



MRF 2.0 Goes Live: Optimizing MRF Scheme and Expanding Cross-Border Business Opportunities

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On December 20, 2024, the China Securities Regulatory Commission (“**CSRC**”) released the *Provisions on the Administration of Recognised Hong Kong Funds* (“**MRF Regulation**”), which will come into effect on January 1, 2025. The *Interim Provisions on the Administration of Recognised Hong Kong Funds* effective from July 1, 2015 will be repealed. Nearly a decade after the implementation of the Mainland-Hong Kong Mutual Recognition of Funds (MRF) scheme (“**MRF Scheme**”), it is further optimized, releasing greater policy flexibility and business opportunities.

On the same day, CSRC released an updated version of the *Frequently Asked Questions of the China Securities Regulatory Commission on Mainland-Hong Kong Mutual Recognition of Funds* (“**CSRC FAQ**”) and an updated version of the *Guidelines on Application Documents for Registration of Recognised Hong Kong Funds*. The Hong Kong Securities and Futures Commission (“**SFC**”) also released an updated version of the *Frequently Asked Questions on Mainland-Hong Kong Mutual Recognition of Funds*. The People’s Bank of China and the State Administration of Foreign Exchange issued an amendment to the *Operational Guidelines on Capital Management for Cross-Border Offering and Distribution of Securities Investment Funds between the Mainland and Hong Kong*. These measures provide institutional guarantee for the smooth implementation of the optimized MRF Scheme.

I. Major Optimizations of the MRF Regulation

The amended MRF Regulation primarily optimizes the Northbound MRF in the following three aspects:

1. The upper limit on the value of units in a Northbound MRF fund sold to investors in the Mainland has been relaxed from the original 50% of the value of the fund’s total assts to 80%. For example, if the AUM of a Hong Kong fund is RMB 1 billion in Hong Kong, under the previous rules, the AUM of this fund sourced from Mainland distribution shall not exceed RMB 1 billion. After the implementation of the MRF Regulation, the sales scale of this fund in the Mainland is able to reach RMB 4 billion, increasing the potential scale by RMB 3 billion. Additionally, it is expected that some Northbound MRF funds currently suspending Mainland distribution due to the 50% sales limit will gradually resume subscription in the Mainland until they reach the new upper limit of 80%.
2. It is allowable to delegate the investment management functions of Northbound MRF funds to overseas asset managers in the same group with the Hong Kong managers.
 - (1) Previously, if any investment management function of a Hong Kong fund is delegated to any affiliate of the manager which is not domiciled in Hong Kong, this fund will not be eligible to apply for the distribution in the Mainland under the MRF Scheme. The MRF Regulation removes this restriction, which will enable dozens of Hong Kong funds with delegated investment functions to qualify for distribution in the Mainland through the MRF Scheme. These funds typically invest in mature markets such as the United States and Europe, and are managed by affiliates of the manager in related markets in the capacity as sub-manager or investment manager.

- (2) If any investment management function of a Hong Kong fund is delegated to an entity which is not an affiliate of the manager and is domiciled in a country or region outside Hong Kong, this fund is still not eligible to apply for the distribution in the Mainland under the MRF Scheme.
 - (3) According to the MRF Regulation, the securities regulator of the country/region where the affiliated investment delegates domicile shall have signed MoU on regulatory cooperation with CSRC and maintained effective regulatory cooperative relationship with CSRC.
3. The MRF Regulation adds the flexibility to accommodate the potential inclusion of more Hong Kong funds under the MRF scheme in the future. According to the MRF Regulation, not only conventional equity, mixed, bond and index funds (including ETFs) can participate in the MRF Scheme, but “other types of funds recognized by CSRC” may also be included in this scheme. This means that certain types of funds (such as FOF), which are currently hot topics in the market, may gradually be included in the MRF scope upon recognition by CSRC as the Northbound MRF Scheme matures.

II. Development of the Northbound MRF

Under the MRF Scheme, the distribution of Hong Kong funds in the Mainland is referred to as “Northbound MRF”, while the distribution of Mainland funds in Hong Kong is referred to as “Southbound MRF”. After nearly ten years of development, Northbound MRF has effectively met the growing diversified investment needs of Mainland investors. Currently, 41 Hong Kong funds managed by 21 Hong Kong fund managers have been registered with CSRC and are publicly offered in the Mainland.

