

MESSAGE

To: consult/SFC@SFC CEOO Ext :
cc: "Regulatory Wma" <regulatory.wma@ipac.com.hk> Ext :
From: "Tina Lau" <tina.lau@ipac.com.hk>
Date: 30/12/2009 01:18 PM
Subject: Response to Consultation Paper on Proposals to Enhance Protection for the Investing Public - ipac HK

Hi there,

Please kindly see attached response to the Consultation Paper on Proposals to Enhance Protection for the Investing Public from our company.

Should you have any queries, please do not hesitate to contact me.

Regards,

Tina

Tina Lau | Compliance Specialist | ipac financial planning Hong Kong Limited | Licensed by the Securities & Futures Commission of Hong Kong. CE No: AAN641
Suite 5101 The Center 99 Queen's Road Central Hong Kong | ☎ 852 2285 2638 | ☎ 852 2285 2899 | ✉ tina.lau@ipac.com.hk

This email and any files transmitted with it are confidential and intended solely for the use of the individual or entity to whom they are addressed. If you have received this email in error please do not read, copy, distribute, disclose or use any information of this email in any way and please immediately notify the sender and delete this email. Thank you for your cooperation.



***** SFC Consultation Paper_Nov09_all questions_FINAL.doc

Submission deadline: 31 December 2009

Published date: 25 September 2009

Submitted by: ipac financial planning Hong Kong limited ("ipac HK")

Contact person:

Sharon Chan, Head of Compliance Tel: 2285 2656 Email: sharon.chan@ipac.com.hk OR

Tina Lau, Compliance Officer Tel: 2285 2638 Email: tina.lau@ipac.com.hk

SFC Consultation Paper on Proposals to Enhance Protection for the Investing Public

Part II Products

Q1 Do you have any comments on the Overarching Principles Section of the Handbook generally or any particular provisions in the Section? Please explain your views.

ipac HK: The overarching principles are fine but it is too generic and it is hard for industry players to understand the standard and requirements of SFC. We suggest SFC providing specific guidance on the requirements and standards.

Q2 What are your views on the proposed disclosure requirements in Appendix C (Information to be Disclosed in Offering Documents for Unlisted Structured Products) and Appendix D (Advertising Guidelines Applicable to unlisted Structured Products) to the SP Code?

ipac HK: We recommend the definition of Structured Products should be clearly defined. The advertising guidelines for Structured Products should be in line with the advertising guidelines of Unit Trust Code but with additional disclosure requirements.

On the other hand, currency and interest rate-linked products should fall within the SP code. Banks sell a number of dual-currency type deposits which are sold as safe deposit-type instruments where clients can choose to pair 2 currencies. Banks do not disclose how derivatives are embedded in these types of structures which carry more than a deposit-type risk. The disclosure in this area should be enhanced. Similar for range accrual-type interest-linked notes or deposits. They can sometimes be sold as conservative instruments. The payout mechanisms and risks will be better disclosed if these products fall under the SP code.

Aside from disclosure requirements, Investment advice is needed prior to selling structured products.

Risks should include not just the investment, currency, interest rate risks, etc. Credit risk of the counterparty and issuer of the structured note should also be clearly stated, i.e. what happens if the issuer defaults, where the recourse is, etc.

Q3 What are your views on the requirement for Issuers to provide ongoing disclosure of the types of information set out in 7.6 of the SP Code throughout the term of a structured product? Please explain the reasons for your views. Are there any other matters which you think an Issuer should be obliged to disclose to investors on an ongoing basis?

ipac HK: The requirement should be in line with the Unit Trust Code. The ongoing disclosure should be provided by the product issuers, rather than the distributors, so the information can be standardized.

Q4 What are your views on the eligibility requirements for Issuers and Guarantors of unlisted structured products proposed by the Commission?

ipac HK: No comment because ipac HK does not issue any structured products.

