rules, it should be noted that the form of the listing agreement for a CIS in Appendix 7G of the Listing Rules has also been updated to conform with the new terminology of Chapter 20, as revised. Again most of these amendments are not substantive – for example, references to the “Code” being replaced by references to the SFC’s “Authorisation Conditions” in the covenants made by the manager, the fund itself (if incorporated) and the trustee/custodian, as appropriate. However, three major revisions have been made to the listing agreement for CIS:

- the fund is no longer required to notify the SEHK of any changes either in control of the manager or in the “general character” of the fund (Paragraphs 4(1) and (2) have been replaced by a duty to notify the SEHK if the SFC withdraws the fund’s authorisation under the SFO);
- the fund is no longer required, under the now deleted Paragraph 5, to provide the SEHK with ten copies of its reports and accounts at the same time these are sent to investors (a small but useful waiver); and
- the fund no longer needs to submit all advertisements post-listing to the SEHK under (the now repealed) Paragraph 8. As mentioned above, the SFC will take primary responsibility (under Section 115 of the SFO) to





approve all advertisements relating to CIS. Note iii) to Rule 20.01 makes clear that all marketing materials and announcements must be submitted to the SFC, not the SEHK, for approval and filing.

A further revision, is the insertion in the listing agreement of a new Paragraph 9A under which all authorised funds will need to provide the SEHK with soft copies of circulars, notices, financial reports and other documents for publication on the SEHK's website. The SEHK reserves the right to stipulate the electronic format of such filings.

The Revised Chapter 20

In addition to the form of the CIS listing agreement set out in Part G of Appendix 7 to the Listing Rules, new definitions relevant to Chapter 20 have been added to Chapter 1 of the Listing Rules. In addition to the definition of a CIS, "CIS Operator" is defined to mean the entity which operates or manages the collective investment schemes (most often the fund manager), whilst a new term of "CIS Disclosure Document" is also provided. The latter essentially means the Hong Kong offering document or such other product description documents as required by the SFC's various codes.

The references throughout Chapter 20 to the CIS Disclosure Document

are key. Under the new rules laid out in Chapter 20 of the Listing Rules, the CIS Disclosure Document which is the listing document for a CIS is principally reviewed and commented upon by the SFC although, as in the old Chapter 20, a disclaimer regarding the SEHK's liability must still be included under Rule 20.24, and the CIS Disclosure Document may not be issued until the SEHK has confirmed it has no further comments under Rule 20.13.

In terms of timing the CIS Disclosure Document is also key. As previously, Rule 20.04 of the Listing Rules requires that an application to the SEHK for listing be supported by the CIS Disclosure Document (complying with Chapter 20). However, in one important respect the procedure is now different. Although (as before) it is advisable to discuss the proposed listing with the SEHK in advance, the formal application to the SEHK may now be made under Rule 20.07 before actual SFC authorisation under Section 114 of the SFO has been given by the SFC provided, however, that the SFC confirms that it has no further comments on the CIS Disclosure Document. This ties in with the requirements of the REITs Code, under which the SFC will make the authorisation of a HK-REIT conditional upon its listing – in other words, SEHK listing approval and SFC authorisation can be concurrent.

As regards timing, under Rule 20.05 the advance booking time has been revised from 15 clear days prior to bulk printing of the listing document to 10 clear business days prior to the expected SEHK approval date (and the SEHK now has the express right to vary this period by prior agreement).

In addition, the procedure itself has been simplified. Whereas under the old Rule 20.14 the "advanced" listing document was submitted on a different date, under the new Rule 20.14, (a) the advanced proof CIS Disclosure Document, (b) four copies of the subscription or application form for investors, and (c) the draft listing agreement (see above) are submitted with the Form A2 (the advance booking form). It is also noticeable that the documents in support of the Form C3 (the formal listing application) must now be submitted five, rather than three, clear business days before the hearing date - although the SEHK may also agree to a variance of this period.

Another useful simplification is that Form C3 will not be required to be accompanied by a certified copy of the trust deed or other constitutive documents governing the CIS. Under revised Rule 20.17, these should be provided (with the relevant resolutions approving the listing and with the listing fee) after the issue of the CIS Disclosure Document but before trading on the SEHK commences. Rule 20.08 of the new Chapter 20 also revises the need to pre-agree a timetable with the SEHK when booking the listing. In practice, of course, the SEHK will need to be comfortable with the proposed timetable but the new wording of this rule removes the SEHK's strict right of veto unless the CIS fails to submit the required documentation on time.

The Agent

Aside from the above, the other major change which has been introduced in the revised Chapter 20 is the replacement of the need to

appoint a sponsor, in conformity with Rule 3.01, with the need for the CIS or CIS Operator to appoint an “agent” with sufficient experience to (a) deal with the SEHK in connection with the listing application and compliance with Chapter 20, and (b) manage overall the listing process with responsibility to ensure the listing is conducted in a “fair, timely and orderly manner”. The “listing process” is described as including (i) processing applications, (ii) allocation, (iii) underwriting, (iv) administration of subscription lists, and (v) processing of subscription monies.

Although the term “agent” matches the requirements under the REITs Code, the role is essentially that of a sponsor. Certainly to perform these functions, as indicated in Rule 5.12 of the REITs Code, an agent of a listed CIS in any IPO or other offer will need to be licensed under the SFO to perform these duties. Accordingly whilst the Note to Rule 20.06 of the Listing Rules states that an agent may be the CIS Operator (i.e. the manager) it is more likely that the manager will appoint an agent (probably being an entity which would otherwise have been a sponsor). The new Rule 20.06 does, however, leave open the possibility of a cost saving for a listed CIS which in theory need not appoint a third party agent as sponsor.

Grounds for Optimism

In practice the new Chapter 20 of the Listing Rules could not be less successful than the old. It is clear that both the SFC and the SEHK have attempted to create an easier and more open set of listing rules for CIS applicants and CIS Operators. Whilst most of the changes may have been prompted by the SFO’s entry into force earlier this year and the issuance of the SFC’s REITs Code, the revisions to Chapter 20 should facilitate more listed CIS, both homegrown and foreign. Certainly there is greater clarity as to the respective roles of the SFC and the SEHK which is welcome.

Whilst much will depend on the experience to be gained by the regulators, the revised requirements are a step in the right direction of creating a market for listed funds in Hong Kong to rival those developing elsewhere in Asia.

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