From the perspective of Hong Kong managers, the following global asset managers, local Hong Kong asset managers and Hong Kong subsidiaries of Mainland financial institutions are actively participating in Northbound MRF business:

Global asset managers (6)	JPMorgan, Schroders, Amundi, HSBC, Pictet, UBS
Local Hong Kong asset managers (6)	Hang Seng, Zeal, BEA Union, Value Partners, Income Partners, Gaoteng
Hong Kong subsidiaries of Mainland financial institutions (9)	CCBI, BOCHKAM, BOCI-Prudential, Haitong, Bosera, ChinaAMC, E Fund, CISI, CSOP

In terms of the product type, the existing MRF funds with global theme account for a small share, while the predominance are the funds with major investment in Hong Kong stocks, China theme and Asia/Asia-Pacific theme. As of the end of October 2024, the net outflow of Northbound MRF funds amounts to RMB36.5 billion. Given that the total quota for Northbound MRF is RMB 300 billion, there remains an available quota of around RMB 260 billion for Northbound MRF funds.

III. Eligibility Requirements for Northbound MRF Funds

In line with the new provisions of the MRF Regulation, Hong Kong funds participating in the Northbound MRF Scheme shall meet the following eligibility requirements:

1. Requirements on Hong Kong Fund

- (1) **Domicile:** The proposed MRF fund is established and operates in Hong Kong in accordance with Hong Kong laws, is authorised by SFC for public offering and is regulated by SFC.
- (2) **Product type:** The proposed MRF fund shall be a conventional fund, including conventional equity, mixed, bond or index fund (including ETF), as well as any other type of fund recognized by CSRC. "Any other type of fund recognized by CSRC" leaves flexibility to the inclusion of more types of Hong Kong funds in the MRF Scheme.
- (3) **Track record:** The proposed MRF fund shall be established for more than one year. If the fund was redomiciled to Hong Kong from another jurisdiction (such as the Cayman Islands or the British Virgin Islands), it shall be redomiciled for more than one year.
- (4) **AUM:** The proposed MRF fund shall have a minimum fund size of no less than RMB 200 million or its equivalent in a different currency. The requirement of RMB 200 million refers to the size of the fund at the time submitting the MRF application, but CSRC will also take into account the fund size of a certain period prior to the submission.
- (5) **Primary investment direction:** The proposed MRF fund shall not primarily invest in the Mainland market, and its investment in the Mainland market shall not exceed 20% of the fund's assets.
- (6) **Upper limit on sales scale in the Mainland:** The value of units in the proposed MRF fund sold to investors in the Mainland shall not exceed 80% of the value of the fund's total assets.
- (7) **Dispute resolution method:** If the proposed MRF fund adopts litigation for dispute resolution, it shall not exclude the jurisdiction of Mainland courts.

2. Requirements on Fund Manager

- (1) **Qualification of the manager:** The fund manager of the proposed MRF fund shall be registered and operate in Hong Kong and hold the asset management license in Hong Kong;
- (2) **Compliance of the manager:** The fund manager of the proposed MRF fund shall not have been the subject of any major regulatory actions by SFC in the past three years or if it has been established for less than three years, since the date of its establishment. Regarding how to

determine major regulatory actions, the CSRC FAQ clearly states that “during the registration process of a Northbound MRF fund, the fund manager shall truthfully disclose to CSRC whether it has been the subject of any regulatory actions by SFC in the past three years or since the date of its establishment, and CSRC may consult SFC on the determination of ‘major regulatory actions’”.

- (3) **Delegation of investment functions:** The investment management functions of the proposed MRF fund can be delegated to any asset management institution operating in Hong Kong and holding relevant license granted by SFC, or to any asset management affiliate “within the same group”. “Within the same group” refers to that there is actual control relationship between the manager and the investment delegate, or the manager and the investment delegate are controlled by the same actual controller. Meanwhile, the securities regulator of the country/region where the affiliated investment delegate domiciles shall have signed MoU on regulatory cooperation with CSRC and maintained effective regulatory cooperative relationship with CSRC.
3. **Trustee:** The assets of the proposed MRF fund shall be under custody, and the trustee shall satisfy the eligibility requirements stipulated by SFC.
4. **Mainland agent:** A Mainland retail fund manager or Mainland bank/securities firm with custody license shall be appointed as the agent of the proposed MRF fund. The Mainland agent is responsible for handling product registration, information disclosure, distribution arrangement, data exchange, funds settlement, regulatory reporting, communication and liaison, client service, monitoring and other matters of the proposed MRF fund in the Mainland on behalf of the Hong Kong manager.

