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Brief Analysis on the Measures on Supervision and Administration of Private Investment Funds (Draft for Consultation)

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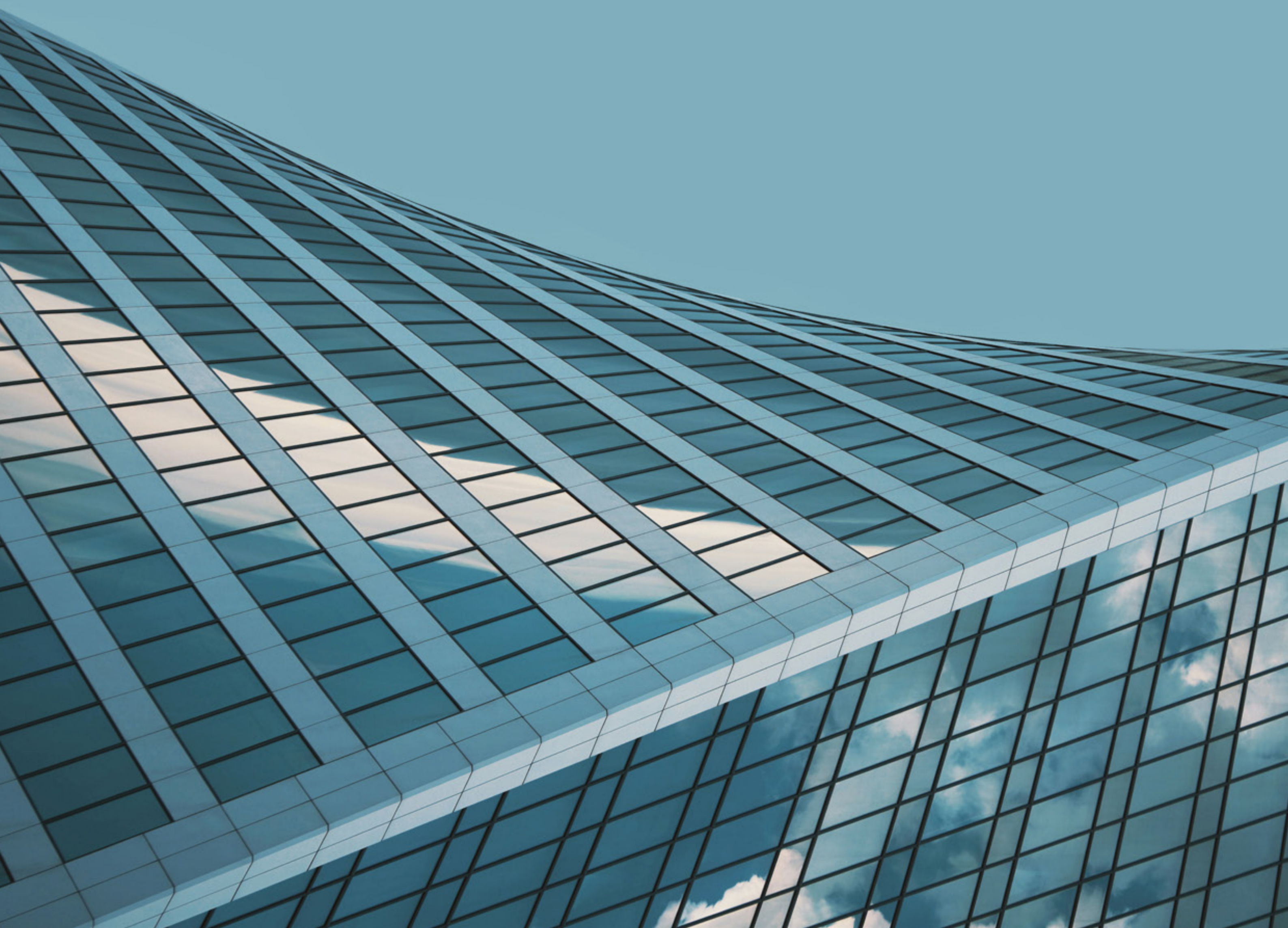

On 30 June 2014, the China Securities Regulatory Commission ("**CSRC**") promulgated the *Interim Measures on Supervision and Administration of Private Investment Funds* (the "**Interim Measures**"), integrating private funds into the regulatory framework by formulating departmental regulations, establishing basic requirements for registration and filing of private funds, qualified investors, fundraising, investment operation, etc. Since the promulgation of the Interim Measures, private funds have witnessed rapid development, leading to new requirements for the direction and content of the supervision and administration of private funds. To further promote the standardized and healthy development of the industry and implement the requirements in the *Regulation on Supervision and Administration of Private Investment Funds* (the "**Private Fund Regulation**") of the State Council, CSRC promulgated the *Measures on Supervision and Administration of Private Investment Funds (Draft for Consultation)* (the "**Private Fund Measures**") on 8 December 2023, proposing a comprehensive revision to the Interim Measures.

The Private Fund Measures consist of 10 chapters and 82 articles, putting forward many new requirements in respect of qualification and compliant operation of private fund managers, design of private fund products, fundraising and investment operation, etc. This article provides a brief analysis of the Private Fund Measures from the perspective of private securities fund managers and private securities investment funds.

I. Grace Period and Rectification Requirements in the Private Fund Measures

The regulations and self-disciplinary rules related to private funds promulgated in the past usually had a “new-old cut” arrangement and did not apply retroactively to certain extent. For instance, the *Measures for Registration and Filing of Private Investment Funds* (the "**Registration and Filing Measures**") issued by the Asset Management Association of China ("**AMAC**"), effective on 1 May 2023, did not require the existing private fund managers (the “PFM”) and private funds to fully rectify in accordance with the new requirements of the Registration and Filing Measures, while the new rules in the case of any change in relevant matters after the implementation of the Registration and Filing Measures shall be complied with.