Q5

- a) What are your views on the proposed requirements applicable to SPV Issuers?
- b) What are your views on the current proposal to mandate the appointment of a Hong Kong-licensed Product Arranger for structured products issued by an SPV and make such Product Arranger responsible for ensuring an SPV Issuer's compliance with the SP Code throughout the term of the structured product?
- c) Do you think a Product Arranger should also be appointed for structured products issued by Issuers (whether SPVs or not) or guaranteed by Guarantors where these entities are not local Regulated Entities (ie. Where the Issuers/Guarantors are not licensed banks regulated by the HKMA or corporations licensed by the Commission pursuant to section 116 of the SFC)?
- d) Other than what has been proposed, what other obligations or requirements (if any, both before and after an offering), do you think a Product Arranger should be made subject to? Please give a list of any such additional obligations with reasons.

Please explain your views.

ipac HK: No comment because ipac HK does not issue any structured products.

Q6

- a) What are your views on the proposed eligibility criteria for collateral in respect of structured products?
- b) Do you think that collateral should be subject to any additional eligibility criteria? If so, what criteria?
- c) What are your views on the requirement that investors' claims to collateral proceeds should be accorded priority and should not be subordinated to claims by counterparties to transactions with the Issuer that are related to the structured product?

ipac HK: No comment because ipac HK does not issue any structured products.

Q7 Do you believe that the Commission should take into account any additional eligibility criteria for reference assets, or any other factors, when considering whether or not to accept a proposed reference asset class for a structured product? If so, please list such additional criteria / factors and give an explanation for each.

ipac HK: No comment because ipac HK does not issue any structured products.

Q8

- a) Should indicative valuations of structured products be required to be provided daily? Do you think there are additional or other measures which could help investors to assess the performance of their investments? If so, please provide details.

- b) With regard to the proposal to provide liquidity by way of making firm price quotations, do you think an exemption is justifiable for structured products with a short scheduled tenor, eg. of one month or less? How often do you think Issuers or their market agents should provide liquidity by way of making firm price quotations? Do you think that there are other circumstances or periods during the terms of certain structured products in which liquidity provision should not be required or could not reasonably be provided? If so, why?

ipac HK: No comment because ipac HK does not issue any structured products.

Q9 Please give your views on the use of annualised returns in offering documents and advertisements for structured products.

ipac HK: Annualised returns should be presented carefully and consistently. There are instances when a structured product has a big upfront fixed payout in the first year with the succeeding payouts dependent on the performance of the underlying asset. There should be clear delineation between an expected payout/return given a specific scenario vs. the actual/return. In the offer documents and promotional materials, investors should not be led to believe that a "potential" payout will lead to the actual payout/return.

Q10 Please provide your views on the length of the transition period for compliance with SP Code requirements for unlisted structured products where the issue of documents has been authorized prior to the date of the SP Code's effectiveness.

ipac HK: No comment because ipac HK does not issue any structured products.

Q11 In relation to proposals regarding investment activities set out in Proposal 1 (structured funds), Proposal 2 (funds that invest in FDI) and Proposal 3 (investments in other schemes), other than the proposed general requirements, what other requirements do you think should be included? Please explain your views.

ipac HK:

(Proposal 1) We recommend SFC clarifying whether the structured funds are under the definition of Structured Product. If yes, the structured funds should be regulated under the Structured Product Code, rather than Unit Trust Code.

(Proposal 2) No comment as ipac HK does not invest in FDI.

(Proposal 3) No comment.

Q12 In relation to the disclosure and reporting requirements set out in Proposal 4 (bilingual annual reports) and Proposal 5 (Product KFS), do you agree with the proposals? Please explain your views.

ipac HK:

(Proposal 4) The disclosure and reporting requirements should not be compulsorily published in both Chinese and English. As some offshore funds are hard to be translated into Chinese for every disclosures and reports, we suggest Chinese documents can be provided based on client's request.

(Proposal 5) agree with the standardized KFS format.

