



**Asia-Pacific
Economic Cooperation**

Asia Region Funds Passport consultation on the detailed rules and operational arrangements

Annexes 1, 2 and 3

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Annex 1: Host Economy Laws and Regulations

1 Purpose

This Annex sets out the Participants' understanding in relation to the obligations that may be imposed on a Passport Fund or its Operator in a Host Economy by the Host Economy Laws and Regulations. Each Participant will not apply Host Economy Laws and Regulations to a Passport Fund or its Operator, for which it is the Host Economy, other than in accordance with this Annex.

2 Main areas in which Host Economy Laws and Regulations may apply

(1) Each Participant may, in addition to the Passport Rules, choose to apply laws and regulations which apply to Regulated CIS in its economy on Passport Funds for which it is the Host Economy in the areas listed below:

- (a) Restrictions on the labelling of a Passport Fund as an exchange-traded fund, index fund, capital-guaranteed fund or money market fund;

Explanatory note:	Paragraph 2(1)(a) does not stipulate the requirements for labelling in a particular way. The provision articulates that labelling for the funds specified above is covered by the Host Economy laws and regulations.
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- (b) Disclosure and annual and periodic reporting (other than financial statements) to members, former members and prospective members including:
 - (i) point of sale disclosure relating to the product (for example, prospectuses and product highlight sheets) and any requirements to update that disclosure or provide continuous disclosure (for example, of significant changes);
 - (ii) any requirements to respond to requests for information from members or prospective members (for example, to provide a facility to enable confirmation that an investment has been accepted);
 - (iii) disclosure relating to the Passport Fund, other than information to be included in financial statements and audit report, for example, disclosure on portfolio holdings;
 - (iv) periodic reporting relating specifically to the members' interests or former members' interests in the Passport Fund including matters affecting the taxation position of members; and
 - (v) any requirements to provide consolidations or copies of documents or translated copies of documents including constituent documents, financial statements or reports and registers of members (but not relating to the content or manner of keeping those documents unless otherwise provided in this Annex).
 - (c) Distribution and licensing of distributors operating in the Host Economy, including:
 - (i) licensing requirements for the provision of financial advice and the offering of financial products and any associated obligations;
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- (ii) distribution agreements including the payment of commissions by a Passport Fund or its Operator to distributors;
 - (iii) listing or quotation on financial markets;
 - (iv) advertising of financial products;
 - (v) offering interests to investors; and
 - (vi) communication with members or prospective members (including misleading and deceptive conduct in relation to such communication).
- (d) Member complaints including:
- (i) the manner in which complaints are received, processed and responded to by a Passport Fund or its Operator; and
 - (ii) any requirement for membership of an external dispute resolution scheme; and
- (e) Appointing a local representative or agent in its economy, requiring the Passport Fund or its Operator to register as a foreign company, or both.
- (2) Notwithstanding subsection (1)(c) above, an Operator shall not require licensing for the provision of advice to or through, or in relation to its issue or offer of interests in a Passport Fund to or through, a qualified distributor, where such conduct is undertaken for the purpose of distributing interests in the Passport Fund.

Explanatory note:	Passport Funds will not be required to be licensed in order to approach a qualified distributor where retail investors are not involved.
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- (3) For the purposes of subsection (2), a qualified distributor is an entity or person that arranges for the acquisition or, who may market, solicit, or offer interests in a Passport Fund on behalf of its Operator, and is licensed or exempted from licensing for such activities under the Host Economy Laws and Regulations.

[Table to be inserted post-consultation]

- (4) For the purposes of subsection 2, there must be at least one class of qualified distributor in each Host Economy.

Consultation question 1:	<p>For certainty, the Working Group intends to provide a table which will specify who is a qualified distributor in a Participant. This will reflect the approach identified in subsection (3) above, although there will be some differences.</p> <p>For Singapore, a qualified distributor may be restricted to certain entities such as banks and holders of a capital markets service licence. For Australia, a qualified distributor would be the holder of an Australian financial services licence authorised to deal in interests in managed investment schemes.</p> <p>The Working Group is seeking feedback on whether, in relation to each economy, there are adequate avenues through which an Operator is able to market a Passport Fund without obtaining a licence in that economy.</p>
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3 Additional requirements may be imposed

Each Participant, in its capacity as a Host Economy, may impose requirements on a Passport Fund or its Operator, within the matters referred to in section 2, in relation to their dealings with members, former members or prospective members that are additional to those imposed on Regulated CIS that are not a Passport Fund and its Operator, if the additional obligations:

- (a) are not unduly burdensome for the Passport Fund in comparison to Regulated CIS in its economy that is not a Passport Fund; and
- (b) are reasonable to promote confident retail investment in Passport Funds in the Host Economy.

Note: For example, excluding the application of shorter form disclosure that is applicable to some of those Regulated CIS to Passport Funds.

4 Other understanding

- (1) Each Participant will ensure that any fee or charge imposed in relation to a Passport Fund or its Operator for which it is the Host Economy does not exceed any fee or charge payable in relation to Regulated CIS in that economy or its Operator in like circumstances. If there is no corresponding fee or charge relating to Regulated CIS in that economy, any fee or charge should not exceed a reasonable estimate of the cost to the Participant of performing the relevant function in relation to the Passport Fund.
- (2) Each Participant will ensure that the offering of interests of a Passport Fund in a Host Economy will not create a taxable presence in that economy.

5 Guidance

Each Participant will ensure that guidance is prepared on the Host Economy Laws and Regulations that will apply to Passport Funds that offer interests in its economy including a comprehensive list of applicable Host Economy Laws and Regulations. Such guidance, or a hyperlink to such guidance, will be published in English on the official Passport website.

6 Recognition frameworks

This Annex does not prevent a Participant from introducing or maintaining a framework for the recognition of Passport Funds or their Operators, provided it:

- (a) is consistent with the Common Regulatory Arrangements in Annex 2; and
- (b) does not impose obligations on Passport Funds that are additional to the Home Economy Laws and Regulations, the Passport Rules, and understanding relating to Host Economy Laws and Obligations set out in this Annex.