IV. Application Documents for Northbound MRF Funds

After being registered with CSRC, Northbound MRF funds can be publicly distributed in the Mainland. To apply for the registration with CSRC, Hong Kong managers shall submit registration applications to CSRC via the Mainland agents appointed by them. According to the *Guidelines on Application Documents for Registration of Recognised Hong Kong Funds*, Hong Kong managers shall submit the following materials to CSRC via Mainland agents:

1. Application report: mainly including the basic information of the fund, the fund’s fulfillment of registration conditions, the fund’s Mainland agent, arrangements for distribution and information disclosure in the Mainland, as well as issues that require special attention from the regulator
2. Fund documents, including:
 - Trust Deed;
 - PRC Prospectus and Product Key Facts Statement (KFS);

3. Explanatory statements and undertaking letters about the fund documents:
 - Explanatory statement on whether there are any differences between the Trust Deed, Prospectus and KFS to be released in the Mainland and SFC-approved versions, and the reasons for such differences;
 - Statement confirming that the Trust Deed is the latest complete version authorised by SFC;
 - Statement confirming that the consolidated prospectus and the SFC-authorised version in other languages are consistent with each other and both versions have equal effect;
 - Statement confirming that the Simplified Chinese versions of the registration application documents and offering documents are consistent with and have the same effect as the other language versions authorised by SFC;
4. Agency agreement duly executed by Hong Kong manager and the Mainland agent for the Northbound MRF fund;
5. Other relevant fund materials, including:
 - SFC's approval letter for authorising the fund;
 - Latest audited annual financial report of the fund;
 - Statement on the daily AUM of the fund during the recent one month;
6. Eligibility statement and supporting documents for the manager, trustee, and Mainland agent (registration certificates, licenses, etc.);
7. PRC legal opinion issued by a PRC law firm;
8. Other materials required by CSRC.

According to the MRF Regulation, relevant materials should satisfy the following requirements:

- (1) Being written in Simplified Chinese;
- (2) Relevant terminology shall conform to the practice of the Mainland fund industry;
- (3) If the original is in another language, a true, accurate, and complete Simplified Chinese translation shall be provided.

Given that Hong Kong documents, such as fund documents and annual reports, are typically available only in English or in both English and Traditional Chinese versions, and that the terminology used in Traditional Chinese versions differs from Mainland financial market conventions, Hong Kong managers shall prepare Simplified Chinese translations of relevant documents in advance. These Simplified Chinese translations shall not only truthfully, accurately and completely reflect the content of the original language versions, but shall also optimize and adjust the terminology, wording, and expressions to align with Mainland fund industry practices and Mainland regulators' reading and review habits.

V. Updates of Existing Northbound MRF Funds

For Northbound MRF funds that have been approved and are publicly distributed in the Mainland, the current Mainland offering documents specify a 50% limit on Mainland distribution. Hong Kong managers shall promptly initiate updates to the Mainland offering documents, and release updated versions as soon as possible after the MRF Regulation takes effect on January 1, 2025, so as to validate subsequent Mainland distribution. For Northbound MRF funds that have currently suspended Mainland subscription due to the 50% limit, in addition to the aforementioned document modifications, Hong Kong managers can also begin preparing relevant announcements to resume Mainland subscription after the MRF Regulation takes effect.

VI. Participants in Northbound MRF Business

In the Northbound MRF business, Hong Kong managers need to appoint the following Mainland institutions to carry out the distribution of Northbound MRF funds:

- (1) Engaging a Mainland institution as the Mainland agent
- (2) Engaging the Mainland fund distributors to distribute Northbound MRF Funds
- (3) Engaging China Securities Depository and Clearing Corporation Limited (“**CSDC**”) to provide services such as unit registration, distribution data transfer, fund settlement
- (4) Engaging Shenzhen Securities Communication Co., Ltd. (“**SSCC**”) to handle data conversion and transmission for Northbound MRF funds

1. Mainland Agents

As mentioned above, the Hong Kong manager needs to engage a Mainland agent which is either a Mainland retail fund manager or a Mainland institution with custody license for securities investment funds, to handle relevant matters for Northbound MRF funds in the Mainland.

According to public information disclosed by CSRC, among the 41 approved Northbound MRF funds, there are 11 Hong Kong managers engaging affiliates in the Mainland as their Mainland agents of the Northbound MRF funds. For example, JPMorgan engages JPMorgan Asset Management (China) Company Limited, HSBC AM engages HSBC Jintrust Fund Management Company Limited, Amundi engages ABC-CA Fund Management Co., Ltd., Schroders engages BOCOM Schroders Fund Management Co., Ltd. as their Mainland agents. There are 10 Hong Kong managers managing total 16 funds that engage independent non-affiliated fund management companies or banks with fund custody license as Mainland agents. Among these independent Mainland agents, Tianhong is the most active one, which provides agency services for total 9 Northbound MRF funds of 5 Hong Kong managers.

