



**CONSULTATION ON  
PROPOSED AMENDMENTS TO THE SECURITIES  
AND FUTURES (PROFESSIONAL INVESTOR) RULES**

**The Law Society's Submissions**

The Securities and Futures Commission (“SFC”) in March 2017 launched a consultation on proposed amendments to the Securities and Futures (Professional Investor) Rules. It sought views on five questions. The Law Society has reviewed the above consultation paper (“Consultation Paper”) and provided the following submissions.

**Overall response**

2. The Law Society welcomes the proposed changes, which are a helpful codification and re-statement of principles and views that have been prevalent in some parts of the market for some time. We consider this exercise demonstrates the importance of ensuring transparency as far as possible under the regime to avoid as far as possible some market participants being disadvantaged where they were not aware of the availability or likely availability of certain modified treatments of clients. The avoidance of piecemeal regulation in this regard is highly welcome. It is to be hoped that the success of this codification exercise will lead to further, similar exercises in the future, to similar effect.

3. We would suggest that, following implementation of the changes, any *ad hoc* modifications, if essential for the sake of flexibility and commercial practicality, while within the perceived intentions underlying the overall regime, should be publicized to the rest of the market at or around the time of the modification to ensure a level playing field for participants. Any such modification could, for the sake of certainty, be publicized through relevant industry bodies and then formally codified at a suitable time in early course afterwards.

***Question 1:*** *Do you agree that the proposed amendments to the Professional Investor Rules would introduce appropriate levels of consistency and flexibility,*

*and better serve the interests of both intermediaries and their clients? Please explain your view.*

*Do you have any other suggestions?*

**Law Society's response:**

4. We agree, subject to the points made below and our overall view set out above.

**Question 2:** *Do you agree that section 3(b) of the existing Professional Investor Rules in relation to individuals should be extended so that:*

(a) *an individual's share of a portfolio that is held in a joint account with a non-associate can be counted towards meeting the prescribed threshold to qualify as a professional investor (as outlined in paragraph 14(b) (in the Consultation Paper) and provided for in Rule 6(1)(c) in Appendix A (to the Consultation Paper))?* Please explain your view.

**Law Society's response:**

5. We consider this approach to be appropriate to take into account varied models under which investors operate in the Hong Kong market, including broader family participation. The proposal goes further and would cover inclusion of portfolios held with any non-associate. We do not consider this to be likely to create problems in practice given the nature of a joint account, under which as a matter of law a joint account holder is entitled (subject to any relevant agreement among the parties) to the whole of the proceeds of the joint account.

6. A warning from the intermediary may be appropriate in such cases to warn the client of the dangers of reliance on a joint account should the other party or parties decide to use the contents of their account for other purposes. However, that is not relevant in the context of treatment as a professional investor, more in the context of account management in general by intermediaries.

*In determining the share of an individual's portfolio held in a joint account with a non-associate for the purpose of meeting the prescribed threshold, [the SFC] propose that the individual's share is either based on the share specified in the written agreement between the account holders or an equal share of the portfolio in the absence of a written agreement (as provided for in Rule 6(2) in Appendix A (to the Consultation Paper)). Do you agree with [the SFC'S] approach? Please explain your view.*

**Law Society's response:**

7. As indicated above, it needs to be borne in mind that an arbitrary partition of the joint account according to "equal shares" where there is no agreement is a useful indication of the investor's access to funds, but may not in the event prove to determine the actual access to funds when they are needed. That is of course a risk for the intermediary when an account is initially documented, and for the client in assessing its appropriate treatment under the SFC Code of Conduct.

(b) *an individual's portfolio or share of a portfolio held by a corporation, the principal business of which is to hold investments and which is wholly or partially owned by the individual, can be counted towards meeting the prescribed threshold to qualify as a professional investor (as outlined in paragraph 14(a) (in the Consultation Paper) and Rule 6(1)(d) and Rule 6(1)(e) in Appendix A (to the Consultation Paper))?* Please explain your view.

*Do you have any other suggestions?*

**Law Society's response:**

8. We agree, given the protections built into the rules relating to the classification of professional investors.

**Question 3:** *Do you agree that the scope of the existing Professional Investor Rules should be extended so that:*

(a) *any corporation, the principal business of which at the relevant date is to hold investments and which is wholly owned by one or more of the persons where each of them is qualified as a professional investor, will qualify as a professional investor (as outlined in paragraph 14(c) (in the Consultation Paper) and provided for in Rule 7(b) in Appendix A (to the Consultation Paper))?* Please explain your view.

**Law Society's response:**

9. We agree. We regard it as important to retain suitable control over the definition by limiting the treatment to whole ownership in turn by professional investors.

