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Impact of the New Disclosure Measures on Northbound MRF Funds

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Since the implementation of the *Interim Provisions on the Administration of Recognised Hong Kong Funds* (香港互认基金管理暂行规定, the "**MRF Interim Provisions**") on 1 July 2015, there has been 20 Northbound MRF funds which have been registered with the China Securities Regulatory Commission ("**CSRC**") and been permitted to be publicly offered in Mainland China. The information disclosure of Northbound MRF funds in Mainland should comply with the regulatory requirements of Hong Kong Securities and Futures Commission ("**SFC**") and the funds' legal documents, meanwhile, how the Mainland China funds information disclosure rules apply to Northbound MRF funds and relevant impact of the rules should be noted.

On 26 July 2019, CSRC released the *Administrative Measures on Information Disclosure of Publicly-raised Securities Investment Funds* (公开募集证券投资基金信息披露管理办法, the "**Disclosure Measures**") and the *Provisions on Issues Relating to Implementation of the Administrative Measures on Information Disclosure of Publicly-raised Securities Investment Funds* (关于实施《公开募集证券投资基金信息披露管理办法》有关问题的规定, the "**Implementing Provisions**"), which took effect from 1 September 2019, while part of the provisions requesting system improvement of fund distributors in order to comply with the *Disclosure Measures* will take effect from 1 September 2020. This article aims to summarize the application principles and the impact of the *Disclosure Measures* to the Northbound MRF funds.

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I. Principles of Application of the *Disclosure Measures* to the Northbound MRF Funds

According to Article 41 of the *Disclosure Measures*, "as to the MRF funds registered with CSRC, if onshore information disclosure is involved, the *Disclosure Measures* shall be followed, except as otherwise required by laws and regulations and CSRC". It is provided in Article 7 of the *MRF Interim Provisions* that, "the content, format, timing, frequency and events regarding the information disclosure documents of a Northbound MRF fund in the Mainland (including the offering document, KFS, publication of net asset value, periodical financial reports and ad hoc announcements) shall comply with the regulatory requirements of the SFC and the fund's legal documents, except as otherwise provided herein". Article 7 of the *MRF Interim Provisions* can be deemed to be "as otherwise required by laws and regulations and CSRC" stipulated in Article 41 of the *Disclosure Measures*. Therefore, the scope of application of the *Disclosure Measures* to Northbound *MRF* funds can be reasonably extended to those information disclosure matters that only relate to Mainland distribution and Mainland investors while there is no information disclosure requirement and rules in Hong Kong.

1. Principles of Information Disclosure

(1) The *Disclosure Measures* shall be followed where the information to be disclosed is solely relating to the Northbound MRF fund's Mainland distribution and Mainland investors, and also Hong Kong rules and the Northbound MRF fund's Hong Kong legal documents keep silent on how to disclose such information. Northbound MRF fund managers are reminded to pay attention to the following:

- For the events such as disclosing the dividend distribution of the share class(es) offered in Mainland only, change of the accrual basis, accrual method or fee rate of the ongoing sales service fee (if any), Mainland subscription fee and redemption fee, error of calculating the NAV per unit of the share class(es) offered in Mainland reaching 0.5% and suspension / resumption of subscription and redemption in Mainland, the Northbound MRF fund managers should at least issue interim announcement within 2 days of the occurrence of the event according to Article 21 of the *Disclosure Measures*. Prior announcements should still be issued if PRC Cover of the Northbound MRF funds or common practice adopts prior announcement for certain events, such as changing the Mainland subscription / redemption fee rate within the maximum fee rate as specified in Hong Kong offering documents, and suspension / resumption of subscription and redemption in Mainland.

- Where there is change to the Mainland subscription / redemption fee rate specified in PRC OD and PRC KFS, for prudent purpose, it is suggested that PRC OD and PRC KFS be updated and disclosed within 3 working days after the change. Previously, some Northbound MRF funds only disclosed the change of the Mainland subscription fee rate by issuing announcement, but did not update PRC OD and PRC KFS in time. After the implementation of the *Disclosure Measures*, PRC OD and PRC KFS should at least be updated as a restated version within 3 working days after the announcement is issued.

- Where there is an amendment to the trust deed, and the contents in the trust deed to be amended have been quoted in PRC OD and PRC KFS (such as the rights and obligations of fund parties, procedures and rules of unitholders' meeting, events and procedures for the termination of the fund and dispute resolution), for prudent purpose, it is suggested that PRC OD and PRC KFS be updated as a restated version within 3 working days after such change takes effect.