The Private Fund Measures set unprecedentedly strict rectification requirements, which will have material impact on existing PFMs and private funds. For registered PFMs that do not comply with the new rules, except for the name, business scope, paid-in capital, and senior management personnel’s shareholding in PFMs, which are not required to be rectified according to the new rules, all other matters shall be rectified within one year from implementation of the Private Fund Measures. For existing private funds filed with AMAC that do not comply with the new rules, despite the “new-old cut” principle, before the completion of the rectification, they are **not allowed to make new investment**, increase new fundraising, onboard new investors, or extend the fund duration, and private funds shall be liquidated upon the expiration of the fund contract. The prohibition on new investments significantly impacts most existing private funds. Without rectification in accordance with the new rules, the investment operation of such private funds may only "exist in name". If the existing private funds do not meet the requirement of Article 54 of the Private Fund Measures regarding multilayered nesting restrictions, even without new investment, they shall complete rectification within two years from the implementation of the Private Fund Measures. The Private Fund Measures also establish a relatively strict supervision mechanism, under which AMAC will make special announcements about the PFMs and private funds that fail to complete rectification by the due date, and depending on the severity, will take self-disciplinary management measures or disciplinary actions.

II. Ongoing Qualification Requirements for PFMs

Paragraph 1 of Article 7 of the Private Fund Measures establishes the qualification requirements for PFMs in respect of company name, business scope, paid-in capital, financial conditions, capital contribution structure, personnel requirements and basic infrastructures. It also emphasizes that PFMs shall meet these requirements on an ongoing basis.

We note that most of the requirements in this article are substantially consistent with those set forth in the Registration and Filing Measures and the implementation guidelines. With regard to the existing PFMs not complying with the Paragraph 1 of Article 7 of the Private Fund Measures, the Private Fund Measures set out rectification requirements based on different circumstances, which set out as follows:

1. Qualification Requirements (existing PFMs are not required for rectification)

No.	Qualification Requirements
1	Having a name and business scope that comply with relevant requirements;
2	Being in good financial conditions; the minimum paid-in monetary capital shall be commensurate with the PFM's assets under management, of which the initial paid-in monetary capital shall be no less than RMB 10 million;
3	The legal representative, executive partner or authorized representative, and the senior management personnel in charge of investment management shall have relevant working experience, and the total equity interests or property shares held by them shall be no less than 20% of the minimum initial paid-in monetary capital of the PFM. PFMs controlled by financial institutions, PFMs controlled by governments at or above the level of city divided into districts and their authorized authorities, and PFMs controlled by institutions regulated by offshore financial regulatory authorities are exempted from this requirement.

	Note: we understand that, for existing PFMs, this exemption mainly applies to the shareholding requirements for the legal representative, executive partner, and the senior management personnel in charge of investment management. If an existing PFM changes the aforementioned personnel, the new personnel shall also "have relevant working experience ", which is currently clearly stipulated in the Registration and Filing Measures.

2. Qualification Requirements (existing PFMs shall complete rectification within one year from the implementation of the Private Fund Measures)

No.	Qualification Requirements	Highlights
1	The capital contribution structure of a PFM shall be concise, clear and stable, and its controlling shareholder, general partner and actual controller shall have good financial condition and good integrity record, and **shall have relevant working experience in investment and asset management, etc.**	The controlling shareholder, general partner and actual controller may also be institutions. We suggest replacing the term "working experience" with "relevant experience" to include the circumstance of institutions in the Private Fund Measures. The Registration and Filing Measures stipulate specific requirements of "relevant experience" for the controlling shareholder, general partner and actual controller, specifying that the controlling shareholder, actual controller and general partner shall have relevant experience in operating, managing, or engaging in asset management, investment or related industries for **at least five years**. If the relevant experience requirements of the Private Fund Measures refer to those in the Registration and Filing Measures, there might be a large number of PFMs in the market facing restructuring of their equity structure, which will have a wide impact.
2	A PFM **shall have senior management personnel** and other fund practitioners **meeting the required number, competence requirements** and integrity record.	(1) Is it necessary to appoint the senior management personnel in charge of investment management? Article 26 of the Private Fund Regulation explicitly requires that PFMs shall employ senior management personnel with corresponding professional experiences to be

		responsible for investment management, risk control, compliance, etc. As part of the existing PFMs in the market have not appointed senior management personnel in charge of investment management, it is necessary to appoint such personnel as soon as possible during the grace period of the Private Fund Measures.[1] (2) Competence requirements for senior management personnel The Private Fund Measures do not further stipulate on the competence requirements that senior management personnel shall meet, that may refer to specific requirements in the Registration and Filing Measures and the implementation guidelines thereof. Comprehensive rectification of the existing PFMs during the one-year grace period may lead to changes of some senior management personnel. It is anticipated that the official version of Private Fund Measures will clarify the above issues.
3	A PFM shall have qualified **<u>information technology system, security facilities</u>**, other facilities in relation to the private fund management business, and independent business premises;	It puts forward more explicit requirements on IT systems and security facilities.
4	A PFM shall have qualified internal governance structure, **<u>conflict of interest prevention and accountability mechanism</u>**, and internal policies to ensure independent compliance and risk control and effective performance of duties	It is suggested that PFMs shall sort out its internal control policies to ensure that relevant mechanisms are in place.

[1] It shall be noted that PFMs shall appoint senior management personnel in charge of investment management, but if the general manager or deputy general manager of the PFM is competent and capable to be responsible for investment, such personnel can also serve as the personnel in charge of investment management. As such, it is not mandatory to set up a dedicated chief investment officer in addition to the general manager and deputy general manager.

