Hong Kong Practice Series – Asset Management

Hong Kong

Private Fund Offering Playbook

Cooley

Part I. Hong Kong Regulatory Regime – Fund Manager Licensing Requirements

Hong Kong securities law is primarily governed by the Securities and Futures Ordinance (Cap. 571) (SFO). Fund managers are expected to comply with the codes and guidelines published by the Securities and Futures Commission (SFC), especially the Fund Manager Code of Conduct, the Code of Conduct for Persons Licensed by or Registered with the SFC and the SFC Licensing Handbook.

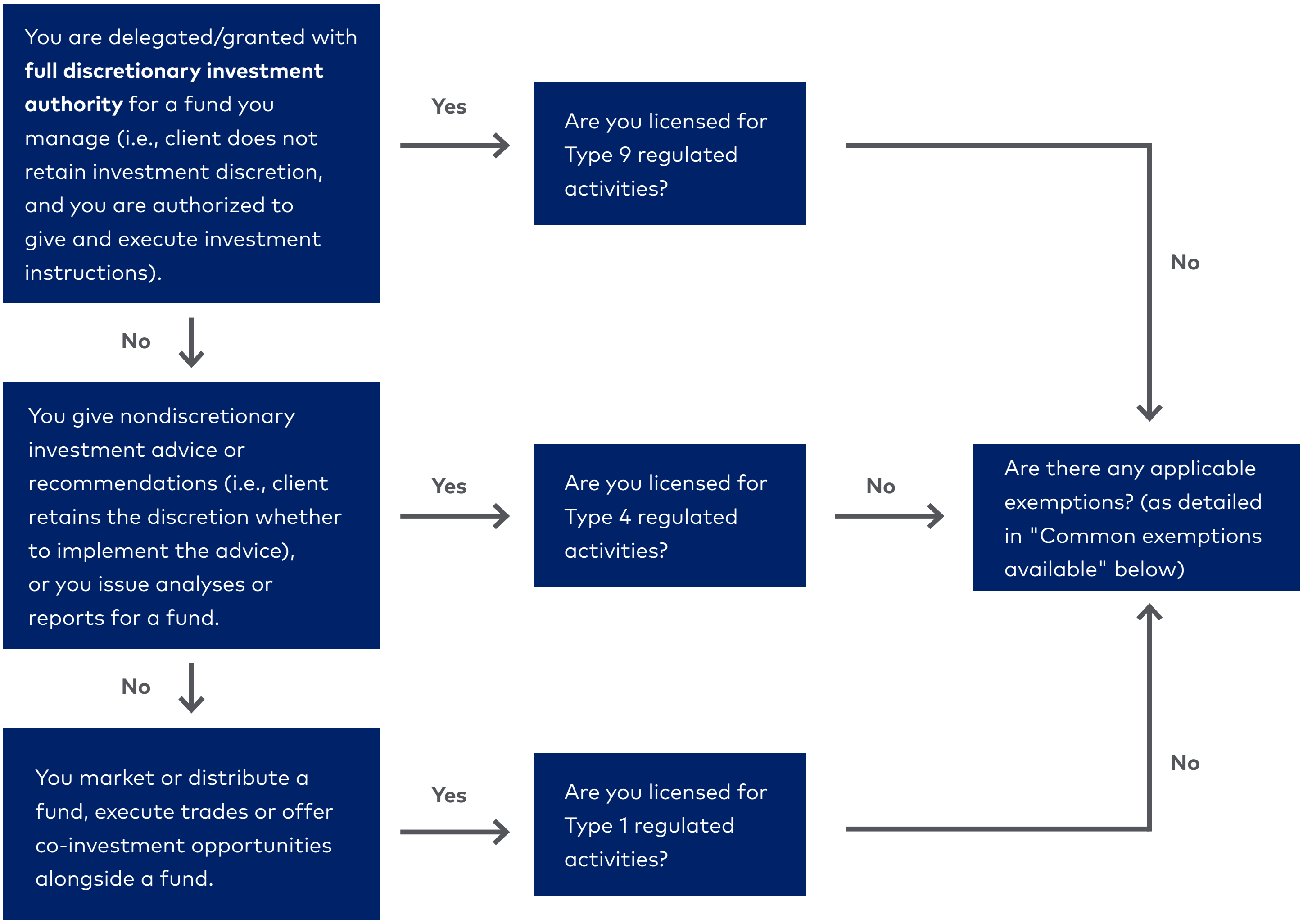
Are you required to be licensed in Hong Kong?