Annex 2: Common Regulatory Arrangements

Part 1 General

1 Purpose

This Annex contains the regulatory arrangements for Passport Funds to which each Participant will give effect. This Annex is not designed to be directly incorporated into the law of a Participant.

2 Interpretation

Unless otherwise specified,

- (a) all notifications required to be given by this Annex are to be in writing;
- (b) any document required to be given to a Passport Regulator by this Annex must be translated into an official language of the relevant economy, if requested by the Passport Regulator; and
- (c) any public register required to be kept by this Annex must be available on the internet and free of charge.

Part 2 Application process

3 Registering a Regulated CIS as a Passport Fund

- (1) An Operator or a Regulated CIS may lodge an application to register a Regulated CIS or a sub fund of a Regulated CIS as a Passport Fund with the Home Regulator for the Regulated CIS.
- (2) To be considered by the Home Regulator, the application must contain:
 - (a) the general information to be agreed by Passport Regulators (Part A);

Explanatory note: The information referred to in paragraph 3(2)(a) could include matters such as:

- details of the Operator and custodian;
- the name and objectives of the Regulated CIS or sub fund;
- details of key people associated with the Regulated CIS or sub fund;
- the constituent documents;
- consent to the disclosure of information between regulators and others; and
- consent to the publication of the application or part of the application as part of the public register.

- (b) any specific information required by the Home Regulator (Part B); and
 - (c) any fee charged by the Home Regulator.
 - (3) The Home Regulator may register the Regulated CIS or the sub fund of the Regulated CIS as a Passport Fund only if it is of the opinion that:
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- (a) it is a Regulated CIS or a sub fund of a Regulated CIS in the Home Economy;
 - (b) its Operator is an *eligible entity*; and
 - (c) it is likely to be operated in compliance with:
 - (i) the Home Economy Laws and Regulations; and
 - (ii) the Passport Rules.
- (4) For subsection (3), the Operator of the Regulated CIS is an *eligible entity* only if at the time of application of each Regulated CIS or sub fund;
- (a) it and its related parties are responsible for the operation of financial asset CISs with a total value of at least USD 500,000,000; and
 - (b) it has officers with the relevant qualifications (see section 10 of the Passport Rules); and
 - (c) it meets the financial resources test (see section 11 of the Passport Rules); and
 - (d) it meets the organisational arrangements test (see section 12 of the Passport Rules);
 - (e) it meets the track record test (see section 13 of the Passport Rules); and
 - (f) it meets the good standing test (see section 14 of the Passport Rules); and
 - (g) it has a principal place of business in the Home Economy of the Regulated CIS.
- (5) If the Home Regulator decides to register a Passport Fund under subsection (3), it must allocate the Passport Fund a unique registration code.
- (6) A Regulated CIS or sub fund of a Regulated CIS becomes a Passport Fund on receiving a unique registration code under subsection (5).

Explanatory note:	The Working Group expects the registration code will be set by the Home Regulator in consultation with other Passport Regulators to avoid duplication, for example, all Singaporean funds could start with '1', all New Zealand funds could start with '2' etc.
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4 Offering interests in a Host Economy

- (1) To offer interests in a Host Economy as a Passport Fund, a Passport Fund must:
- (a) apply to the Host Regulator for entry in accordance with subsection (2); and
 - (b) complete the entry process that the Host Economy has implemented under subsection (3).
- (2) An application for entry to a Host Economy must contain:
- (a) the Passport Fund's unique registration code;

Explanatory note:	This will be proof of registration as a Passport Fund by the Home Regulator and can be checked against the public register.
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- (b) Part A of the Passport Fund's registration application;
- (c) any document or information required by the Host Regulator which is reasonably required under or is necessary to assess the Passport Fund's compliance with the Host Economy Laws and Regulations; and
- (d) any fee charged consistently with subsection 4(1) of Annex 1.

Explanatory note:	The documents or information referred to in paragraph 4(2)(c) could include: disclosure documents; details of local agent; and details of external dispute resolution membership.
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- (3) There will be two entry processes a Participant can implement:
 - (a) the streamlined authorisation process described in section 5; or
 - (b) the notification process described in section 6.
- (4) Under either process described in subsection (3), the entry process is not completed if the application is refused.
- (5) An application for entry may only be refused, having afforded procedural fairness to the applicant in accordance with the Host Economy Laws and Regulations, if the Host Regulator is of the opinion that:
 - (a) the Passport Fund or its Operator, in respect of that Passport Fund, does not comply with or is not likely to comply with:
 - (i) the Host Economy Laws and Regulations;
 - (ii) the Home Economy Laws and Regulations; or
 - (iii) the Passport Rules; or
 - (b) it is not in the public interest of the Host Economy to authorise the Passport Fund for offer in the Host Economy or authorising the Passport Fund would breach sanctions applied against another economy in the Host Economy; or

Explanatory note:	Paragraph 4(5)(b) may also be used to give effect to sanctions against a particular country. For example, in a scenario where Country 1 has imposed sanctions against Country 2, and ARFP member economy A has chosen to join in the imposition of sanctions, but ARFP member economy B has not. ARFP member economy A may reject a Passport Fund from ARFP member economy B that has investments in Country 2.
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- (c) an exemption from or modification to a Passport Rule has been given to the Passport Fund in accordance with Part 6 of this Annex and the Host Regulator has not agreed and does not agree to the exemption or modification; or
 - (d) the name of the Passport Fund is not available for use in the Host Economy because it is already in use or the use of the name is subject to restriction in the Host Economy that also applies to Regulated CIS in the Host Economy.
- (6) The opinion of the Home Regulator will be used by a Host Regulator for the purpose of determining, under subparagraphs (5)(a)(ii) or (iii) and section 10 whether the Passport Fund or its Operator has complied or is likely to comply with a Home Economy Law or Regulation or to a Passport Rule where such Passport rule refers to the opinion of the Home Regulator.
 - (7) For the purposes of paragraph (5)(b), the public interest may not include any benefit to the Host Economy that may arise from limiting competition to the Host Economy's fund management industry.