(b) *any corporation, which wholly owns another corporation which has been*

*qualified as a professional investor under the Professional Investor Rules by meeting the asset or portfolio threshold, will qualify as a professional investor (as outlined in paragraph 14(c) (in the Consultation Paper) and provided for in Rule 7(c) in Appendix A (to the Consultation Paper))? Please explain your view.*

*Do you have any other suggestions?*

**Law Society's response:**

10. We agree, for the reasons stated above.

**Question 4:** *Do you agree that the evidential requirements set out in section 3(a) to (c) of the existing Professional Investor Rules (as outlined in paragraph 11(b) (in the Consultation Paper) should be extended to include public filings and certificates issued by auditors, certified public accountants or custodians (as outlined in paragraph 14(d) (in the Consultation Paper) and provided for in Rule 9 in Appendix A (to the Consultation Paper))? Are these alternative forms of evidence used commonly by intermediaries as proof of clients meeting the stipulated monetary thresholds?*

*Please explain your view.*

**Law Society's response:**

11. We agree that a broader range of permissible types of evidence should indeed be introduced to reflect market practice. We cannot comment on the extent and nature of the current practices in this regard, but it is important to ensure that the evidential requirements keep pace with the commercial realities in the market.

*If so, do you also agree that the Professional Investor Rules should prescribe the types or categories of documents that could be regarded as "public filings" and the extent of details to be included in the content of "certificates" issued by auditors, certified public accountants or custodians? Please explain your view.*

**Law Society's response:**

12. We consider that a degree of principle-based assessment needs to be retained in this type of procedural rule, to avoid as far as possible over-prescription which might going forward lead to the perceived need for more "modifications", which would be an unwelcome outcome. Intermediaries are better placed to respond to this question in relation to the practical types and categories of documents.

*In particular, which documents are used in practice as “public filings” and “certificates” issued by auditors, certified public accountants or custodians? Please provide examples.*

**Law Society’s response:**

13. We have no comment on this question but, by way of remark, would draw your attention to the fact that the existing Rules recognize certificates issued by an auditor or a certified public accountant in the case of individual Professional Investors, although the term “certificates” is not defined or explained in the existing Rules. We take the view that the approach in the existing Rules should be preserved and there is no need to define or explain “certificates” in the revised Rules.

*Do you consider that the Professional Investor Rules should impose conditions for the use of these alternative forms of evidence? Please explain your view.*

**Law Society’s response:**

14. We note that the definition of “public filing”, as it currently stands, is framed as follows:

*public filing (公開檔案) in relation to an individual, a trust corporation (or any trust of which it acts as a trustee), corporation or partnership (the entity) means a document that, pursuant to legal or regulatory requirements applicable to the entity in Hong Kong or in a place outside Hong Kong, has been submitted by or on behalf of the entity to a person or body that is under a duty to publish the document to, or otherwise make the document available for inspection by, members of the public in Hong Kong or in a place outside Hong Kong.*

15. On the face of it, the test would be that, in relation to a potential professional investor:

- the professional investor would need to be subject to legal or regulatory requirements in a jurisdiction;
- the professional investor must have submitted (or had submitted on its behalf) a document to a person or body (that is not necessarily the regulator nor in that jurisdiction);
- that person or body must be under a duty to publish the document to members of the public in Hong Kong or elsewhere

16. That is in our view appropriate in relation to Hong Kong regulators, but we should add that, for the sake of clarity and for the avoidance of doubt, the person or body to which the professional investor has submitted the document should include exchanges and listed companies. This is because, in practice, the most helpful “public filings” are probably the financials and other reports and materials published by exchanges and listed companies. Following from this, we would agree that regulators, exchanges and listed companies, in appropriate other jurisdictions, should be included in this provision.

17. We submit that it would be appropriate to apply some controls to the inclusion of other jurisdictions, to ensure that suitable jurisdictions are relied upon, rather than an across-the-board approach. There are numerous instances in the Hong Kong securities regulations of suitable criteria being applied to ensure appropriate offshore regulation. If applied in the professional investor context that would avoid as far as reasonably possible, any inappropriate reliance upon inappropriate jurisdictions to justify client categorisations.

*Do you have any other suggestions?*

**Law Society’s response:**

18. No comment.

***Question 5:** Do you have any other comments on the indicative draft of the proposed Professional Investor Rules in Appendix A (of the Consultation Paper)? Please explain your view.*

*Do you suggest any alternative wording for the proposed rules? If so, please give your suggestions and explain your view.*

**Law Society’s response:**

19. Please see the suggestion set out above in principle in relation to *public filings*.

20. Regarding the definition of *portfolio*, we note the continuing circularity resulting from *portfolio* meaning a “portfolio”. Reference to assets held rather than a “portfolio” in the body of the definition may be preferable.

**The Law Society of Hong Kong  
3 April 2017**