Choosing a retail fund manager as the Mainland agent, especially when the Hong Kong manager has a Mainland affiliated retail fund manager, can take advantage of the extensive market foundation and client resources of the Mainland retail fund manager. The retail fund manager can organize distribution network to expand the distribution of Northbound MRF funds in the Mainland. Meanwhile, it can also leverage the retail fund manager's years of compliance experience in fund distribution and information disclosure, thereby providing experiential support for the distribution, information disclosure and regulatory reporting of Northbound MRF funds in the Mainland.

In recent years, with the steady progress of capital market opening-up, 9 foreign institutions have established WFOE FMCs (wholly foreign-owned retail fund management companies) in China, including BlackRock, Neuberger Berman, FIL, Schroders, AllianceBernstein, Allianz, Manulife, JPMorgan and Morgan Stanley. WFOE FMCs have a unique advantage in terms of onshore and offshore resource integration and in promoting the deep involvement of offshore affiliates in the Northbound MRF business.

In terms of custodian banks, currently 5 WFOE banks (wholly foreign-owned banks) have been approved for securities investment fund custody license, including Standard Chartered, Citibank, Deutsche Bank, BNP Paribas and HSBC. If the group to which the WFOE custodian bank belongs has long-term cooperation with the group to which the Hong Kong manager belongs, and the WFOE custodian bank holds the fund distribution license, such WFOE custodian bank can provide one-stop services that combine both of agency and distribution services for Northbound MRF funds. WFOE banks can effectively extend their rich resources and professional advantages accumulated in the bank QDII to the market of Northbound MRF funds which offers a larger investment quota capacity, fully leveraging their inherent advantages in cross-border asset allocation and wealth management.

2. Mainland Distributors

According to the MRF Regulations, Hong Kong managers can either directly or engage the Mainland agents to sign the distribution agreements with Mainland distributors. In practice, there are three models for signing distribution agreements:

- (1) Hong Kong managers directly sign bilateral agreements with Mainland distributors;
- (2) Mainland agents sign bilateral agreements with Mainland distributors based on authorization from Hong Kong managers;
- (3) Hong Kong managers and Mainland agents jointly sign trilateral agreements with Mainland distributors.

The direct involvement of Hong Kong managers in the negotiation of distribution agreements and the appointment of Mainland distributors allows for better control of the distribution process and strategy, and greatly reduces compliance and legal risks. However, since Hong Kong managers may not have cooperation with Mainland distributors before, this model usually entails higher due

diligence costs and increased coordination efforts. In contrast, Mainland agents are more familiar with the domestic market, allowing them to provide sales strategies and customer services that are better tailored to local market conditions and leverage past sales experience and long-term cooperative relationships with relevant distributors. Hong Kong managers can choose the most suitable cooperation model by considering the actual needs and the mainland distribution arrangement.

3. CSDC and SSSC

The MRF Regulation requires Hong Kong managers to appoint Mainland agents to exchange data with fund distributors through technical platforms designated by CSRC. Currently, most Hong Kong managers of Northbound MRF funds authorize the Mainland agents to sign agreements with CSDC via which the Mainland agents engage CSDC to provide services such as unit registration, distribution data transfer, fund settlement. Additionally, Mainland agents need to engage SSSC to handle data conversion and transmission for Northbound MRF funds.

When engaging CSDC with unit registration and data transfer, Hong Kong managers shall conduct business testing with CSDC during their initial onboarding to CSDC's TA platform for open-end funds. If Hong Kong managers appoint new registrars in Hong Kong, they shall coordinate with these registrars to join CSDC's TA platform and participate in business testing. It is important to note that CSDC currently requires registrars accessing their system to be institutions registered and operating in Hong Kong. We have observed that some Hong Kong retail funds use registrars based in Luxembourg, Cayman Islands or the British Virgin Islands. If such funds intend to register as Northbound MRF funds for Mainland distribution, additional work may be necessary so as to access CSDC's system.

VII. Conclusion

The optimization of MRF Scheme will better serve the cross-border investment needs of investors in both the Mainland and Hong Kong, promote high-level institutional opening-up of Mainland capital markets, further strengthen Hong Kong's position as an international financial center, and provide global asset management institutions with more business opportunities.

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