5 Streamlined entry process

- (1) A Passport Fund completes the streamlined authorisation process when the Host Regulator authorises the Passport Fund for offer in the Host Economy.

- (2) The Host Regulator must assess the application within 21 days of receipt of a complete application (the assessment period).
- (3) For the purposes of subsection (2), an application is complete if the Host Regulator did not, within 21 days after the day the Passport Fund applies for entry into the Host Economy, notify the Passport Fund, or its Operator that the Host Regulator is of the opinion that the application does not include all the information required in the application in subsection 4(2).
- (4) The Host Regulator and either the Passport Fund or its Operator may agree in writing to further extensions of the assessment period for additional periods of up to seven days each time. Such an agreement must be made before the expiration of the assessment period, taking into account any prior extensions that have already been agreed upon.

6 Notification process

- (1) A Passport Fund completes the notification process when 21 days have passed since the Passport Fund made a complete application for entry into the Host Economy (the exposure period) and the Host Regulator has not notified the Passport Fund that its application for entry is refused.
- (2) The Host Regulator and the Passport Fund, or its Operator may agree in writing to further extensions of the exposure period for additional periods of up to seven days each time. Such an agreement must be made before the expiration of the assessment period, taking into account any prior extensions that have already been agreed upon.
- (3) For the purposes of subsection (1), an application is complete if the Host Regulator did not, within 21 days after the day the Passport Fund applies for entry into the Host Economy, notify the Passport Fund, or its Operator that the Host Regulator is of the opinion that it does not include all the information required in the application in subsection 4(2).

7 Register of Passport Funds

- (1) Each Passport Regulator will maintain a current public register of the Passport Funds and deregistered Passport Funds for which it is the Home Regulator in English, which includes:
 - (a) Part A of a Passport Fund's registration application except the Passport Fund's constituent documents and any portion of Part A marked in the form published by Passport Regulators as confidential;
 - (b) a Passport Fund's unique registration code;
 - (c) a list of the economies in which a Passport Fund has completed the entry process notified to the Home Regulator;
 - (d) any updated information in relation to information provided by the Operator of matters on the public register;
 - (e) any notification by an Operator of the commencement or completion of the winding up of a Passport Fund, the deregistration of a Passport Fund or the cessation of the obligations relating to a deregistered Passport Fund;
 - (f) any exemption or modification of the Passport Rules applying to the Passport Fund and not a class of the Passport Fund; and

- (g) financial statements and reports of auditors of financial statements of the Passport Fund provided to the Home Regulator.
- (2) The registers referred to in subsection (1) may be consolidated.

Explanatory note: This is to allow for the possibility of combining the registers on the Asia Region Funds Passport website.

8 Confidentiality

- (1) Subject to Annex 4, each Passport Regulator will take all reasonable measures to keep confidential, information provided to it by a Passport Fund or Operator of a Passport Fund.

Explanatory note: Annex 4 (not released as part of this consultation) will contain arrangements for cross-border supervisory arrangements for regulators.

- (2) Notwithstanding subsection (1) but subject to subsection (3) a Passport Regulator may disclose the information referred to in subsection (1) if the law in the economy of the Passport Regulator requires or permits disclosure.
- (3) Where the Passport Regulator is the Host Regulator and to the extent disclosure of the information referred to in subsection (1) is permitted but not required by the law in the economy of the Passport Regulator, the Passport Regulator may disclose such information only when reasonable having regard to:
 - (a) the purposes of the MOU; and
 - (b) the interests of a Passport Fund and its Operator to which such information relates.

Part 3 Supervisory and investigative powers

9 Supervisory and investigative powers

- (1) A Passport Regulator will have power to use any supervisory, investigative and information gathering powers that it has in relation to Regulated CIS and Operators in its economy in order to:
 - (a) supervise the compliance of a Passport Fund for which it is the Home Regulator with the Home Economy Laws and Regulations and the Passport Rules;
 - (b) supervise the compliance of a Passport Fund for which it is the Host Regulator with the Host Economy Laws and Regulations that apply to the Passport Fund in its economy and the Passport Rules; and
 - (c) assist another Passport Regulator to supervise Passport Funds as described in paragraphs (a) and (b) above where the assisting regulator is the Home Regulator or the Host Regulator, subject to the provisions set out in Annex 4.
- (2) The powers referred to in subsection (1) could, but are not required to, include the power to:
 - (a) require the provision of information, books or records;
 - (b) require a person to make a statement or attend an examination;

- (c) require the preparation of a separate set of audited financial statements where the Host Regulator believes that the audit report prepared in the Home Economy is not true and fair; or

Explanatory note:

The Working Group inserted subsection 9(2) to allow some flexibility for jurisdictions where a Host Regulator can verify the financial statement, for example, checking the details of a balance sheet audited by an auditor regulated in the Host Economy. It is not intended that a Host Regulator be able to use these powers on every Passport Fund.

- (d) conduct an on-site examination.

Part 4 Administrative powers

10 Stop orders, suspension of authorisation or revocation of authorisation

Orders issued by the Home Regulator

- (1) In the circumstances set out in subsection (2), a Passport Regulator must have the power to notify a Passport Fund or its Operator for which it is the Home Regulator that it must not or must no longer offer interests in the Passport Fund to persons in the Home Economy and any Host Economy, or take other action to achieve that outcome.
- (2) The power in subsection (1) must be able to be exercised if the Passport Regulator is of the opinion that the Passport Fund is not complying, or is not likely to comply, with:
 - (a) the Home Economy Laws and Regulations; or
 - (b) the Passport Rules.

