

CSRC Provides Guidance for Fund Investment

By Sandra Lu

The *Guidance for Securities Investment Funds to Participate in Stock Index Futures Trading* (Guidance) was promulgated and implemented by the China Securities Regulatory Commission (CSRC) on 21 April 2010. Pursuant to the Guidance, equity funds, hybrid funds and capital guarantee funds are allowed to invest in Stock Index Futures (SIFs) while bond funds and money market funds are prohibited.

The SIFs in which funds are allowed to invest refer to financial futures contracts that are based on stock price indices approved by the CSRC and listed on the China Financial Futures Exchange (CFFE). Funds' investment in SIFs is for hedging risks and conducted in accordance with the relevant provisions of *Measures for the Administration of Hedge* promulgated by the CFFE.

Restrictions on Funds' Investment in SIFs

The Guidance requires funds' investment in SIFs to be subject to the following requirements:

- At the end of any trading day, the value of SIFs contracts with call options held by a fund shall not exceed 10% of the net asset value of the fund.
- At the end of any trading day - for a close-ended fund, an open-ended index fund (excluding the enhanced fund) and an ETF - the value of SIFs contracts with call options and the market value of securities held by it shall not exceed 100% of its net asset value; and for other types of funds, the ratio is 95%.
- At the end of any trading day, the value of SIFs contracts with put options held by a fund shall not exceed 20% of the total market value of the stocks held by the fund.

如果您需要本出版物的中文本，请与下列人员联系：

韩东红: (86 21) 3135 8709
Publication@llinkslaw.com

If you would like other Llinks publications, please contact:

Lily Han: (86 21) 3135 8709
Publication@llinkslaw.com

Llinks Law Offices
www.llinkslaw.com

CSRC Provides Guidance for Fund Investment

- The aggregation (calculated by netting) of the market value of stocks and the value of SIFs contracts with call or put options held by a fund shall be subject to the ratio of stock investment provided in the fund contract.
- The turnover of SIFs contracts (excluding close of positions) traded by a fund within a trading day shall not exceed 20% of the net asset value of the fund on the previous trading day.
- At the end of each trading day, cash held by a close-ended fund and an ETF shall, after deducting the transaction margin of SIFs contracts, be not lower than double of the transaction margin. Cash held by other open-ended funds shall be not lower than 5% of the net asset value of the funds or government bonds with less than a one year term after deducting the transaction margin of SIFs contracts.

Special Provisions on the Guarantee Funds' Investment in SIFs

Pursuant to article 3 of the Guidance, guarantee funds can invest in SIFs for purposes other than hedging risks. Pursuant to article 5 of the Guidance, guarantee funds are not restricted by the provisions stated in the previous paragraph. However, guarantee funds' investment in SIFs shall comply with the capital guarantee strategy and investment objective prescribed in the fund contracts, and the daily maximum potential loss of SIFs contracts and securities held by it shall not exceed the balance of the net fund asset deducting asset used for capital guarantee.

The Guidance also requires that guarantors of guarantee funds (whether the existing funds or the funds to be launched) shall be fully aware of the transaction strategies and potential loss of SIFs and make special statement in the guarantee agreements.

Relevant Policies of Fund Management Companies (FMCs)

Pursuant to the Guidance, if the funds managed by FMCs propose to invest in SIFs, FMCs shall at least set up the following internal policies:

- relevant investment decision-making procedures;
- risk control policies; and
- relevant policies on authorisation and management (including authorising certain management personnel(s) to approve the investment in SIFs).

Investment decision-making procedures and risk control policies shall be subject to the approval of the board of directors of FMCs.

Existing Funds Investing in SIFs

CSRC Provides Guidance for Fund Investment

If an existing fund established before the implementation of the Guidance plans to invest in SIFs, its fund manager shall specify relevant investment strategy, proportion limits and ways of information disclosure in the fund contract and conduct relevant procedures accordingly. Whether a meeting of unit holders is required to be convened to add such provisions in the fund contract depends on the provisions of the current effective fund contract and whether the investment in SIFs will have impact on the overall investment strategy and investment purpose of the fund.

New Funds Investing in SIFs

If a new fund, which applies for offering after implementation of the Guidance, plans to invest in SIFs, its application materials, i.e. fund contract, prospectus and product scheme etc., shall contain the SIFs' trading plans and other relevant contents. Meanwhile, the internal policies of SIFs and description of preparation status shall also be submitted when submitting the fund application materials.

Information Disclosure on Funds' Investment in SIFs

Pursuant to the Guidance, a fund shall, in its periodical reports (i.e. quarterly reports, semi-annual reports and annual reports) and prospectus (renewal), make information disclosure on SIFs' trading status. This includes investment policies, held positions, profit and loss, risk indicators etc. A fund shall also fully disclose the influence of its overall risks with SIFs' investment and whether it is in compliance with set investment policies and investment objectives.

CSRC Provides Guidance for Fund Investment

Contact Details

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

Shanghai	Beijing
Christophe Han Tel: (86 21) 3135 8778 (86 10) 6655 5050 Christophe.Han@llinkslaw.com	Wayne Chen Tel: (86 10) 6655 5050 - 1022 Way.Chen@llinkslaw.com
Charles Qin Tel: (86 21) 3135 8668 (86 10) 6655 5020 Charles.Qin@llinkslaw.com	
Sandra Lu Tel: (86 21) 3135 8776 (86 10) 6655 5050 Sandra.Lu@llinkslaw.com	

This article was first published in *China Law & Practice*, July / August 2010, Volume 24, Number 6.