According to the Paragraph 2 of Article 7 of the Private Fund Measures, the controlling shareholder and actual controller of a PFM shall make a written commitment not to transfer its equity interests or actual control within three years after the registration or change of registration of the PFM, which is consistent with requirements under the Registration and Filing Measures and the implementation guidelines. However, the Registration and Filing Measures also specify a reasonable circumstance of exemption[2], that is, the equity interests or actual control can be transferred within three years upon the occurrence of certain circumstances. It remains to be seen whether such reasonable exemption will be included in the official version of the Private Fund Measures.

III. Qualification Requirements for the PFM Acting as the Securities Investment Advisor

In accordance with Article 13 of the Private Fund Measures, in addition to privately raising funds and conducting investment management, PFMs may also provide securities investment advisory services to asset management product[3] launched by financial institutions. With respect to qualifications of securities investment advisors, the previous laws and regulations mainly stipulated from the perspective of financial institutions, setting forth what qualifications third parties (e.g. PFMs) shall meet to be engaged by financial institutions to provide investment advisory services. Articles 14 and 15 of the Private Fund Measures, for the first time, set forth from the perspective of PFMs the requirements on qualifications, code of conduct and duty performance for their provision of securities investment advisory services.

1. Providing securities investment advisory services to asset management products launched by institutions regulated by CSRC

   According to the *Interim Regulation on Administration of Operation of Private Asset Management Business of Securities and Futures Business Institutions* (the "**New Eight Bottom Lines**") effective on 18 July 2016, any securities PFM meeting the "1 + 3 + 3 Conditions" may act as the investment advisor for private asset management plans launched by securities and futures business institutions and private securities investment funds. The same provisions were also made in the detailed rules on private asset management business issued by CSRC (the "**PAM rules**") which were released in order to echo the *Guiding Opinions on Regulating the Asset*

[2] Exemption circumstances include: (1) the equity interests or property shares are transferred in administrative means or changed in accordance with regulations; (2) the equity interests or property shares are transferred between different entities controlled by the same actual controller; (3) the PFM implements an employee stock ownership plan without changing the status of its actual controller; (4) the equity interests or property shares are obtained due to inheritance or other statutory reasons; (5) other circumstances required by regulatory authorities

[3] It specifically refers to the asset management products stipulated in the item (2) of Article 42 of the Private Fund Measures, that is, asset management products launched in accordance with the law by institutions established in accordance with the law and subject to the regulation of the financial regulatory authority of the State Council (including securities companies and their subsidiaries, fund management companies and their subsidiaries, futures companies and their subsidiaries, commercial banks and their wealth management subsidiaries, insurance companies, insurance asset management companies, financial asset investment companies, trust companies, finance companies and other institutions specified by CSRC).

Management Business of Financial Institutions ("**Guiding Opinions**") of the People's Bank of China. Based on the existing provisions, Article 14 of the Private Fund Measures has enhanced the qualification requirements for PFMs to serve as securities investment advisors to certain extent. Please refer to the comparison table below for details.

Qualification Requirements	"1 + 3 + 3 Conditions"	Article 14 of the Private Fund Measures
Number of years registered with AMAC	The PFM shall have been **one year** since the registration with AMAC.	The PFM shall have been **three years** since the registration with AMAC.
Requirements for investment management personnel	The PFM shall have **at least 3 investment management personnel with traceable track record of securities and futures investment management for more than three consecutive years** and no negative practicing record.	The PFM shall have **investment management personnel with required numbers and qualified track record** and without any negative practicing record.
Compliance Requirements	The PFM shall have no record of material violation of laws and regulations.	The PFM shall have stable compliance and risk control, and neither the PFM nor its controlling shareholder, actual controller, legal representative, senior management personnel and investment management personnel has been involved in any of the circumstances stipulated in Article 8 and Article 9 of the Private Fund Regulation in the last five years.
Others	The PFM shall hold membership of AMAC.	Other requirements stipulated by CSRC

(1) Issues regarding the application of rules

Regarding the inconsistencies listed in the above table, based on the principle that the new law prevails over the old law, we understand that, the provisions set forth in the Private Fund Measures (e.g. 3 years of registration term) shall prevail. With regard to the specific requirements for the number of investment management personnel and track record, if there is no specific provision in the official version of the Private Fund Measures, further clarification may be needed from CSRC or AMAC in the supporting documents. It remains to be seen whether the criterion of "at least 3 investment management personnel with traceable track record of securities and futures investment management for more than three consecutive years" set forth in the "New Eight Bottom Lines" will continue to apply.

(2) Whether to allow to appoint investment advisor for private securities investment funds, and whether to allow PFMs to act as investment advisors of other private securities investment funds

According to Article 27 of the Private Fund Regulation, where a PFM appoints other entities to provide securities investment advisory services for the PFM, the entities accepting the appointment shall be the investment advisor stipulated in the *Securities Investment Funds Law*. Although the *Securities Investment Funds Law* does not stipulate the qualifications of investment advisor for private funds, we understand that according to the Private Fund Regulation as the higher-level law of the Private Fund Measures, it is allowed to appoint investment advisors for private securities investment funds. Previously, according to the "New Eight Bottom Lines", it is allowed to appoint securities and futures business institutions or securities PFMs meeting "1 + 3 + 3 Conditions" to provide investment advisory services for private securities investment funds. However, Articles 13 to 15 of the Private Fund Measures only stipulate the PFMs' provision of securities investment advisory services for the asset management product of financial institutions. It remains to be clarified whether the "New Eight Bottom Lines" shall still be followed with respect to the investment advisory services for private securities investment funds, and whether private securities investment funds would also be included in Item (2) of Article 13 in the official version of the Private Fund Measures.

2. Providing securities investment advisory services to asset management products launched by institutions regulated by the National Financial Regulatory Administration

When a PFM provides investment advisory services to such products, in addition to complying with the provisions of Article 14 of the Private Fund Measures, it shall also meet the qualification requirements stipulated in applicable laws and regulations of such financial institutions and their asset management products. For example, where a PFM provides investment advisory services for insurance asset management products, it shall also meet the relevant conditions stipulated in the *Interim Measures on Administration of Insurance Asset Management Products*, including but not limited to that key personnel shall possess professional knowledge and skills, and have at least three years of relevant business experience, and the entity shall be free of any violation of laws and regulations in investment advisory business in the last three years.