Orders issued by the Host Regulator

- (3) Subject to subsection (4), a Passport Regulator may notify a Passport Fund or its Operator for which it is the Host Regulator that it must not or must no longer offer interests in the Passport Fund in its economy, or take other action to achieve that outcome.
- (4) The power in subsection (3) may only be exercised if:
 - (a) the Passport Regulator is of the opinion that the Passport Fund is not complying or is not likely to comply with any Host Economy Laws and Regulations that apply to the Passport Fund in its economy, or
 - (b) both of the following apply:
 - (i) the Passport Regulator is of the opinion that the Passport Fund is not complying or is not likely to comply with the Home Economy Laws and Regulations or the Passport Rules; and

- (ii) the Passport Regulator is satisfied that the stop order or other action is necessary considering the potential impact of the non-compliance or potential non-compliance on the members or potential members of the Passport Fund in its economy and any action taken or that may be taken by the Passport Fund's Home Regulator.

Application of orders

- (5) The orders in subsections (1) and (3) will be able to be expressed to apply either for a particular or indefinite period.
- (6) The period referred to in subsection (5) may be extended by notice to the Passport Fund if a condition for issuing the order in subsection (2) or (4) continues to be met.
- (7) Before issuing an order under subsection (1) or (3) or extending an order under subsection (6), the Passport Regulator must afford the Passport Fund procedural fairness to the extent that this is practicable in the context of protecting members and potential members in accordance with the Laws and Regulations in its economy.
- (8) A Passport Regulator will revoke, or otherwise cease or negate the effect of an order issued under subsection (1) or (3) by notice to the Passport Fund if the Passport Fund can establish to the Regulator's satisfaction that the conditions for issuing the order in subsections (2) or (4) no longer apply, and provided that such an order or other action may be revoked or ceased under the relevant Laws and Regulations.

11 Other administrative action

- (1) A Passport Regulator will be able to use any administrative powers that it has in relation to Regulated CIS and their Operators when dealing with Passport Funds and their Operator for which it is the Home Regulator.
- (2) The powers referred to in subsection (1) could, but are not required to, include the power to:
 - (a) direct or order that a Regulated CIS or Operator do something or refrain from doing something;
 - (b) prohibit, temporarily or permanently, the Operator or its directors or officers from operating or being involved in the operation of a Regulated CIS including by revoking their licence or authorisation;
 - (c) remove or replace the Operator;
 - (d) warn or caution a Regulated CIS or Operator;
 - (e) accept an enforceable undertaking from the Regulated CIS or Operator;
- (3) In addition to the grounds provided for in the laws and regulation of its economy for Regulated CIS that are not Passport Funds, a Passport Regulator will be able to exercise the powers referred to in subsection (1) in relation to Passport Funds for which it is the Home Regulator if:
 - (a) the Passport Regulator is of the opinion that the Passport Fund has not complied with or is not likely to comply with the Home Economy Laws and Regulations or the Passport Rules; or
 - (b) both of the following apply;

- (i) a Host Regulator of the Passport Fund is of the opinion that the Passport Fund has not complied with or is not likely to comply with the Host Economy Laws and Regulations; and
- (ii) the Passport Regulator is satisfied that it should use its administrative powers given the potential impact of the non-compliance or potential non-compliance on the members or potential members of the Passport Fund.

Explanatory note:

This does not restrict where the action may be taken. An action may be brought in the economy of a member alleging breaches of the law of another economy. This is provided for in the Passport Rules which require the constituent documents to contain a mandatory choice of forum clause (where the forum is the member's Home Economy).

12 Action by regulators

- (1) In addition to the power to take administrative action in relation to a Passport Fund registered in its economy under section 10, each Passport Regulator will have the power to prosecute or refer to a relevant authority in its economy for criminal prosecution in respect of:
 - (a) a breach of the Home Economy Laws and Regulations or Passport Rules by a Passport Fund registered in its economy, the Operator or an officer of the Operator where it is the Home Regulator; and
 - (b) a breach of the Host Economy Laws and Regulations or Passport Rules by a Passport Fund offered in its economy, the Operator or an officer of the Operator where it is the Host Regulator.
- (2) The power of a regulator in subsection (1) may be restricted to situations in which there has been a serious breach, which includes, for example, a breach that is intentional, reckless or dishonest.
- (3) A Passport Regulator may, but is not required to, have the power to issue a fine or order compensation or to request a court to issue a fine or order compensation in the circumstances referred to in subsection (1).
- (4) This paragraph does not limit other powers a Passport Regulator may have in relation to a Passport Fund for which it is the Home Regulator including the power to freeze the assets of a Passport Fund or cause such assets to be frozen.

Part 6 Exemptions and modifications**13 Exemptions and modifications**

- (1) A Passport Regulator may exercise any powers it has to:
 - (a) exempt a Passport Fund for which it is the Home Regulator from the Home Economy Laws and Regulations or modify those regulations with respect to a Passport Fund; or
 - (b) exempt a Passport Fund for which it is the Host Regulator from the Host Economy Laws and Regulations that apply to the Passport Fund in its economy or subject to Annex 1, modify those Laws and Regulations with respect to a Passport Fund.

- (2) A Home Regulator may exempt a Passport Fund from a Passport Rule or modify a Passport Rule with respect to such a Passport Fund or vary or revoke an exemption or modification if all Host Regulators of the Passport Fund agree to the exemption or modification or to the variation or revocation of the exemption or modification of the Passport Rule.
- (3) Where an exemption or modification to a Passport Rule is granted, varied or revoked, the Home Regulator must notify any affected Passport Fund.
- (4) Each Passport Regulator must maintain or ensure there is maintained a current public register of any exemption or modification it grants under this Part to a Passport Fund, which includes the details of the exemption or modification.
- (5) The registers referred to in subparagraph (4) may be consolidated.

Part 7 Deregistration and winding up

14 Deregistration as a Passport Fund

- (1) A Passport Fund may be deregistered by the Home Regulator if:
 - (a) the Home Regulator is of the opinion that the Passport Fund is not complying or is not likely to comply with the applicable Home Economy Laws and Regulations or the Passport Rules; or
 - (b) at the request of the Passport Fund if it no longer has any members:
 - (i) who became members:
 - (A) when the deregistered fund was registered as a Passport Fund; or
 - (B) on the expectation that the fund would become a Passport Fund;
 - (ii) who are not the current Operator or any previous Operator; and
 - (iii) who are not related parties of the current Operator or any previous Operator.
- (2) Deregistration as a Passport Fund does not affect the status of the Passport Fund as a Regulated CIS or sub fund of a Regulated CIS.