(2) If an event to be disclosed only relates to the Northbound MRF fund's distribution in Mainland and Mainland investors, while in Hong Kong, there are disclosure requirements and rules on such event, Hong Kong regulatory requirements must be followed.

For example, Article 14 of the *Disclosure Measures* relating to disclosure details and frequency of NAV is not applicable to the Northbound MRF funds. Although Northbound MRF funds usually set up share class(es) to be distributed in Mainland only, the calculation and disclosure of NAV of such share classes must follow the fund's Hong Kong legal documents.

(3) If an event to be disclosed only relates to the Northbound MRF fund's distribution in Mainland and Mainland investors, while the *MRF Interim Provisions* have clearly stipulated the information disclosure matters for such event, the information disclosure should be made in accordance with the *MRF Interim Provisions* rather than the *Disclosure Measures*.

For example, Article 9 of the *MRF Interim Provisions* requires that the offering related documents (including PRC OD, PRC KFS, offering announcement, trust deed, annual report and semi-annual report) of a Northbound MRF fund must be disclosed at least 3 days before launch in Mainland. Thus, the Northbound MRF fund will not be subject to the requirements on disclosure of the offering related documents as stipulated in Article 10 of the *Disclosure Measures*.

(4) Where an event may simultaneously affect a Northbound MRF fund's Hong Kong investors and Mainland investors, such event should, according to Article 7 of the *MRF Interim Provisions*, be disclosed according to SFC's regulatory requirements and the fund's legal documents and by following the principle of equal treatment of Hong Kong and Mainland investors. If an event is

required to be disclosed in Hong Kong according to Hong Kong regulatory requirements or the fund's legal documents or Hong Kong common practice, such event should be disclosed to Mainland investors simultaneously with the disclosure to Hong Kong investors based on equal treatment principle. If an event is not required by Hong Kong regulatory requirements or fund's legal documents or Hong Kong common practice to be disclosed to Hong Kong investors, it is not required to follow the *Disclosure Measures* to disclose such event in Mainland, otherwise it may trigger unequal treatment to Hong Kong investors. For example:

- Article 16 of the *Disclosure Measures* requires that the annual reports of funds shall be disclosed within 3 months from the end of each year. However, the Hong Kong fund managers only need to comply with SFC's regulatory requirements to disclose the annual reports of Northbound MRF funds to Hong Kong investors and Mainland investors simultaneously within 4 months from the end of each financial year.

- Article 18 of the *Disclosure Measures* requires that quarterly reports of funds shall be prepared. However, it is not required to prepare and disclose quarterly reports of Northbound MRF funds since quarterly reports are not required under Hong Kong regulatory requirements.

- Article 22 of the *Disclosure Measures* requires that the announcement of convening unitholders' meeting shall be disclosed at least 30 days in advance. However, Northbound MRF funds only need to disclose the announcement of convening unitholders' meeting to Hong Kong investors and Mainland investors simultaneously at least 21 days in advance in accordance with Hong Kong regulatory requirements.

- Paragraph 11 of Article 21 of the *Disclosure Measures* requires that, an interim announcement shall be disclosed within 2 days if more than 50% of the fund manager's directors are changed within the most recent 12 months. However, Northbound MRF funds only need to disclose the change of the fund manager's directors when updating the list of directors in Hong Kong offering documents. It is not required for Northbound MRF funds to specifically prepare such interim announcement and to comply with such disclosure timeline.

2. Disclosure Channels

The principle is that, Northbound MRF funds should make information disclosure through Mainland agent's website and the CSRC's electronic disclosure website in accordance with the *MRF Interim Provisions*.

Given that the information disclosure channel of Northbound MRF funds is stipulated in Article 8 of the *MRF Interim Provisions*, it is a case where "as otherwise required by laws and regulations and CSRC" as stipulated in Article 41 of the *Disclosure Measures*. Therefore, Northbound MRF funds need not make information disclosure thoroughly via the channels as stipulated in the *Disclosure Measures*.