In addition, the Private Fund Measures clearly stipulate the duties and code of conduct of a PFM acting as a securities investment advisor, including giving investment advice in accordance with the investment advisory agreement, refraining from directly executing investment orders, treating the private funds under its management and investment advisory products in a fair manner, preventing conflicts of interest, clarifying the decision-making process of the formation of investment advice, and keeping records, etc. PFMs shall also file the information on investment advisory products with AMAC.

IV. Specifying Requirements for the Utilization of Proprietary Funds of PFMs

1. PFM’s Proprietary Investment in Funds Managed by Itself or Its Affiliates

   Where a PFM invests in a fund managed by itself or a private fund managed by any of its affiliates with proprietary funds, the PFM shall enjoy the same rights and interests and assume the same risks with the equal shares held by other investors in the private fund. This requirement of equal rights and responsibilities also applies to the controlling shareholder, general partner, actual controller, senior management personnel or investment management personnel of the PFM where they make proprietary investments into the private funds managed by the PFM or any of its affiliates.

2. Segregation Requirements for Investment with Proprietary Funds

   In addition to investing in private funds managed by the PFM or managed by its affiliates, a PFM should prudently carry out other investment activities with its proprietary funds only when necessary. The PFM shall formulate a dedicated management policy for the use of its proprietary funds and make clear segregation arrangements in respect of personnel, finance, accounts, systems and business, etc., to effectively prevent horizontal competition and conflicts of interest. The PFM shall also fulfill the obligations of information reporting.

V. Restrictions on Establishment of Branches and Subsidiaries by PFMs

According to the *Certain Provisions on Strengthening the Regulation of Private Investment Funds* promulgated by CSRC, PFMs shall not, directly or in a disguise way, establish any branch for the purpose of engaging in fundraising activities, while Article 19 of the Private Fund Measures prohibits PFMs from funding to establish any branch. Furthermore, according to the arrangements of the grace period for rectification set up by the Private Fund Measures, existing PFMs that have already established branches shall complete the rectification within one year. This prohibition represents a significant change from previous regulatory provisions and market practice and is noteworthy.

The Private Fund Measures also impose restrictions on the establishment of onshore subsidiaries by PFMs, including:

1. It shall be necessary, i.e., the subsidiary must be established in order to manage the private fund assets;

2. PFMs shall include the subsidiaries under unified compliance and risk control management, and report to AMAC and local branches of CSRC where the PFMs are domiciled and where the subsidiaries are established in a timely manner.

In addition, a PFM carrying out offshore private fund business activities may have two ways, including having itself to be licensed directly with an overseas regulator as a foreign entity and establishing an offshore subsidiary to be licensed with an overseas regulator. According to the Private Fund Measures, the securities regulatory authority of the country or region where offshore private fund business activities are domiciled shall have entered into a memorandum of understanding on securities regulatory cooperation with CSRC or other authorities recognized by CSRC, and shall comply with national regulations on foreign exchange administration and cross-border investment.

VI. Relevant Requirements for Private Securities Investment Funds

The Private Fund Measures comprehensively regulate private securities investment funds from the perspective of private fund product design, criteria for qualified investors, fundraising and investment operations. We summarize and analyze relevant key points and highlights as follows.

1. Custody Arrangement and Duties of Custodians

According to the current laws and regulations, private funds shall be under custody, unless the fund contract otherwise agrees on the policies, measures and dispute resolution mechanisms for ensuring the safety of the private fund assets. Based on the above principle, the Private Fund Measures stipulate mandatory custody requirements for private funds under certain specific circumstances, including where:

(1) private funds established in a contractual form;
(2) private funds accepting investment by any asset management products or other private funds;
(3) private funds mainly investing in a single target, offshore assets, or over-the-counter derivatives, etc.;
(4) private funds conducting leveraged financing;
(5) other circumstances stipulated by CSRC.

The Private Fund Measures distinguish the circumstances of private securities investment funds, private equity investment funds and fund of funds (FOF), and respectively stipulate the duties of private fund custodians. For private securities investment funds, the Private Fund Measures expressly stipulate that the *Securities Investment Funds Law* shall apply. The circumstance in the market where the custodian of private securities investment fund narrowed or excluded the custodian duties stipulated in the *Securities Investment Funds Law* in the fund contract, is expected to be corrected. For private equity investment funds and FOF, due to the current imperfect regulations and the regulatory orientations of different financial regulators and other reasons, the Private Fund Measures still only provide in principle that the custodian shall perform its duties in accordance with laws, administrative regulations, provisions of CSRC and the fund contract.

2. Investment Targets of Private Securities Investment Funds

Articles 27 to 29 of the Private Fund Measures specify the investment scope, investment targets, prohibited investment targets and prohibited transaction activities of the private funds, which are basically consistent with the existing rules.

Regarding the investment targets of private securities investment funds, in terms of derivative investments, the Registration and Filing Measures only list option contracts, swap contracts and forward contracts, while the Private Fund Measures, in consistent with the *Futures and Derivatives Law*, use the term "derivatives" for a more comprehensive and flexible approach. Moreover, it is noted that, compared with Article 31 of the Registration and Filing Measures, Article 28 of the Private Fund Measures removes "asset- backed securities" from the scope of investment targets of the private securities investment fund. We understand that this does not mean that private securities investment funds are not allowed to invest in asset-backed securities, but that they are included within the scope of the "other securities" listed in the article.

Furthermore, Article 29 of the Private Fund Measures stipulate that CSRC will guide AMAC to establish a black list for private fund investment. PFMs may continuously pay attention to the release and updates of such black list.