Q13 Do you have any comments on the revisions to the UT Code generally? Please explain your views.

ipac HK: Agree with the amendments. In relation to appointing multi-manager, we are happy to see the flexibility of the approval requirement, but we also want to seek clarification from the SFC in relation to the requirement of Due Diligence for selecting the manager and the requirements or standards for disclosing the Due Diligence process in the offering document.

We would also like to mention that one of the difficulties with enhancing our product is the regulatory pre-approvals, especially with new managers. For instance, our SIS Asia Pac ex-Japan Equity Fund's appointed securities manager is UBS UK. However, UBS UK in turn delegates the investment management functions to its sister company, UBS SG. We need to obtain the approval for not only UBS UK as the main contracting entity but also UBS SG as the delegate of UBS SG.

However, refer to item 179 from page 50 of the Consultation Paper, the flexibility provided for in the consultation paper does not seem wide enough to allow for various redemption situations. We suggest the delay and suspension of redemption should also cover the following situations:

- ~ when any of the principal markets or stock exchanges on which any significant portion of the Investments of the relevant Sub-Fund from time to time are quoted, listed, traded or dealt in is closed (otherwise than for customary weekend or ordinary holidays) or during which dealings therein are restricted or suspended or trading on any relevant futures exchange or market is restricted or suspended;
- ~ when, as a result of political, economic, military or monetary events or any other circumstances outside the control, responsibility and power of the Manager, any disposal or valuation of Investments of the relevant Sub-Fund is not reasonably practicable without this being seriously detrimental to the interests of owners of Units in general or the owners of Units of the relevant Sub-Fund or if, in the opinion of the Manager, the Redemption Price cannot fairly be calculated or any such disposal would be materially prejudicial to the owners of Units in general or the owners of Units of the relevant Sub-Fund;
- ~ during any period when any breakdown occurs in the means of communication normally employed in determining the price of any of the Investments of the Sub-Fund or when for any other reason the value of any of the Investments or other assets of the relevant Sub-Fund cannot reasonably or fairly be ascertained; or
- ~ during any period when the Sub-Fund is unable to repatriate funds required for the purpose of making payments on redemption or when such payments cannot, in the opinion of the Manager, be effected at normal prices or normal rates of exchange or during which any transfer of funds involved in the realisation or acquisition of Investments cannot, in the opinion of the Manager, be effected at normal prices or normal rates of exchange.

Q14 What are your views about the idea of UCITS schemes which have issued KIDs under their own E.U. regulators' regime using KIDs in place of the Product KFS? The issue here is how we should balance the importance of developing broadly standardized Product KFS across all products sold to the Hong Kong public so that it is easy for Hong Kong investors to understand and compare different products, and the commercial needs of individual fund houses to reduce costs and lessen administrative burdens. Also, if a large number of SFC-authorized funds adopt KIDs instead of Product KFS, it may defeat the purpose of comparability under the Product KFS proposal. The SFC would like to hear your views.

ipac HK: We agree that if KIDs or similar KFS' are available (which provide the general information required by the SFC) that these be used instead of a SFC-imposed KFS.

Q15 Do you agree that the proposed approach to implementation of the revised UT Code is acceptable and practicable, taking into account the needs and circumstances of various stakeholders? Do you have any particular views as to exactly how long the transition period should be for Existing Schemes to fully comply with the Product KFS and Other Disclosure Requirements (paragraph 191)?

ipac HK: At least 1 year to be given to the industry player to prepare.

Q16 Do you have any comments on (1) the Product KFS requirements, (2) the enhanced disclosure requirements on "with-profit" features and internal funds, (3) the deletion of Chapter 5, 8 and 9 of the current ILAS Code, and (4) the codification of the existing practices regarding the computation of surrender values and the notification requirements on scheme changes?

ipac HK: Agree with the KFS requirements. Agree with the proposal.

Q17 Do you agree that the proposed approach to implementation of the revised ILAS Code as acceptable and practicable, taking into account the needs and circumstances of various stakeholders? Do you have any particular views as to exactly how long the transition period should be for Existing Schemes to fully comply with the Product KFS and Other Disclosure Requirements (paragraph 214(c))?

ipac HK: No comment as ipac does not issue ILAS products.