15 Deregistration as a Regulated CIS

- (1) The deregistration of a Regulated CIS that is a Passport Fund will be in accordance with Home Economy Laws and Regulations applying to Regulated CIS.
- (2) A Home Regulator will not deregister a Regulated CIS, on the application of a Regulated CIS or Operator or otherwise a Regulated CIS that was, or had a sub fund which was, a Passport Fund if it is of the opinion that to do so would not be in the interests of members of the sort described in paragraph 14(1)(b). In reaching this opinion, a Home Regulator will take into account the implications of deregistration on the Regulated CIS' continued requirement to comply with the Home Economy Laws and Regulations applying to Regulated CIS and the Passport Rules and any other relevant matters.

- (3) If a Passport Fund, or Regulated CIS in which a sub fund is a Passport Fund, is deregistered as a Regulated CIS it will immediately cease to be a Passport Fund.

Explanatory note:

Since deregistration will deprive investors of protections, including foreign protections, no decision to do so would be made if it would be contrary to their interests. Other steps may be appropriate to restrict the operation of the scheme, for example, stop orders, or punishment. This is what subsection 15(2) is intended to address.

16 Winding up

- (1) Winding up of a Passport Fund will be in accordance with the Passport Fund's Home Economy Laws and Regulations, subject to subsection (2).
- (2) A member of a Passport Fund will not be unfairly disadvantaged under the Home Economy Laws and Regulations relating to the winding up of a Regulated CIS by reason of the member not being present in the home economy.

Explanatory note:

Subsection 16(2) is intended to address any differences between investors relating to different rights to the amount and time of payouts based on where the investor is. For example, a member must have a right to appoint a proxy at a meeting of members and access to the same information as members in the Home Economy. However, this is not an issue if the difference arises from holding a different class of interest.

Annex 3: Passport Rules

Explanatory note: The Passport Rules should be read in conjunction with the Feedback Statement.

Part 1 Introduction

1 Citation

The rules set out in this Schedule may be cited as the Rules, the Passport Rules, or the Passport Rules (Annex 3 to the Memorandum of Understanding on the Asia Region Funds Passport).

2 Application of Rules in the Economy of a Participant

These Rules apply in an economy that is a Participant when they are legally enforceable in the economy of the Participant.

3 Interpretation—the Dictionary

- (1) The Dictionary at the end of these Rules defines certain words and expressions, and includes references to words and expressions that are defined elsewhere in these Rules.
- (2) A definition in the Dictionary applies to each use of the word or expression in these Rules unless the contrary intention appears.

Part 2 Constituent documents

4 Constituent document for a Regulated CIS

- (1) The Operator of a Passport Fund must ensure that the Passport Fund has a compliant constituent document at all times.
- (2) For these Rules, the *constituent document* of a Regulated CIS is the document shown in the following table:

Annex 3 – Passport Rules

Home Economy of the Passport Fund	Constituent document
Australia	The constitution of the registered scheme required by the <i>Corporations Act 2001</i> (Cth).
Korea	The trust contract of the Operator (if it is an investment trust) or articles of incorporation of the Operator (if it is an investment company) under the Financial Investment Services and Capital Markets Act of Korea.
New Zealand	The governing document for the managed investment scheme required by the <i>Financial Markets Conduct Act 2013</i> of New Zealand.
Philippines	Effective Registration Statement and Prospectus pursuant to the Securities Regulation Code and Investment Company Act.
Singapore	The trust deed required for the collective investment scheme constituted as a unit trust to be authorised under the Securities and Futures Act of Singapore.
Thailand	In case of a scheme established as a mutual fund, the commitment between the unit holders and the securities company required under the Securities and Exchange Act of Thailand. In a case of a scheme established as a trust, the trust deed as required by the Trust for Transactions in Capital Market Act.

(3) For this section, the constituent document is **compliant** if the constituent document includes provisions that:

(a) either confer on:

- i. each member of the Passport Fund a right to take civil action against the Passport Fund, if it is a legal entity, and its Operator, in both the Home and any Host Economy of the Passport Fund, to seek remedy in relation to loss suffered by the member due to breach of duty to the member arising from a breach of the Home Economy Laws and Regulations or breach of the Passport Rules by the Passport Fund, or its Operator; or
- ii. a specified person the power and duty to take civil action on behalf of any member of a Passport Fund when it is in the best interests of members against the Passport Fund, if it is a legal entity, or its Operator in both the Home and any Host Economy of the Passport Fund, to seek remedy in relation to loss suffered by the member due to breach of duty to member arising from a breach of the Home Economy Laws and Regulations or breach of the Passport Rules by the Passport Fund or its Operator;

- (b) includes a provision to the effect that the Passport Fund, if it is a legal entity, and its Operator agrees that where a member of the Passport Fund has commenced proceedings against the Passport Fund or its Operator in a court in the member's economy, that court will be a convenient forum to hear the proceedings, unless a similar action has been commenced against the Passport Fund or its Operator in another economy and it would be reasonable for the member to participate in that action; and
 - (c) includes a provision to the effect that the Passport Fund, if it is a legal entity, and its Operator agrees that the convenient forum for the Passport Fund or its Operator bringing an action against a member will be the member's economy unless the member otherwise agrees in writing in relation to the particular proceedings.
- (4) For this section, the *member's economy* in relation to the Passport Fund is:
- (a) the economy in which the member was when they applied to be accepted as a member of a Passport Fund if that economy is a Participant; or
 - (b) in all other cases, the Home Economy.