The licensing regime under the SFO is activity-based. Fund managers that **carry on a business** in one or more **regulated activities in Hong Kong** are required to be licensed under the SFO. Regulated activities that are most relevant to a private fund manager are Type 1 (dealing in securities), Type 4 (advising on securities) and Type 9 (asset management).

- **Dealing in securities** means making or offering to make an agreement with another person, or inducing or attempting to induce another person to enter into or offer to enter into an agreement to acquire, dispose of, subscribe for or underwrite securities, or to secure a profit to any of the parties from the yield of securities or by reference to fluctuations in the value of securities.
- **Advising on securities** means giving advice or issuing analyses or reports for the purposes of facilitating the recipients of the analyses or reports to make decisions on whether, which, the time at which, or the terms or conditions on which securities should be acquired or disposed of.
- **Asset management** means real estate investment scheme management, or securities or futures contracts management.

Private equity and venture capital investment firms routinely engage in one or more of these regulated activities. It is common for these types of firms operating in Hong Kong to hold one or more licenses for carrying out the regulated activities under the SFO.

Are you required to be licensed for regulated activities?



Notes to fund managers:

- The term "securities" is broadly defined under the SFO and includes shares or debentures in private offshore companies, listed shares and interests in collective investment schemes (e.g., mutual funds and unit trusts).
- If a fund manager from outside of Hong Kong "actively markets" to the Hong Kong investing public services that would constitute regulated activities, the fund manager is required to obtain the relevant SFC license. This may include, for example, those who frequently call on Hong Kong investors and market their services and products, as well as those who run mass media programmes and/or internet promotions targeting the investing public in Hong Kong.

Consider forming your fund entity in Hong Kong

The open-ended fund company (OFC) and the limited partnership fund (LPF) are the two most commonly adopted Hong Kong fund vehicles for private fund managers. An LPF is a Hong Kong limited partnership administered by the Companies Registry (CR) and primarily governed by the Limited Partnership Fund Ordinance (Cap. 637) (LPFO). An OFC is a Hong Kong corporation with limited liability and a board of directors and must be registered with the SFC under the SFO.

Key features of OFCs and LPFs

	Key parties	Investor count	Establishment procedure	Hong Kong tax incentives	Umbrella structure (sub-funds) allowed?
OFC	Directors, custodian, investment manager	No limits	Application for registration of the OFC shall be submitted to the SFC	OFCs may benefit from profits tax exemptions	Yes, sub-funds (with different underlying assets, investment strategies and fund economics) may be established within one OFC, with segregated assets and liabilities of each sub-fund
LPF	General partner (GP)/limited partner (LP), investment manager (No custodian required)	At least one LP	Application for registration of the LPF shall be submitted to the CR by a Hong Kong law firm on behalf of the GP	LPFs may benefit from profits tax exemptions and exemptions on eligible carried interest received by a qualifying fund manager	No

In practice, we more often see an OFC adopted by hedge fund managers (including crypto hedge funds), due to its capability to house multiple segregated sub-funds under one single fund vehicle, which is aligned with the prevailing structure for open-ended funds in Asia. LPFs are more commonly used for closed-end funds, including single-deal project funds and special-purpose investment vehicles.

Regulatory framework for OFCs and LPFs

	OFC	LPF
Legislation and codes governing the vehicle	• SFO • Securities and Futures (Open-ended Fund Companies) Rules • Securities and Futures (Open-ended Fund Companies) (Fees) Regulation • Code on Open-Ended Fund Companies • SFC Products Handbook	• LPFO • Certain provisions of the Partnership Ordinance (Cap. 38) • Rules of equity and of common law
Is it required to appoint an investment manager?	Yes, for managing the scheme property of the OFC	Yes, for carrying out the day-to-day investment management functions of the LPF
Required to be licensed by the SFC?	Yes, must be licensed for Type 9 regulated activities	Depends on whether the investment manager carries on any regulated activities under the SFO; if so, it would need to be licensed by the SFC

Common exemptions available

Despite the foregoing requirements, there are statutory exemptions available. Below is a checklist of the most commonly applied exemptions from the SFC's licensing requirements:

Incidental exemptions

Factors to consider for incidental exemptions:

- Is the activity subordinate to the carrying on of another regulated activity for which the fund manager is already licensed?
- Are discrete fees charged for the activity?
- Does the activity constitute a major part of the fund manager's business?

