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Brief Analysis of the Provisions on Issues concerning the Implementation of the "Measures for the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors" by CSRC

By Sandra Lu and Elva Yu

China Securities Regulatory Commission (hereinafter referred to as "CSRC") promulgated *the Provisions on Issues concerning the Implementation of the "Measures for the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors"* (hereinafter referred to as "**New QFII Provisions**") on 27 July 2012, which modified *the Circular on Issues Relevant to the Implementation of the "Measures for the Administration of Securities Investments in China by Qualified Foreign Institutional Investors"* (hereinafter referred to as "**QFII Circular**") promulgated in 2006 by CSRC. The New QFII Provisions will take effect as of the date of promulgation. The following brief analysis will give the several important modifications in the New QFII Provisions against the QFII Circular.

Significantly lowering the requirements of QFII applicants

The requirements of QFII applicants are lowered significantly in the New QFII Provisions. The requirement for asset under management of QFII applicants such as foreign assets management institutions, insurance companies and other institutional investors including pension fund and charitable foundation etc in the most recent year is reduced from US$5 billion to US$500 million and the years of establishment of such applicants are reduced from 5 years to 2 years accordingly. The requirement for asset under management of QFII applicants such as foreign securities companies and commercial banks in the most recent year is reduced from US$10 billion to US$5 billion.

According to relevant news release on the CSRC website[1], foreign private equity investment institutions can also apply for QFII qualification in the capacity of assets management institutions. Based on the abovementioned changes, we believe that there will be more qualified foreign investors applying for QFII status in the future.

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Simplifying the QFII application documents

According to the New QFII Provisions, QFIIs are no longer required to submit their articles of association (photocopy) to CSRC when applying for QFII qualification. In addition, the previous requirement of submitting the “draft of custody agreement to be executed between the QFII and its custodian” is now modified into the “power of attorney for its custodian”, and that of submitting the “audited financial statements for the most recent three years” modified into the “audited financial statements for the most recent year”.

Furthermore, the previous requirement in the QFII Circular that a QFII shall submit the formal custodian agreement to CSRC within five working days after the opening of its special Renminbi accounts is also deleted in the New QFII Provisions, which means QFIIs no longer need to submit the custody agreement (regardless of a draft or a formally signed document) to CSRC.

Account opening rules

In the New QFII Provisions, the wording “one-to-one” in Article 6 of the QFII Circular (i.e. “A QFII shall appoint its custodian to apply to the China Securities Depository and Clearing Corporation Limited to open several securities accounts, application for which shall correspond one-to-one with the special Renminbi account approved by SAFE.”) is deleted, which means a QFII may open several securities accounts with respect to one special Renminbi account, solving the problem that a QFII can only open one securities account opened each of the Shanghai securities market and Shenzhen securities market to correspond with the only one cash account.

In addition, compared with the previous consultation draft, there are no substantial breakthroughs in relation to the name of the securities accounts of QFIIs in the formally promulgated New QFII Provisions. With regard to the clients’ assets, it is still distinguished into two categories, i.e. general clients’ assets and long-term funds such as public funds and insurance capital, etc., and the accounts of which will be respectively opened in the name of “QFII + the client’s name” and “QFII + Fund (or insurance capital, etc.)”. In terms of the ownership issue of securities accounts opened in the name of “QFII + the client’s name”, it is still not clarified in the New QFII Provisions.

Clarifying that fund management companies are allowed to manage QFII assets by means of special accounts

It is clarified in Article 7 of the New QFII Provisions that QFIIs may appoint domestic fund management companies to provide assets management services of specific clients (hereinafter referred to as “Special Accounts“), and it is also clarified that the investment scope shall be in compliance with relevant provisions of QFII.

However, there are still many inconsistencies in the operational level between the relevant provisions of QFII and provisions of Special Accounts services provided by fund management companies, and it is yet to be clarified by the regulatory authorities how to apply the provisions when there are inconsistencies between provisions of QFII and provisions of Special Accounts. For example, according to the provisions of Special Accounts, the name of the securities accounts opened by the fund management companies for such Special Account in the event of one single client shall be in the name of “the name of fund management company + the name of the custodian bank + the client’s name”, which is definitely different from the rules of opening securities accounts of QFII, and how to solve such problems is yet to be made clear in practice.

Expanding the investment scopes of QFIIs and relaxing the limits on shareholding ratio

According to Articles 8 and 9 of the New QFII Provisions, not only has the stock index future been included in the Renminbi-denominated financial instruments which QFII may invest in, but also the fixed income instruments traded in the inter-bank bond market is allowed to be invested by QFIIs, which is further expanding the investment scopes of QFIIs. Meanwhile, the limits on shareholding ratio by foreign investors have been relaxed in the New QFII Provisions. The limit on shareholding ratio by all foreign investors is increased from 20% (as provided in the QFII Circular) to 30%, and the limit on the shareholding ratio by single foreign investor is unchanged.

1 http://www.csrc.gov.cn/pub/newsite/bgt/xwdd/201207/t20120727_213209.htm

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