

MESSAGE

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From: "Odetta Ng" <ong@aima.org>

Date: 30/12/2009 11:44 AM

Subject: AIMA Comments of the SFC's Consultation paper on Proposals to Enhance Protection for the Investing Public

Dear Sir/Madam,

Here attached please find our submission in pdf file for your record, please confirm back to us upon received this mail. Thank you.

Best regards,

Odetta Ng

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Enhancing understanding, sound practices and industry growth

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AIMA Comments of the SFC's Consultation Paper on Proposals to Enhance Protection for the Investing Public

Part III.- Amendments to Professional Investor Rules

1. Investor Characterisation

There is merit in imposing a requirement on intermediaries to conduct due diligence to ensure that their clients have an understanding of the use and risks of derivative products before recommending such products.

It would be logical to extend this obligation to cases where the product in question is a fund, deposit, note or other structure which effectively acts as a "wrapper" for a derivative contract or transaction.

However, we do not believe that it would be appropriate to restrict promotion of funds which make use of derivatives for hedging or investment purposes as part of their investment strategy. In such circumstances, appropriate disclosure of the strategy and risks should be made in the offering document, and it is the obligation of the manager to make use of derivatives within the scope of his mandate, but it is not necessary for an investor in the fund to have experience of trading in derivatives.

We believe that the criteria which investors will need to meet to qualify as "clients with derivative knowledge" are too narrow. Very few investors will be willing to attend training courses on derivatives, and attendance will not necessarily enhance their understanding any better than reading the products offering materials. Even fewer investors will have derivative work experience, and the pool of investor with trading experience is likely to shrink if derivative products can no longer be promoted to investors who do not qualify as "clients with derivative knowledge".



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2. Suitability Obligation

The application of the suitability obligation and the extent of its scope is unclear, particularly in the context of promotion by fund managers.

In many cases, managers will appoint third party distributors or enter into commission agreements with entities such as banks, insurance companies and other financial intermediaries (“intermediaries”). In such circumstances it is clear that the investor is the client of the intermediary, and the intermediary will have the obligation to ensure suitability if the investor is not in professional investor (who meets the criteria set out in Ch. 15 of the Code of Conduct and have consented to be treated as such).

It is important to note that the intermediary acts as the agent of the investor and not of the manager or the fund in these circumstances.

However, where the manager promotes the fund which he manages directly to investors the position is less clear. The manager, not the agent of the investor, does not assume an obligation to advise the investor. There will not be a client agreement in the conventional sense. Under paragraph 6.4.2(b) of the Fund Manager Code of Conduct, where the manager is acting as distributor of an authorised fund the offering document and application form are regarded as the client agreement, but the position is left open where the manager is selling an unauthorised fund.

The Fund Manager Code of Conduct does not explicitly impose a suitability obligation on the manager in relation to the sale of interests in the fund he manages. Paragraph 1.4 of the Code of Conduct creates confusion as to whether the obligation of suitability in paragraph 5.2 of the Code of Conduct is intended to apply to fund managers. Paragraph 1.4 provides

“To the extent that a licensed or registered person acts in the capacity of a management company in relation to the discretionary management of collective investment scheme (whether authorised or unauthorised), the Code does not apply to such activity. In relation to such activities, such licensed or registered persons are subject to the Fund Manager Code of Conduct issued by the Commission.”



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Revisions to definition of "Professional Investor"

Many hedge fund managers have accepted a condition on their license that they will only deal with professional investors as defined in the SFO and subsidiary legislation. If this condition is intended to restrict managers from selling their funds to investors who are not professional investors as so defined, any change to the definition which would impose qualifying criteria such as those set out in 15.4 of the Code of Conduct may have a significant impact on the industry.

Yours faithfully,

Christophe Lee
Chairman
Alternative Investment Management Association Ltd. (AIMA)
Hong Kong Branch