If you hold a Type 1 license:

- May not need to be licensed for Type 4 or Type 9 if the activities are wholly incidental to Type 1 activities
- For example, stockbrokers providing investment advice (Type 4) or managing discretionary accounts for their clients (Type 9)

If you hold a Type 9 license:

- May not need to be licensed for Type 1 or Type 4 if the activities are carried out solely for the purposes of Type 9 activities
- For example, fund managers placing trade orders to dealers (Type 1) or providing investment advice (Type 4) to clients in the course of managing such clients' portfolio of securities

Professional investor exemptions

- Applicable to **Type 1** regulated activities (dealing in securities)
- A person **as principal** dealing with professional investors as defined under Schedule 1 to the SFO
- Special care should be given to the legal structure and circumstances regarding whether you are indeed acting as a principal

Note: "Professional investor" in this exemption does not include high net worth individuals.

Group company exemptions

What is a group company under this exemption?
Each of companies A, B and C is a group company.

Providing advice or services to a group company:

- May not need to be licensed for Type 4 if you provide nondiscretionary investment advice or research reports to the group company for its own consumption.
  Note: Not applicable to a fund manager advising its group company in respect of that group company's client assets
- May not need to be licensed for Type 9 if you provide asset management services to a group company in respect of that group company's assets.
  Note: Not applicable to the management of a group company's client assets

Note:

- If you only hold a Type 4 license, there is no incidental exemption that you may rely on.

Part II. Hong Kong Anti-Money Laundering Statutory Requirements

Hong Kong is a founding member of the Asia/Pacific Group on Money Laundering (APG) and a member of the Financial Action Task Force (FATF). Private funds are subject to Hong Kong's anti-money laundering (AML) obligations to uphold international standards.

In particular, with respect to LPFs, a responsible person (RP) must be appointed by the general partner (GP) to carry out AML and counter-terrorist financing (CTF) functions under the LPFO. Besides appointment of the RP, LPFs are required to maintain records – including a register of partners, documents of each transaction carried out by the fund and the controller of each of the partners of the fund.

The Anti-Money Laundering and Counter-Terrorist Financing Ordinance (AMLO)

The AMLO is the cornerstone of the AML and CTF regime in Hong Kong and provides relevant authorities with power to supervise compliance and publish guidelines for operation of the statutory provisions. LPFs are subject to the AMLO, and an overview of the requirements under Schedule 2 is as follows:

Customer due diligence (CDD)

- Adopt a risk-based approach when carrying out CDD measures – the extent of this should be commensurate with the money laundering and terrorist financing risks associated with the business relationship.

Record-keeping

- Keep the originals or copies of transaction records, CDD information, and other records regarding each customer and each transaction for at least five years.

Monitor business relationships

- Continuously monitor business relationship with clients – including documents and information obtained from CDD – and monitor and identify unusual transactions.

Checklist of AML and CTF obligations for LPF

- ☐ Appointment of RP

Ongoing obligations

- ☐ Maintain records under LPFO
- ☐ CDD
- ☐ Record-keeping under AMLO
- ☐ Monitor business relationships

What else?

In addition to the AMLO, Hong Kong has put in place several pieces of legislation concerning the AML and CTF regime. There is a statutory obligation to make suspicious transaction reports where a person knows or suspects that any property is connected with:

- An indictable offence – Organized and Serious Crimes Ordinance (Cap. 455)
- Drug trafficking – Drug Trafficking (Recovery of Proceeds) Ordinance (Cap. 405)
- Terrorist property – United Nations (Anti-Terrorism Measures) Ordinance (Cap. 575)

The Weapons of Mass Destruction (Control of Provision of Services) Ordinance (Cap. 526) prohibits the provision of services that will or may develop, produce, acquire or stockpile weapons of mass destruction, and the United Nations Sanctions Ordinance (Cap. 537) imposes sanctions against places outside of the People's Republic of China arising from Chapter 7 of the Charter of the United Nations, with regulations relevant to AML and CTF.

Cooley's Hong Kong office boasts a team of professionals qualified in Hong Kong law in the areas of corporate law, securities regulations and asset management. We represent entrepreneurs, investors, fund managers and select multinationals and help them navigate commercial contractual arrangements and complex regulatory matters. Our lawyers are a combination of seasoned practitioners and Hong Kong-native solicitors who bring a knowledge of local statutes with a global perspective, ensuring comprehensive solutions to navigate the complexities of Hong Kong's legal landscape and beyond.