3. Penalty for Violation of the *Disclosure Measures*

According to Paragraph 2 of Article 41 of the *Disclosure Measures*, in case of any violation of the *Disclosure Measures* by MRF fund managers and Mainland agents with respect to the MRF funds' information disclosure, CSRC has authority to adopt administrative supervision measures or administrative punishment on them according to law. The penalty principle in this provision is also in line with Articles 24, 25 and 26 of the *MRF Interim Provisions*, i.e., where a Northbound MRF fund manager violates the information disclosure requirements in the *Disclosure Measures* or the *MRF Interim Provisions*, the CSRC has authority to adopt administrative supervision measures or administrative punishment on it according to law; while where a Northbound MRF fund's Mainland agent violates the information disclosure requirements in the *Disclosure Measures* or the *MRF Interim Provisions*, the CSRC has authority to adopt administrative supervision measures such as to order it to rectify within a certain period and regulatory conversation.

II. Information Delivery Obligations of Mainland Distributors

In order to make funds information disclosure more effective, Article 29 of the *Disclosure Measures* imposes Mainland distributors obligations of delivering information to retail fund investors, which is also applicable to Northbound MRF funds' Mainland distribution. Such information delivery obligations are elaborated in Article 9 of the *Implementing Provisions*, which include:

1. Mainland distributors shall remind Mainland investors of reading and confirming PRC KFS before they subscribe the Northbound MRF funds;

2. Under the extreme circumstance where a Northbound MRF fund faces or potentially faces significant risks, Mainland distributors shall timely warn the Mainland investors of such risks;

3. Mainland distributors shall timely notify the Mainland investors of the convening of unitholders' meeting.

Northbound MRF fund managers and the Mainland agents should pay attention to such information delivery obligations of Mainland distributors and timely provide relevant information to Mainland distributors.

The provisions about such information delivery obligations of Mainland distributors will be implemented from 1 September 2020. Mainland distributors should, within the transition period, complete the system improvement including upgrading the online distribution system to add the procedure to have Mainland investors to confirm the PRC KFS online, or adjusting the offline distribution procedures.

III. KFS

1. Impact on PRC KFS of Northbound MRF Funds

CSRC also released *Template No.5 (KFS) for Information Disclosure of Publicly-raised Securities Investment Funds* (公开募集证券投资基金信息披露 XBRL 模板第 5 号《基金产品资料概要》, the “**KFS Template**”) as detail rules of the *Disclosure Measures*, in which Article 10 provides the principle of application of the *KFS Template* to MRF funds.
According to such provision, the *KFS Template* does not apply to the Northbound MRF funds, so it does not have impact on the contents and format of the approved Northbound MRF funds’ PRC KFS.

If in the future MRF regime is further initiated between Mainland China and other jurisdictions, and there is no regulatory requirement in such other jurisdictions on preparing KFS, such MRF funds shall prepare PRC KFS by following the *KFS Template*.

2. Comparison of *KFS Template* between Mainland China and Hong Kong

KFS is introduced in Mainland retail fund industry by drawing SFC’s regulatory experience. The document structure and important statement of KFS required in the *KFS Template* are similar with the requirements of Hong Kong KFS in general, while differences exist due to the discrepancies in product features and product regulations between Mainland China and Hong Kong. For example, the *KFS Template* requires to disclose the benchmark and the risk and return feature, while there is no such requirement on Hong Kong KFS. For another example, different from Mainland, lots of Hong Kong funds set up multiple share classes, as such the fund performance should be disclosed by adopting the performance of a representative share class in form of a bar chart, with relevant reminder to investors.

Compared to Hong Kong KFS, the *KFS Template* adds certain disclosure requirements based on Mainland retail funds’ features and disclosure practices. For example, compared to Hong Kong KFS, the *KFS Template* has following additional requirements: in the section of “Product Overview”, the *KFS Template* requires to disclose the short name of the fund, investment adviser, fund type, operation model and the profile of the portfolio manager; in the section “Fund Investment and NAV Performance”, it is required that the assets allocation and regions allocation in a portfolio should be shown in form of pie chart; in the important statement part under the section "Risk Disclosures and Important Statements", the *KFS Template* requires fund managers to make statements about their prudent management and the accordance and ground of investors becoming unitholders; in the section "How to Inquire Other Information", the *KFS Template* requires to exhaustively list the documents available for inquiring.

Different from Hong Kong KFS, the *KFS Template* does not require to disclose minimum investment amount, or to disclose ongoing charges which represent the aggregate fees paid out of the fund assets.

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