Part III Intermediaries conduct

Q18 Do you agree that some of the proposals in this part of the consultation paper should only apply to unlisted investment products? Please explain your views.

ipac HK: We suggest that the standard and proposed rules should be applied to all financial and investment products.

We think the regulations to disclose the product information to the public and investors in relation to different investment products should be the consistent, otherwise the investors are hard to judge and compare among different investment products.

Q19 Do you think that intermediaries should, as part of their "know your client" procedures, seek clients' information about their knowledge of derivatives and characterize those clients (other those professional investor) with such knowledge as "client with derivative knowledge" to assist intermediaries in ensuring that the investment advice and products offered in relation to unlisted derivative products are suitable?

Please give your views on the contents of the proposed measures for intermediaries to access whether investors have knowledge of derivatives.

ipac HK: We agree that intermediaries should, under the assumption that unit trusts are not categorized as "derivatives products", as part of their "know your client" procedures, seek clients' information about their knowledge of derivatives and characterize those clients (other those professional investor) with such knowledge as "client with derivative knowledge" to assist intermediaries in ensuring that the investment advice and products offered in relation to unlisted derivative products are suitable.

It is suggested to define the definition of "derivatives products" as most products in the market have underlying funds invested in derivatives. If these products are also categorized as "derivatives products", there would be no meaning for the categorization or definition, as the majority of the funds in the market would be "derivatives products". It would also scare the general investors if they are told that they are investing in derivatives when they are choosing an unit trust in their portfolio. The definition should only include the futures, options and those complicated structure derivatives, and should exclude the unit trusts and mutual funds which have underlying funds in derivatives. Note that the unit trusts and mutual funds are already diversified. Another suggestion is to define a percentage of the derivatives contained in a product to determine if it is a "derivatives product".

From the contents of the proposed measures, it says "if the product is assessed to be not suitable for the client, the intermediary should exercise caution in serving the client", it is recommended to explain in detail with implementation samples what it means by "exercising caution in serving the client".

We do not think the criteria of "undergoing training or attending courses on derivatives products" is appropriate to be an element to determine whether a client has the knowledge in derivatives; a financial course cannot represent whether a person really understands the risk of an investment product in real life. We recommend to remove this criteria.

We also recommend that no matter a client has the derivatives experience/knowledge or not, providing investment advice to clients should be compulsory unless the client chooses to opt out his right.

We seek the clarification from the SFC in relation to the categorization and definition of derivatives products.

Q20 Should a high net worth investor be considered to have specific knowledge and expertise if:

- a) He is currently working, or has previously worked in the relevant financial sector for at least one year in a professional position that involves the relevant product; or
- b) He has undergone training or studied courses which are related to the relevant product?

Do you have any other suggestions?

ipac HK: We agree that the work experience in the relevant financial sector to be considered as specific knowledge and expertise towards the relevant product.

However, some products in the market are too complex; the knowledge of these complex products may not be something that can be learned from the books or from a course entirely. Moreover, new products with complex features are coming out everyday; a training course may not be able to catch up the new products in the market. Having said that, worldwide professional qualification such as CFP, should be accounted as specific knowledge and expertise towards the relevant product.

Q21 What amount should the minimum portfolio requirement be set at? Please give your reasons.

ipac HK: A portfolio requirement is not relevant when talking about the sophistication level of an investor.

It is more appropriate to name this type of investors as "Frequent Investor" instead of "Professional Investor". Professional Investor gives out a wrong impression as though this type of investors is sophisticated than the average public in investing.

Referring to the Lehman Brothers' incident, most of the people who are protesting and complaining about the products and misleading recommendations are categorized as the Professional Investors simply because of their high net worth asset. We recommend to remove the asset value as a consideration to determine whether a client is a Professional Investor. Sufficient investment experience and knowledge should be more appropriate in the consideration instead.