3. Eligibility Requirements of Qualified Investors of Private Funds

One of the significant changes in the Private Fund Measures is the revision of the criteria for qualified investors of private funds, improvement of the scope of exempted qualified investors, and setting of differentiated investment thresholds for various investors and products.

(1) Criteria for Qualified Investors

Article 40 of the Private Fund Measures revises the criteria for the qualified investors of private funds, including revisions to the requirements for the assets, income and investment experience of qualified investors to make them consistent with the criteria for qualified investors of asset management product of various financial institutions under the Guiding Opinions.

We have compared the current Interim Measures, Private Fund Measures, the Guiding Opinions and CSRC's PAM rules in respect of the assets and experience of the qualified investors as follows:

	Current Rules (Interim Measures)	Private Fund Measures	Guiding Opinions and CSRC's PAM Rules
Criteria for Individual Qualified Investors	Having financial assets with no less than RMB 3 million or the personal average annual income for the last three years with no less than RMB 500,000	Having over two years' investment experience and meeting one of the following conditions: having family financial assets with no less than RMB 5 million, or having family financial net assets with no less than RMB 3 million, or having personal average annual income for the last three years with no less than RMB 400,000.	Same as the Private Fund Measures
Criteria for Institutional Qualified Investors	Shall be an organization with net assets[4] of no less than RMB 10 million	Shall be a legal person or other organization with net assets[4] of no less than RMB 10 million	Shall be a legal person with net assets of no less than RMB 10 million at the end of the last year

[4] According to *Appendix 1-2 Reference Template for Basic Information Form of the Investor (Institution)* of the *Guidelines for Fundraising Agencies on Implementing the Suitability Management of Investors (for Trial Implementation)*, it shall be verified and ensured that assets of the institutional investors at the end of each of the last three months have exceeded RMB 10 million.

Scope of Financial Assets	Including bank deposits, stocks, bonds, fund units, asset management plans, bank wealth management products, trust plans, insurance products and futures, etc.	Bank deposits, stocks, futures, bonds, fund units, asset management products, etc.	Including bank deposits, stocks, bonds, fund units, asset management plans, bank wealth management products, trust plans, insurance products, futures and other derivatives, etc.

(2) Minimum Contribution Amount of a Single Investor

With respect to the investment thresholds for private fund investors, the Private Fund Measures do not adopt the lower investment threshold for private asset management products as stipulated in the Guiding Opinions and CSRC's PAM rules, but instead continue adopting a minimum investment amount of RMB 1 million for a single investor set forth in the Interim Measures in common cases, and make differentiated investment thresholds for a single investor under special circumstances, as follows:

	Circumstances	Minimum Contribution Amount of a Single Investor
Principle	Investment in single private securities investment fund and FOF	RMB 1 million
	Investment in single private equity investment fund	RMB 3 million
Special Circumstances	Investment in a fund with any of the following circumstances: (1) real estate private funds (2) private funds mainly investing in offshore assets and over-the-counter derivatives, etc. (3) private funds without custody arrangement (4) private equity funds distributed by distributors (5) other circumstances stipulated by CSRC	RMB 5 million

	Private funds that mainly (with at least 80% of its assets) invest in a single target	Individual investors: RMB 10 million Other types of investors: RMB 5 million
	Private funds established only upon the entrustment of a single investors * Such single investor shall be limited to regulated financial institutions, social security funds, basic pension funds, annuity funds and other pension funds, charity funds and other social welfare funds, qualified foreign investors, government capital or funds established with eligible government capital.	RMB 100 million

It is noteworthy that "minimum investment amount" requirement is set out in the current relevant rules in private fund sector, the Guiding Opinions and CSRC's PAM rules. It means the initial investment and the ongoing holding amount shall meet such minimum investment amount requirement. If the partial redemption results in the investor's holding amount being lower than the minimum investment amount, full amount of redemption is required. However, the Private Fund Measures use the term of "contribution amount". For investors who have already met the requirement of minimum contribution amount, it remains to be further clarified whether full amount of redemption is required if the amount held are lower than the minimum contribution amount due to partial redemption.

(3) Scope of Exempted Qualified Investors

Investors who are directly deemed as qualified investors based on their identities without verifying their assets and investment experience are usually referred to as "exempted qualified investors" in the industry. Such exempted qualified investors are not required to meet the aforesaid requirements on investment experience, assets and minimum contribution amount for qualified investors. Article 42 of the Private Fund Measures integrates and adjusts the current scope of exempted qualified investors as follows:

<table>
<tr><th>Current Rules</th><th>Private Fund Measures</th></tr>
<tr><td>Interim Measures
Article 13 The following investors are deemed as qualified investors:
(I) Pension funds such as social security funds and enterprise annuities, and social welfare funds such as charity funds;
(II) Investment schemes legally established and filed with AMAC;
(III) <u>PFMs</u> and their <u>fund</u> <u>practitioners that invest in the private funds managed by such PFMs</u>;
(IV) Other investors specified by the CSRC.

Certain Provisions on Strengthening the Regulation of Private Investment Funds
Article 7 …… asset management products legally launched by institutions regulated by the financial regulatory department of the State Council, QFIIs, RQFIIs shall be deemed as qualified investors provided by Article 13 of the Interim Measures …</td><td>Added:
• Institutions legally established and under regulation by the financial regulatory authority of the State Council, including securities companies and their subsidiaries, fund management companies and their subsidiaries, futures companies and their subsidiaries, commercial banks and their wealth management subsidiaries, insurance companies, insurance asset management companies, financial asset investment companies, trust companies, finance companies and other institutions specified by the CSRC (hereinafter referred to as the “Regulated Financial Institutions”)
• PFMs registered with AMAC
• Government capital or funds established with eligible government capital

Deleted:
• PFMs and their fund practitioners that invest in the private funds managed by such PFMs

Remaining the same:
• Asset management products legally launched by the Regulated Financial Institutions
• Pension funds such as social security funds and enterprise annuities, and social welfare funds such as charity funds
• QFIs</td></tr>
</table>

It is noteworthy that:

(a) Regardless of that the Private Fund Measures no longer deem the fund practitioners of PFM as exempted qualified investors, according to Paragraph 3 of Article 40 of the Private Fund Measures, it is not required to verify the assets and income, risk identification and tolerance capability, investment experience, or to be subject to the minimum contribution amount. Therefore, the Private Fund Measures do not change the exemption of the fund practitioners from the verification for qualified investors who invest in the private funds managed by the PFM in which they work.