Part 3 The Operator of a Passport Fund

5 Responsibility of Operator for compliance

Unless these Rules provide otherwise, the Operator is responsible for compliance with a provision that is expressed to impose obligations on a Passport Fund.

6 Qualifications of officers

- (1) The Operator of a Passport Fund must ensure that at all times it has officers with the relevant qualifications.
- (2) For this section, the Operator has *officers with the relevant qualifications* only if it has the following officers or employees with the qualifications or experience indicated:
 - (a) a chief executive officer (or the equivalent) with at least 10 years' relevant experience within the previous 15 years as an officer or employee in an IOSCO financial services related business, with 5 of the 10 years in a managerial or supervisory role;
 - (b) at least 2 executive directors (or the equivalent) each with at least 5 years' relevant experience within the previous 7 years as an officer or employee in a managerial or supervisory role in an IOSCO financial services related business; and
 - (c) 1 or more investment officers, each with either:
 - (i) a bachelor degree, or equivalent, or higher qualification in a relevant discipline, together with at least 3 years' experience within the previous 5 years as an officer or employee with responsibility for making or supervising discretionary investment decisions in an IOSCO financial services related business; or

- (ii) at least 5 years' experience within the previous 7 years as an officer or employee with responsibility for making or supervising discretionary investment decisions in an IOSCO financial services related business.
- (3) For this section:

investment officer means a person who:

 - (a) is an officer or employee of the entity; and
 - (b) is responsible, or is collectively responsible with other investment officers, for making or overseeing discretionary investment decisions for the Passport Fund.
- (4) For this section, a reference to supervising discretionary investment decisions includes monitoring and evaluating on behalf of an entity the performance of another entity that makes discretionary investment decisions as a delegate of the first entity, and being significantly involved in decisions about whether the second entity should remain as a delegate in light of its performance.

7 Financial resources of the Operator

Consultation question 2: The financial resources test is set with reference to a specific currency, USD. Is it appropriate to set the currency as USD for the purposes of the requirements, given possible fluctuations in currency?

- (1) The Operator of a Passport Fund must at all times meet the financial resources test.
- (2) For this section, the Operator *meets the financial resources test* if its equity is greater than USD 1,000,000 plus additional capital amount.
- (3) In calculating the Operator's equity:
 - (a) a guarantee or undertaking held by the Operator may be counted as if it were an asset if, and only if, it:
 - (i) is unconditional;
 - (ii) does not give rise to any liability for the Operator;
 - (ii) is payable on demand; and
 - (iii) is provided by a body that is subject to prudential supervision by a financial supervisory authority broadly under the guidelines of the Basel Committee on Banking Supervision in an economy in which the body has a principal place of business; and
 - (b) the value of an approved professional indemnity insurance policy may be counted but only up to 80% of the additional capital amount.
- (4) For this section:

additional capital amount means $0.001 \times (\text{total assets under management} - \text{USD } 500,000,000)$ and is capped at USD 20,000,000.

approved PI insurance policy means a professional indemnity insurance policy that has been approved for this section by the Home Regulator.

equity of the Operator means the net equity after taking into account losses, as it would appear on a balance sheet prepared in accordance with the relevant accounting standards.

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relevant accounting standards, for a Home Economy listed in the following table, has the meaning given in the following table:

Home Economy of the Passport Fund	Relevant accounting standards
Australia	The accounting standards made by the Australian Accounting Standards Board under section 334 of the <i>Corporations Act 2001</i> (Cth).
Korea	General accounting principles of financial investment under Article 32 of The Financial Investment Services and Capital Market Act of Korea, and standards for accounting under Article 13 of the Act on External Audit of Stock Companies.
New Zealand	The accounting standards issued by the External Reporting Board under Part 2 of the <i>Financial Reporting Act 2013</i> .
Philippines	Philippine Financial Reporting Standards.
Singapore	The relevant accounting standards made by the Accounting Standards Council under the Accounting Standards Act (Cap. 2B) and the Recommended Accounting Practices (or its equivalent) issued by the Council of the Institute of Singapore Chartered Accountants (or its successors).
Thailand	The accounting standards made by the Federation of Accounting Profession under the <i>Accounting Profession Act</i> (2004).

total assets under management, in relation to an Operator, means the sum of the value of:

- (a) the assets of each CIS for the operations of which it is responsible; and
- (b) any other assets for which it performs discretionary investment management on behalf of another person, whether or not on a collective basis;

as those assets would appear on a balance sheet prepared in accordance with the relevant accounting standards for the entity if they were held by the Operator.

8 Organisational arrangements of the Operator

- (1) The Operator of a Passport Fund must at all times meet the organisational arrangements test.
- (2) For this section, the Operator of the Passport Fund *meets the organisational arrangements test* if it has:
 - (a) a well-documented organisational structure that clearly assigns responsibilities and specifies reporting lines;
 - (b) adequate internal control mechanisms including procedures and systems that ensure that:

- (i) assets are managed in accordance with the current constituent documents and disclosure documents of the Passport Fund as well as the Home Economy Laws and Regulations and these Rules;
- (ii) records are kept to sufficiently explain the transactions of the Passport Fund, and all transactions in the interests of the Passport Fund; and
- (iii) registers of members are duly kept;
- (c) an adequate risk monitoring and management process including a risk management framework for the Passport Fund assets, based on the size, complexity and risk of the assets;
- (d) a compliance framework that ensures ongoing compliance with relevant laws and regulations; and
- (e) adequate procedures to manage conflicts of interest.

9 Track record of Operator

(1) The Operator of a Passport Fund must at all times meets the track record test.

Track record—experience of the Operator

(2) For this section, the Operator **meets the track record test** if the Home Regulator is satisfied that:

- (a) for the past 5 years the Operator has been responsible for the operation of financial asset CIS that have been regulated in a way that enables interests in the CIS to be offered to the general public in:
 - (i) a Participant; or
 - (ii) an economy that has a regulatory framework applying to financial asset CIS that is broadly similar in effectiveness to that of the Home Economy in the opinion of the Home Regulator, having regard where relevant to the IOSCO principles and assessment methodology relating to CIS; and
- (b) if the Operator has undergone a relevant change of control:
 - (i) there has been substantial continuity among the officers and employees of the Operator responsible for making discretionary investment decisions for financial asset CIS; and
 - (ii) the decision-making process of the Operator in relation to the operation of financial asset CIS has been independent of any person who controls the Operator.