Having said that, a lot of financial institutions in the market are targeting the Professional Investors as their clients, a much higher minimum portfolio requirement, say HK\$20 million, would definitely eliminate a good number of investors to be abused from the definition of Professional Investor by the financial institutions.

Q22 Where a distributor and/or any of its associates explicitly receives or will receive monetary benefits from a product issuer (directly or indirectly), which of the following three disclosure options would be more appropriate? Please explain your views.

Option 1.1 – Disclosure of dollar amount or percentage

Option 1.2 – Disclosure of percentage bands or ceiling (i.e. "x% to y%" or "up to y%")

Option 1.3 – Generic disclosure

ipac HK: ipac HK has been implementing Option 1.1. We list out all the fees that we receive from a product issuer, both directly and indirectly, to our clients in a written financial plan with specific dollar amount or percentage.

We recommend the fee disclosure to be applicable to the investment-linked (ILAS) products as well so that it is more fair within the industry and consistent enough for the investors to compare among different products.

Q23 Do you have any suggestions as to how the percentage bands referred to in Q22 should be set (e.g. up to 1%, over 1% to 2%, etc)?

ipac HK: We suggest the percentage band to be as specific as possible, for example "x% to y%".

Q24 Where a distributor does not explicitly receive any benefits for distributing an investment product, which of the following disclosure options would be more appropriate? Please explain your views.

Option 2.1 – Specific disclosure of distribution reward

Option 2.2 – Generic disclosure

ipac HK: We agree on the specific disclosure approach where we are able to ascertain the external distribution reward.

However, if we are not able to ascertain the external distribution reward, a specific disclosure will definitely entail higher compliance costs and the internal allocation and budgeting is likely to be subjective. It would also be difficult for investors to compare products and distribution channels on a like-with-like basis.

Therefore, we would prefer a generic disclosure if we are not able to ascertain the external distribution reward.

Q25 Where a distributor makes a trading profit from a back-to-back transaction, which of the following disclosure options would be more appropriate? Please explain your views.

Option 3.1 – Disclosure of specific trading profit

Option 3.2 – Generic disclosure

ipac HK: We agree on the specific trading profit to be disclosed in a back-to-back transaction.

We have to agree that many risk or cost factors such as counterparty credit risk, financing cost etc. may not be reflected from a trading profit from a back-to-back transaction, which means a mere disclosure may overstate the actual profit made by the intermediary. However, the best estimate of exact profit should still be disclosed to the clients.

We also agree on the view that distributors should disclose trading profits only where the transaction results directly from recommendations or solicitations made to clients as this would give rise to potential or perceived conflict of interest.

Q26 Do you consider it appropriate to restrict distributors from offering investors supermarket gift coupons, audio visual equipment and other kinds of gifts having monetary value (except discount of fess and charges) in promoting a specific investment product to investors?

ipac HK: We agree to restrict distributors from offering investors supermarket gift coupons, audio visual equipment and other kinds of gifts having monetary value (except discount of fess and charges) in promoting a specific investment product to investors because it would distract the investors, particularly the unsophisticated investors, as well as the intermediaries from paying sufficient attention to the features of the investment products.

Q27 Do you have any comments on the proposed information content of the Sales Disclosure Document which includes (a) capacity (principal or agent); (b) affiliation with product issuer; (c) monetary and non-monetary benefits; and (d) discount of fees and charges available to investors?

ipac HK: We agree that a Sales Disclosure Document with the listed information would be beneficial to the investors. We also strongly recommend that advisers should provide a written investment advice (financial plan) to the clients unless a client chooses to opt out his right.

We urge to have flexibility on how to implement the suggestion. Since we offer our clients a written financial plan, which includes comprehensive information from KYC to the rationale of the recommendations, it would be great if we could include the Sales Disclosure Document information in the financial plan as well, so that we can avoid too many paperwork to the clients.

We suggest to include a highlighted box/window which clearly states the product types, the risk rating and the warning statements on the front page of the Sales Disclosure Document. Moreover, the KFS should be attached in the Sales Disclosure Document when investment recommendation is provided.