(b) The Private Fund Measures list the PFMs as exempted qualified investors, which means that a PFM is not only exempted from the verification for qualified investors when investing in a private fund managed by itself, but is also treated as exempted qualified investor when investing in a private fund managed by another PFM with its proprietary funds, the same as the Regulated Financial Institutions.

(c) Following the existing rules, the Private Fund Measures do not calculate the number of investors on a look-through basis. In principle, the Private Fund Measures do not require to verify the investors on a look-through basis, but for product investors (including asset management products and private funds) and PFMs, the Private Fund Measures still require to identify the underlying actual investors and the ultimate source of their capital on a look-through basis. We view that such look-through requirement does not mean that all the underlying investors of the product investors shall meet the criteria of qualified investors, but are for purposes of effectively verifying the actual investors and their source of capital. This provision also echos the requirement about identifying and reporting the information of the beneficial owners of investors as set out in the Private Fund Regulation and the Registration and Filing Measures.

4. Product Design of Private Funds

(1) Special requirements on FOF

The Private Fund Measures introduce the "fund of funds" from the regulation level, which is defined as a private fund that invests main fund assets into the units of private equity investment funds, private securities investment funds, asset management products and other investment targets meeting the regulations of the CSRC. AMAC implements differentiated self-disciplinary management against FOF as a category of funds.

(a) Multilayered nesting: in line with Article 25 of the Private Fund Regulation, the Private Fund Measures specify that FOF is not considered as an investment layer, i.e., an asset management product or private fund invested by a FOF may further invest in other asset management products or private funds.

(b) Auditing: according to Article 63 of the Private Fund Measures, FOF shall prepare the audited annual financial reports.

(c) Fundraising size: according to Article 34 of the Private Fund Measures, the paid-in amount of a FOF shall be no less than RMB 50 million.

(d) Disclosure of underlying assets: according to Article 60 of the Private Fund Measures, the FOF manager shall disclose the ultimate underlying assets to its investors on a look-through basis.

(2) Private fund entrusted by a single investor

For the first time in the industry, Article 37 of the Private Fund Measures provides the regulatory requirements under special circumstances where a private fund is established only upon the entrustment of a single investor. In a flexible manner, such private funds may make special agreements in respect of the investment decision-making mechanism, fund custody, information disclosure and auditing, which are exempted from complying with relevant mandatory provisions, and may be agreed in the fund contract after reaching consensus by the PFMs and investors.

However, such single investors shall be limited to the Regulated Financial Institutions, pension funds, charity funds, QFIs, government capital or funds established with eligible government capital, and the minimum investment amount during the initial offering period shall reach RMB 100 million.

After the introduction of the private fund entrusted by a single investor, the concepts of “single” and “collective” are brought into the private fund sector, which is essentially similar to private asset management schemes of securities and futures business institutions. It is still pending further clarification that (i) whether a private fund can be successfully filed with AMAC as a regular fund if it has only one investor (and the investor is an external investor) at the fund launch, even if the fund contract contains subscription and redemption arrangements and specifies continuous distribution plan, and the fund will be open for other investors after the fund launch; (ii) whether it is a must to have two or more investors for a regular private fund at the time of fund filing with AMAC; and (iii) if two or more investors are required for a regular fund, whether existing private funds are required to rectify accordingly.

(3) Private fund investing in a single target

The Private Fund Measures provide that if a private fund invests at least 80% of its fund assets are invested in a single target (single assets and the non-standardized assets of the affiliates shall be deemed as the same assets and calculated in aggregate), such private fund:

(a) shall be under the custody of a fund custodian;

(b) shall clearly stipulate the contents concerning the single target in the fund contract;

(c) shall have a contribution amount of no less than RMB 20 million, and the contribution amount by a single individual investor (if any) shall be no less than RMB 10 million, and the contribution amount by a single non-individual investor shall be no less than RMB 5 million;

(d) shall not raise capital from investors other than existing investors where the private fund is a private equity investment fund making a single project investment;

(e) shall invest in the single target which is not affiliated with the PFM's shareholders, actual controller, partners or fund practitioner, unless unanimously agreed by all investors;

(f) shall conduct the special risk disclosure to all investors which shall be confirmed by all investors, and the PFM shall make written records of the decision-making process and risk disclosures.

(4) Size of the private fund

The Private Fund Measures, on one hand keep consistent with Article 33 of the Registration and Filing Measures, on the other hand further specify the initial fundraising size for various types of private funds:

Types	Initial Fundraising Size
Private securities investment fund	RMB 10 million
Private equity investment fund	RMB 10 million
Venture capital fund	The initial capital contribution shall be no less than RMB 5 million, and the fund size shall reach RMB 10 million in six months after the filing of the fund
Real estate private fund	RMB 30 million
Fund of funds	RMB 50 million
Private fund entrusted by single investor	RMB 100 million
Private fund mainly (at least 80% of its assets) investing in a single investment target	RMB 20 million

5. Fundraising

(1) Clarifying that PFM may engage in direct sale or appoint distributors

After the promulgation of the Private Fund Regulation, Article 17 thereof ("A PFM shall raise funds on its own, and **shall not engage others to raise funds on its behalf**, unless otherwise stipulated by the securities regulatory authority of the State Council") has caused a great response in the industry, and it is urgently needed for CSRC to clarify whether a PFM may appoint distributors. As clarified in the Private Fund Measures, "A PFM shall raise funds by itself or engage a private fund distributor which has obtained the qualification for fund distribution and meets the requirements of the AMAC rules to raise funds". On one hand, it explicitly stipulates that private funds may continue the pattern of adopting direct sale and distribution by distributors at the same time; on the other hand, it emphasizes that a distributor shall "obtain the qualification for fund distribution and meet the requirements of the AMAC rules to raise funds" to distribute private funds.