Track record—experience of a related entity of the Operator

(3) For this section, an Operator is also taken to **meet the track record test** if the Home Regulator is satisfied that:

- (a) the Operator is able to rely on the experience and expertise of a related party in the operation of financial asset CIS having regard to the degree of commonality between the Operator and the related party concerning:
 - (i) decision-making processes;
 - (ii) business processes; and
 - (iii) staff; and

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- (b) the related party meets the track record test in accordance with subsection (2).
- (4) For this section, an Operator (the *first entity*) undergoes a *relevant change of control* if during the past 5 years:
 - (a) an entity has commenced to control the first entity; or
 - (b) an entity has ceased to control the first entity.

10 Good standing of Operator

- (1) The Operator of a Passport Fund must at all times meet the good standing test.
- (2) For this section, the Operator meets the good standing test if the Home Regulator has not notified the Operator that it is of the opinion that there is reason to believe that there is a material risk that a relevant party does not have the integrity or competence required to operate a Passport Fund honestly and competently, and to act in good faith in the interests of the members of the Passport Fund.
- (3) For this section, *relevant party* means any of the following:
 - (a) the Operator;
 - (b) an officer of the Operator;
 - (c) an entity that controls the Operator; and
 - (d) to the extent that the Home Regulator considers relevant, an officer of an entity that controls the Operator.
- (4) In assessing the matters mentioned in subsection (2), the information that the Home Regulator may take into account includes:
 - (a) any relevant finding about a relevant party made by a regulatory body or dispute resolution service;
 - (b) any relevant enforcement action taken by a regulatory body against a relevant party;
 - (c) any relevant judgement or decision in relation to a relevant party given by a court, tribunal, arbitrator, dispute resolution service or equivalent person or body;
 - (d) any relevant settlement reached by a relevant party with a regulatory body, or in relation to an action or proposed action before a court, tribunal, arbitrator, dispute resolution service or equivalent person or body; and
 - (e) any relevant enforceable undertaking or equivalent given by a relevant party to a regulatory body, court, tribunal, arbitrator, dispute resolution service or equivalent person or body.

11 Delegation of functions by Operator

- (1) Subject to any limitations in the Home Economy Laws and Regulations, a function of the Operator of a Passport Fund may be delegated or sub-delegated by the Operator only if the Operator:
 - (a) remains responsible to members for the delegated function;
 - (b) ensures that the delegate employs an appropriate standard of care when performing the delegated function;
 - (c) has in place suitable processes to:

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- (i) monitor and control the activities of the delegate in relation to the delegated function; and
- (ii) evaluate the performance of the delegate in relation to the delegated function;
- (d) ensures that the Home Regulator is at all times able to access information about the delegated functions from the Operator or the delegate; and
- (e) ensures that the performance of the function by the delegate can be effectively monitored and reviewed under these Rules as if done by the Operator.

Limitation on delegation of investment management function

- (2) The function of making discretionary investment decisions for the Passport Fund may only be delegated to an entity (a ***qualifying delegate***) that is regulated by a regulator that is a signatory to Appendix A of the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information.
- (3) Where the function of investment management for more than 20% of the adjusted value of the assets is delegated, the delegate must be regulated in a Participant or in an economy that has a regulatory framework applying to financial asset CIS that is broadly similar in effectiveness to that of the Home Economy in the opinion of the Home Regulator, having regard where relevant to the IOSCO principles and IOSCO assessment methodology relating to CIS.

Explanatory note:	To provide certainty, the Working Group considers, for example, that the regulation of licensed investment managers in France, Germany, Ireland, Luxembourg, the United Kingdom and the United States of America are broadly similar in effectiveness for the purposes of this provision.
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- (4) If the Operator of a Passport Fund delegates the function of making discretionary investment decisions, the Operator must ensure that at all times each of the qualifying delegates has 1 or more investment officers, each with at least either:
 - (a) a bachelor degree, or equivalent, or higher qualification in a relevant discipline, together with at least 3 years' experience within the previous 5 years as an officer or employee of an IOSCO financial services related business with responsibility for making or supervising discretionary investment decisions; or
 - (b) at least 5 years' experience within the previous 7 years as an officer or employee of an IOSCO financial services related business with responsibility for making or supervising discretionary investment decisions.
- (5) For this section:
investment officer in a qualifying delegate means a person who:
 - (a) is an officer or employee of the qualifying delegate; and
 - (b) is responsible, or is collectively responsible with other investment officers, for making or supervising discretionary investment decisions for the Passport Fund.

- (6) For this section, a reference to supervising discretionary investment decisions includes monitoring and evaluating on behalf of an entity, the performance of another entity that makes discretionary investment decisions as a delegate of the first entity, and being significantly involved in decisions about whether the second entity should remain as a delegate in light of its performance.

Part 4 Accountability

12 Reporting of breaches and changes

Reporting breaches and changes to Home Regulator

- (1) The Operator of a Passport Fund must notify the Home Regulator in writing within 7 days if it becomes aware that, without there being a breach of the Passport Rules, a limit set in the following rules has been exceeded for a period of 7 days without being remedied:
- (a) the rules in Division 6.3 (portfolio allocation); or
 - (b) the rules in Division 6.4 (limits on exposure); and
- (2) The Operator of a Passport Fund must notify the Home Regulator as soon as practicable and in any event within 7 days if it becomes aware of a breach of these Rules has occurred, or will occur in relation to the Passport Fund, and that breach:
- (a) might reasonably be regarded as significant including having regard to any other breaches; or
 - (b) when considered on its own or together with any related breach, adversely affects the value of the assets of the Passport Funds by more than 1%.

