



**COMMENTS BY THE LAW SOCIETY OF HONG KONG ON THE
CONSULTATION PAPER ON THE PROPOSED STREAMLINING OF THE
PRE-VETTING OF NOTICES AND ADVERTISEMENTS OF RELEVANT
AUTHORIZED COLLECTIVE INVESTMENT SCHEMES PUBLISHED IN
JANUARY 2008
(THE “CONSULTATION PAPER”)**

We set out our comments on the Consultation Paper below for consideration:

- 1. Do you agree that the Securities and Futures Commission (the “Commission”) should cease pre-vetting notices, letters and announcements to investors, other than those relating to withdrawals of authorization, mergers or terminations, as proposed in paragraph 13 of the Consultation Paper?**

We agree that a post-vetting regime would generally save both time and costs. A move to post-vetting does however raise the issues detailed below which should be anticipated and catered for.

1. As recognised by Hong Kong Exchanges and Clearing Limited in relation to its proposals to cease mandatory pre-vetting of listed issuers’ announcements¹, a move to post vetting may lead to a decline in the quality of disclosure as well as an increase in supplementary disclosures and disciplinary actions.
2. As non-compliance with the requirements of the relevant codes could only be identified after publication of any advertisement, consumers’ exposure will be greater than under the current pre-vetting regime given that consumers may purchase investments on the basis of non-compliant advertisements. Their protection will then depend on their ability to obtain compensation for any loss suffered or to withdraw from the product without penalty to avoid any possible future loss.
3. The Consultation Paper does not contain details of proposed scope and basis of the follow-up action that the Commission will be able to take in the post-vetting process.

¹ Combined Consultation Paper on Proposed Changes to the Listing Rules January 2008 at paragraph 7.13.

4. If the objective of reducing the regulatory and cost burden is to be achieved, it will presumably not be possible to post-vet all advertisements. The Commission should therefore set out how it proposes to balance consumer protection with the need to reduce the regulatory and cost burden. Is it proposed that the Commission should focus its resources on areas which it considers to have the highest risk for consumers or the greatest potential or actual impact?
5. It may not be possible for the management company or product issuer to prevent the private circulation of a non-compliant advertisement in the situation where the Commission issues a request to cease issuing the advertisement as is proposed at paragraph 20 of the Consultation Paper. This could be dealt with by stipulating that no orders to purchase the products may be accepted after the issue of a request by the Commission to cease issuing any relevant advertisement.

The above risks could be mitigated as follows:

- a. The concerns raised at paragraph 1 above could be addressed by allowing product issuers, management companies and other relevant parties to consult with, and request guidance from, the Commission before the publication of any advertisement. The ability to seek guidance from the Commission will be particularly important in the case of novel or complex matters. It would however be necessary to ensure that this process is not used as an alternative to firms' own proper compliance procedures.
- b. Where the Commission makes follow-up enquiries with a relevant party after the publication of an advertisement (as suggested at paragraph 13 of the Consultation Paper), it should inform the party of the basis for the enquiries by reference to specific provisions of relevant codes and guidelines.
- c. In cases where there has been actual consumer detriment, or where consumers have bought products on the basis of a non-compliant promotion, the Commission should have the power to require the relevant party to remedy the situation by allowing investors to withdraw from the product without penalty, or by offering compensation.
- d. The Commission should take steps to create a more transparent regulatory regime. The aim should be to make clear to all parties the standards that are required.

It should in particular seek to increase public awareness of the required standards. Consideration should be given to the following proposals put forward by the UK's Financial Services Authority in April 2002²:-

- Publish regular investor bulletins on financial promotions. These could cover issues the subject of frequent complaints and other contentious issues and could be used as a means of explaining to investors the standards of

² The FSA's Regulatory Approach to Financial Promotions published in April 2002 at paragraph 4.21.

consumer protection they have the right to expect. Case studies, including anonymised/de-branded examples, could be used to illustrate good and bad practice; and

- Encourage investors and others to report any misleading promotional material. The Commission could consider the possible benefits of setting up a telephone hotline for reporting.

Issuers would also benefit from guidance on the Commission's website as to the requirements of the revised Advertising Guidelines. Based on the Commission's monitoring of published advertisements, it could consider including mocked-up examples of advertisements to illustrate non-compliance issues.

2. **Do you agree that advertisement issuers should be permitted to make use of the current exemptions under section 103 of the SFO such that eligible advertisements would not be subject to authorization by the Commission, as proposed in paragraphs 19 to 20 of the Consultation Paper?**

Yes.

3. **Do you agree that the present advertising guidelines under the respective Product Codes be harmonized?**

Yes. Consistency in the requirements under the respective Product Codes is likely increase investor awareness of the required standards.

4. **Do you have any comments on the revised Advertising Guidelines as set out in Annex 5 of the Consultation Paper?**

- **General Principles**

The Commission should consider including on its website examples of advertisements which it would consider to be in breach of the general principles.

- **Paragraphs 28 and 29(a)**

The broadcast of the full name of the issuer under paragraph 28 should not be optional for audio advertisements. If a short form of the issuer's name is used, it may cause confusion to investors as there may be other companies with similar names.

5. **Do you think back-tested or simulated performance information, as discussed in paragraphs 56 to 62 of the Consultation Paper, should be allowed under restricted circumstances? What disclosures do you think are helpful for the interpretation of back-tested or simulated performance information?**

We are of the view that back-tested and/or simulated performance information could be allowed for formula funds, where payouts and returns are based on a specific pre-determined formula. The Commission should adopt the principles summarized at paragraph 60 of the Consultation Paper and detailed rules on the presentation of such

information (as suggested at paragraph 61) to minimize the chances of manipulation and cherry picking. The disclosures should clearly describe the basis of simulation.

6. Do you have any comments on the implementation timetable as proposed in paragraphs 80 and 81 of the Consultation Paper?

The implementation timetable is acceptable.

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