(2) Clarifying the definition of "fundraising"

Article 43 of the Private Fund Measures clarifies the definition of "fundraising", and include "opening private fund transaction accounts for investors" and "providing access to information of private fund transaction accounts" into the scope of fundraising activities of private funds, which is consistent with the definition of fund distribution in the *Measures for the Supervision and Administration of Publicly Offered Securities Investment Fund Distributors*.

Given that such activities fall into the scope of fundraising activities, PFMs shall note that activities such as accounts opening and inquiry of transaction account information shall be conducted by the employees with fund practitioner qualification.

(3) PFM shall not engage an affiliated distributor

Current provisions require that the risk disclosure shall be made to the fund investors if a PFM engages an affiliate to distribute the private fund. However, Paragraph 2 of Article 44 of the Private Fund Measures imposes a stricter requirement that a PFM shall not engage a distributor affiliated with the PFM or any shareholder, partner, actual controller or fund practitioner of the PFM.

If such requirement takes into effect, the PFM shall not engage a distributor in the same group, and shall check whether any of its employees is associated with any fund distributor, if any, the PFM shall not engage such distributor.

(4) Enhancing the protection in raising funds from individual investors

With respect to raising funds from individual investors, Article 49 of the Private Fund Measures provides a higher standard compared with the current rules, requiring audio or video recordings, implementation of the investment cooling-off period, revisit for confirmation and record-keeping for off-site fundraising from individual investors. Comparing the current rules with Article 49 of the Private Fund Measures:

Firstly, under the current investor suitability rules, a PFM and its distributors are only required to take audio or video recordings in certain stages during the distribution to ordinary investors, while audio or video recording is not mandatorily required for professional investors. However, Article 49 requires audio or video recordings for the entire process of the fundraising from individual investors, regardless of whether they are categorized as ordinary investors or professional investors.

Secondly, the current *Administrative Measures for the Fundraising of Private Investment Funds* exempt the cooling-off period and revisit for confirmation in the case of investment by fund practitioners of the PFM. However, Article 49 requires a PFM and its distributor to apply the cooling-off period and revisit for confirmation to all the individual investors, including the fund practitioners of the PFM.

(5) Specifying the timing of the subscription money transfer

Article 32 of the Private Fund Measures provides that PFMs and distributors shall not collect investment money from investors before the execution of the fund contract. In practice, there are cases that the investors are required to transfer subscription money while the fund manager or the fund custodian has not signed the fund contract. In accordance with this article, strictly speaking, investors shall make payments only after all parties have signed the fund contract.

(6) The fees incurred during the fundraising shall not be paid out of the fund assets

Article 50 of the Private Fund Measures expressly provides that private fund assets may not be used to pay the expenses during the fundraising process. In practice, it is agreed in some private fund contracts that fees incurred during the fundraising process, such as the document preparation fees and legal fees paid for the establishment of the fund, and service fees charged by fundraising supervision institutions, etc., shall be paid from fund assets after the establishment of the fund. According to this article, such arrangement is no longer allowed.

6. Fund Operation

(1) Connected-party transactions

As explicitly provided in Article 53 of the Private Fund Measures, the identification standards of the connected-party transactions shall comply with the provisions of the *Accounting Standards for Business Enterprises* in addition to the Private Fund Regulation. Therefore, PFMs shall also refer to the provisions of the *Accounting Standards for Business Enterprises No.36 – Disclosure of Connected Parties* in judging how to identify connected parties and connected-party transactions. Existing PFMs shall also review their internal control policies and fund contracts and make appropriate amendments.

(2) Specify the time limit for commencement of fund liquidation

Article 57 of the Private Fund Measures specifies that a PFM shall commence the fund liquidation within five working days as of the occurrence of any circumstance for termination of the fund, unless otherwise agreed in the fund contract. Therefore, if a PFM needs a longer period to commence the fund liquidation, it shall explicitly stipulate such period in the fund contract, otherwise the timeline of five working days as provided in the Private Fund Measures will prevail.

(3) Improving the market-oriented exit mechanism

Article 58 of the Registration and Filing Measures provides for a market-oriented exit mechanism triggered under the circumstance "where a PFM is unable to perform or neglects to perform its duties due to loss of contact, deregistration of PFM, or occurrence of significant risks, resulting in the failure to exit normally". Article 58 of the Private Fund Measures uses more general and comprehensive expressions to specify that the market-oriented exit mechanism shall apply "where a private fund cannot be terminated normally".

7. Fund Auditing

The Registration and Filing Measures stipulate that annual audit shall be conducted for the private equity investment funds, and the annual financial report of a fund shall be audited by an accounting firm filed with CSRC where the AUM of the fund exceeds a certain amount or the number of investors exceeds a certain number. According to the *Guidelines for the Operation of Private Securities Investment Funds (Consultation Paper)* promulgated by AMAC on 28 April 2023, the annual financial report of a private securities investment fund with year-end net assets of more than RMB 100 million shall be audited, and the annual financial report of a private securities investment fund with year-end net assets of more than RMB 1 billion shall be audited by an accounting firm filed with CSRC. Besides, it is provided in the Private Fund Regulation that “PFMs shall, as required, engage accounting firms to audit the fund assets of private funds, provide investors with the audit results, and report to the registration and filing organization”.