Recommendations with appropriate analysis and reasons should also be clearly recorded in the Sales Disclosures Document.

Q28 Do you think audio recording of the client risk profiling process and the advisory or selling process for investment products should be made mandatory or the current record keeping requirements are sufficient? If audio recording is made mandatory, how long do you think these audio records should be kept for? Please explain your views.

ipac HK: We do not think that audio recording is the best suggestion to protect the investors. ipac HK has been implementing a process to document the product recommendations and their rationale in a written financial plan for each client. The client reads through, agrees and signs off the financial plan before the actual investment implementation is processed. We trust that this is sufficient enough to protect our clients.

Currently, banks are implementing the audio recording system for the risk disclosure and the advice process. However, this practice is more like an exercise that they have to comply without its true value. Bank staff go through the whole sales process with the client before they repeat the risk disclosure and the advice part just for the sake of the audio recording purpose. We do not think this is an effective way to protect the investors. We suggest to provide clients with a well-written document which includes clear explanations of the recommendations that are provided to the clients, rather than simply rely on the verbal recommendations. We also think that providing financial advice should be a compulsory process to investors, unless the client chooses to opt out his right.

Part IV Post-sale arrangement – cooling off period

Q29 Do you believe that a cooling-off period would generally be beneficial for investors, or do you believe that costs associated with its implementation would outweigh the benefits for investors?

ipac HK: Cooling-off period can certainly allow investors to reconsider their investment decision after the trade is implemented and not to be "pushed" at the point of sales. However, we do not see the cooling-off approach adding much value to our clients. ipac HK's Lifestyle Financial Planning process typically includes at least three client meetings and numerous communications with the client before the actual investment implementation is processed. A written financial plan is also done for each client. We trust that this is sufficient enough to protect our clients.

As for the refund arrangement, we agree that the commission should be refunded with the principal invested amount. However, the client should also bear the market price differences and product fees involved.

Q30 Please provide your views on whether investors should be given a period of time after placement of their orders during which execution of the trade is delayed and the investor is given an opportunity to cancel the order before the trade is executed. If your view is that this would generally be beneficial to investors, please provide your views on the types of investment products for which it should be considered and the appropriate cooling-off timeframe.

ipac HK: We agree that investors should be given a period of time after placement of their orders during which execution of the trade is delayed and the investor is given an opportunity to cancel the order before the trade is executed unless he specifies to proceed with the trade immediately, and we suggest the timeframe to be 7 days.

Q31 Please provide your views on whether, and in what circumstances, you think a window could or should be provided to investors after the date the trade in the relevant product is executed during which an issuer should be required to buy back the product at an investor's request.

ipac HK: We agree that a cooling-off period would be of most beneficial for investors in situations:

- a) where there will be a relatively long lock-up period for the investment; and/or
- b) where there will not be dealings in the product or other liquidity provision on a frequent basis.

c) complex products such as derivatives and structure products

We believe that a well-structured, probably a quite complicated, system is required to be set up to buy back the products from the product issuer. We trust that most issues raised from the investors regards to the investment are about the investment advice rather than the nature of the investment product. Therefore, we do not think the product issuers should be responsible for the advice provided, whether it is appropriate or not.

Q32 On the basis that a cooling-off period is incorporated in an investment product and a client has exercised his right under the mechanism, do you consider that a distributor should promptly pass on to the client the full amount of refund (including the sales commission) received from the product issuer less a reasonable administrative charge? Please explain your views.

ipac HK: We agree that if a cooling-off period is incorporated in an investment product and a client has exercised his right under the mechanism, a distributor should promptly pass on to the client the full amount of refund (including the sales commission) received from the product issuer less a reasonable administrative charge.

This could eliminate the potential for investors to become less vigilant in reviewing the product at or prior to the point-of-sale, and the danger that the right may be abused by some investors who take advantage of it if no administrative fee is charged.