

9th August 2013

Kinetic Partners (Hong Kong) Limited's response to SFC's consultation on proposed enhancements to the Professional Investor regime

Question 1: Should Corporate and Individual Professional Investors continue to be allowed to participate in private placement activities ?

Yes

Question 2: Do you think that the minimum monetary thresholds for Corporate and Individual Professional Investors should be increased ?

For corporations, we believe the current monetary thresholds are adequate. Although we believe that the current minimum monetary limit for Individuals is acceptable, we would nonetheless encourage Hong Kong to adopt a similar approach to Singapore and the United States, by providing an additional option for an individual to qualify as a professional investor, e.g. an individual whose income in a preceding period is not less than a certain level proscribed by the SFC.

Question 3: Do you agree that intermediaries should observe the Code without exception when they deal with individuals ?

This proposal has some merit and we agree that the vast majority of mis-selling cases involve individual investors. However, we believe that the current exemption on suitability should remain, that is, the Code should continue to allow the option for individuals to opt out of the suitability requirements. For example, someone who has worked in the financial industry for a substantial period of time on the front line, with liquid wealth well above the minimum HKD8 million, tend to be interested in intermediaries informing them of any products, as long as the chances of good returns are reasonable - notwithstanding the risks attached to the product. This type of individual will generally be in a position to make a considered decision and generally will be a discerning investor and therefore we believe it unnecessary for that individual to receive a copy of the intermediary's rationale for each investment recommendation and transaction conducted on his/her behalf. Such investor will not want to have his/her options or exposure to products limited based on a "client profile".

Our view is that licensed corporations have an existing obligation under the Code to act honestly and fairly toward their customers, and best practice for licensed corporations is to have some form of documentation on record, e.g. taped line or file note, confirming that the discussion that has taken place with respect to a particular transaction with a customer.

Question 4: Do you agree that investment vehicles wholly owned by individuals and by family trusts should be treated on the same basis as individuals under the Code ?

We do not agree. Traditionally investment vehicles and family trusts investing in financial products appoint experienced professionals to manage the assets under the structures. These individuals include professional trustees who have significant experience of fiduciary responsibilities for assets under management.

Question 5: Do you agree that a principles-based Knowledge and Experience Assessment should dispense with bright line tests concerning dealing experience ?

We agree with this proposal.

Question 6: Do you have any views on the Suitability Requirement ?

We believe that the Suitability Requirement is well-balanced between investor protection and compliance costs on intermediaries and no enhancements are required. It will be an unnecessary burden for intermediaries to provide each client with recommended product circulars and other relevant documents and rationale for investment recommendations, unless requested, for the reasons set out in our response to Question 3 and 4. Most Professional Investors who opt out of the suitability requirements still undertake reasonable due diligence on investment products and have robust discussions with intermediaries before making a decision. The process of assessing suitability in any event is subjective and notwithstanding any changes or enhancements, requires intermediaries and individual investors to apply their judgements on a number of issues.

Question 7: Do you agree with the above proposals in relation to the client agreement ?

The Suitability Requirement being incorporated into client agreements should be an option available, but not mandatory, and dependent on each customer and the category of service agreed, e.g. Managed Advisory.

We agree that client agreements should not contain terms which are inconsistent with the Code and should accurately set out, in clear terms, the actual services to be provided. We believe that the industry should adopt four broad categories:

- 1) Execution Only – Client gives instruction to trade and intermediary executes the trade;
- 2) Advisory Dealing – (non-managed advisory) – Intermediary makes recommendations (sometimes upon request) but does not have an obligation to review the suitability of the investment(s);
- 3) Managed Advisory – Intermediary makes recommendations but will need client's express approval before any trade AND has an obligation to review the suitability of the investment(s); and
- 4) Discretionary – Investment decision on behalf of client without their input but considering the investment parameters per the client agreement, client risk profile and the general market conditions.

For enquiry of the comments above, please contact

Yours faithfully,

KINETIC PARTNERS (Hong Kong) Limited