There are many discussions on the necessity of annual audit of private securities investment funds in the industry, and it is generally believed that the audit burden is too heavy and the relevant rules by the CSRC are urgently needed. According to the Private Fund Measures, PFMs shall report the annual financial reports of the private funds, and the annual financial reports of PFMs, private equity investment funds, FOFs, and private securities investment funds without custodian shall be audited by accounting firms. If such provision of the Private Fund Measures takes effect, it will be advantageous for private securities investment funds.

VII. Improving the Requirements of Information Disclosure and Reporting

The Private Fund Measures restate that PFM shall establish and improve the information disclosure and reporting system at the level of departmental rules, and enhance the requirements on information disclosure and reporting in terms of the scope and time limit of the ad-hoc material matters, including:

1. In the event of any material change in a PFM, liquidation of private funds, material litigation or arbitration of a private fund, or a material risk event or any other material matters that may affect the interests of investors as agreed upon in the fund contract, the PFM shall disclose the relevant information to the investors within two working days.

2. Where any material risk event occurs to a PFM or any of its controlling shareholder, actual controller or a private fund under its management, the PFM or the fund custodian shall report to the local branch of the CSRC and the AMAC at the place where the PFM is domiciled and the place where the risk event occurs within two working days.

VIII. Application of QDLP Managers and QDLP Funds

QDLP (Qualified Domestic Limited Partners) has been piloted in the regions such as Shanghai, Shenzhen[5], Beijing, Hainan, Qingdao, Tianjin, Chongqing, Jiangsu, Guangdong and Ningbo, with a considerable number of institutions actively engaged in QDLP business, launching and managing QDLP funds investing in overseas markets. A common business model for QDLP is that a foreign asset

[5] Such regime is called QDIE (Qualified Domestic Investment Enterprise) in Shenzhen.

manager establishes a PFM in a pilot area, registers the PFM as an "Other Type" PFM with AMAC, and invests, through the investment quota approved by the State Administration of Foreign Exchange ("**SAFE**"), in an offshore flagship fund launched and managed by its foreign parent company or any of its affiliates. The types of offshore funds include mutual funds and private funds, and the investment field covers primary PE/VC markets, secondary securities and futures markets, as well as other alternative investment products. The structure of a QDLP fund is usually a master-feeder fund, the main fund assets of which are invested in a single offshore master fund.

As QDLP funds are privately raised from onshore qualified investors, the QDLP managers are registered as private fund managers with AMAC in accordance with the private fund related rules, and its initial registration and ongoing compliance shall comply with private fund related rules and regulatory requirements. Meanwhile, QDLP funds shall be filed with AMAC, and its initial filing and ongoing investment operation shall also comply with the rules and regulatory requirements in the private fund sector. As Article 61 of the Private Fund Regulation includes legislative authorization ("the administrative measures governing foreign-invested PFMs shall be jointly formulated by the securities regulatory authority of the State Council and other relevant departments of the State Council in accordance with foreign investment related laws and administrative regulations, as well as this regulation"), the industry generally expects that CSRC and SAFE will jointly promulgate special regulations governing QFLP[6] and QDLP as soon as possible and that AMAC will promulgate special guidelines applicable to QFLP and QDLP business, which will apply to QFLP and QDLP business in accordance with the principle of special laws prevailing over the general laws.

If the *Private Fund Measures* are officially released but at that time special regulations and guidelines applicable to QFLP and QDLP are not issued, QDLP will be confronted with the challenges of stricter requirements of the *Private Fund Measures* considering the stringent rectification requirements. For example:

1. In some cases, the controlling shareholder of a QDLP manager is a holding company (Holdco) rather than a licensed financial institution, and the controlling shareholder may not have relevant experience in investment and asset management despite the fact that the group has rich experience in investment and asset management.

2. As most QDLP funds are master-feeder funds without active management, most QDLP managers have not equipped with senior management personnel in charge of investment management and it is difficult to appoint such a personnel who meets the requirements of working

[6] QFLP (Qualified Foreign Limited Partner) refers to a mechanism that foreign investors, after obtaining relevant pilot qualification, convert the offshore capital into RMB to invest in domestic PE in accordance with the foreign exchange regulatory procedures applicable to QFLP. QFLP fund management enterprises refer to the enterprises established by foreign investors with the establishment and management of QFLP funds as their main business.

experience, management experience and having track record specified in the Registration and Filing Measures and the implementation guidelines.

3. Most QDLP funds adopt master-feeder structure, and if it is deemed as private funds investing in a single investment target, it will contradict with the Private Fund Measures as the offshore funds invested by the QDLP funds are launched and managed by the affiliates of QDLP managers, while the Private Fund Measures require that the single investment target shall not be affiliated with the PFM and its shareholders, actual controller, partners and fund practitioners.

4. The AUM of some QDLP funds in the market may be less than RMB 20 million. The contribution amount by a single individual investor may be less than RMB 10 million, and the contribution amount by a single non-individual investor may be less than RMB 5 million.

5. Some QDLP funds may have only one investor (such as a trust plan), it is not sure whether the requirement on the “private fund entrusted by a single investor” will apply. Although such QDLP fund only has one investor, such investor may not fall within the scope of eligible single investor under the *Private Fund Measures* and the AUM of the fund may not reach RMB 100 million.

If all existing QDLP managers and QDLP funds are required to be rectified in accordance with the Private Fund Measures, the QDLP managers shall complete rectification within one year, and no new investment is allowed for the QDLP funds before the rectification. It may be a terrible blow to QDLP business. QDLP managers are eager to see the clarifications by the regulators with respect to the application of the Private Fund Measures to QDLP managers and QDLP funds, and the progress of subsequent special legislation for QDLP sector.

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