Explanatory note:	Subsection 12(2) imposes thresholds so that immaterial breaches of the Passport Rules are not required to be reported, for example a change to the reporting lines in the Operator's organisational arrangements that results in a delay of one day. Nonetheless, these breaches should not be considered in isolation. While individual breaches may be minor, when considered together with other breaches they can establish a pattern.
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Reporting breaches to Host Regulator

- (3) Subsection (4) applies to the Operator of a Passport Fund where the Host Economy Laws and Regulations of a particular Host Economy (the **relevant Host Economy**) apply to the Passport Fund.
- (4) The Operator of a Passport Fund must notify the Home Regulator and Host Regulator as soon as practicable and in any event within 7 days after it becomes aware of a breach of the Host Economy Laws and Regulations of the relevant Host Economy in relation to the Passport Fund, and that breach:
- (a) might reasonably be regarded as significant including having regard to any other breaches; or
 - (b) when considered on its own or together with any related breach, adversely affects as much of the value of the assets of the Passport Funds as is attributable to members of the Passport Fund in the relevant Host Economy by more than 1%.

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Reporting other changes

- (5) If an event listed in the table below occurs, the event must be notified to the Home Regulator and each Host Regulator by the entity listed in the table as soon as practicable and in any case within 7 days after it became aware of the event having occurred.

Event	Entity who must notify of the event
The Operator of a Passport Fund has disclosed to any person other than an associate of the Passport Fund or its Operator, that it intends to propose a change in the Operator.	The Operator of the Passport Fund.
The Operator of a Passport Fund is changed in accordance with the Home Economy Laws and Regulations.	The Operator of the Passport Fund.
The Operator of a Passport Fund has disclosed to any person other than an associate, of the Passport Fund or its Operator, that it intends to propose the Passport Fund be wound up.	The Operator of the Passport Fund.
A Passport Fund commences being wound up in accordance with the Home Economy Laws and Regulations.	The Operator of the Passport Fund.
A Passport Fund completes being wound up in accordance with the Home Economy Laws and Regulations.	The Operator of the Passport Fund.
The Operator of a Passport Fund has disclosed to any person other than an associate of the Passport Fund or its Operator that it intends to apply for the deregistration of the Passport Fund as a Regulated CIS and if this intention has not been notified that an application deregistration has been made.	The Operator of the Passport Fund.
A Regulated CIS is deregistered as a Passport Fund.	The Operator of the Regulated CIS.
A Regulated CIS that has been deregistered is no longer required to be operated in compliance with these Rules in accordance with Division 8.	The Operator of the former Regulated CIS.

13 Custody of Passport Fund assets

Legal responsibility for holding Passport Fund assets

- (1) For this section, the responsible holding party of the assets of a Passport Fund under the laws and regulations of the economy of a Participant is the entity who is responsible for the safekeeping of the assets of the Passport Fund, as shown in the following table (see also the table in section 4):

Home Economy of the Passport Fund	Responsible holding party
Australia	The Operator of the Passport Fund.
Korea	The trust business entity for the collective investment scheme under the Financial Investment Services and Capital Markets Act of Korea.
New Zealand	The licensed supervisor of the managed investment scheme under the <i>Financial Markets Conduct Act 2013</i> of New Zealand.
Philippines	A custodian which is a duly authorised local commercial bank of good repute (Investment Company Act Rule 35-1 [a][1][E]) authorised by the Bangko Sentral Ng Pilipinas to perform trust functions.
Singapore	An approved trustee under the Securities and Futures Act of Singapore of an authorised scheme.
Thailand	In case of a scheme established as a mutual fund, the mutual fund supervisor appointed for the mutual fund under the Securities and Exchange Act of Thailand. In case of a scheme established as a trust, the entity approved by the Securities and Exchange Commission under the Trust for Transactions in Capital Market to perform the custodial function of assets of the authorised scheme.

- (2) The function of holding Passport Fund assets may, subject to any limitation in the Home Economy Laws and Regulations, be delegated, or sub-delegated, only if the responsible holding party remains legally responsible for the safekeeping of Passport Fund's assets as if it held the assets itself.

Entities that hold Passport Fund assets

- (3) For this section, a custodian for a Passport Fund is an entity that holds assets of the Passport Fund.
- (4) The responsible holding party of a Passport Fund must ensure that each custodian for the Passport Fund:
- (a) meets one of the following criteria:

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- (i) the custodian is authorised in its place of business to carry on a business of holding assets on behalf of others; or
 - (ii) the asset holding is subject to regulatory requirements in the home economy or the custodian's place of business in relation to the asset holding; and
- (b) is not the Operator.

Note The effect of paragraph (b) in Australia is that the Operator must delegate the function to another entity.

Assets must be accounted for

- (5) A custodian of the Passport Fund must ensure that the assets of the Passport Fund which it holds are properly accounted for as the Passport Fund's assets and identifiable as such in the custodian's records.

Assets must be held separately or in a permitted omnibus account

- (6) The custodian of a Passport Fund must hold the Passport Fund assets:
- (a) separately from assets that are not assets of the Passport Fund; or
 - (b) in an omnibus account with the following characteristics:
 - (i) it is managed in accordance with good custodial practice where the account is held and in accordance with reasonable standards;
 - (ii) it is reconciled each business day in the place where the account is held;
 - (iii) it does not also hold any assets of the custodian other than contingent amounts; and
 - (iv) the custodian recovers any contingent amount as soon as practicable.
- (7) For subsection (6), an amount paid into an omnibus account by the custodian is a **contingent** amount if:
- (a) it is paid solely to prevent the continuation of a shortfall that occurred because of circumstances that were beyond the custodian's control or that was not intended by the custodian to arise; and
 - (b) the custodian will be entitled to recover the amount when the circumstances are rectified or addressed.
- (8) The custodian of a Passport Fund must ensure that there is separation between the functions of asset holding and investment such that activities that relate to asset holding are being performed by officers who are separate from, and able to act independently from, investment officers, for example:
- (a) no investment officer of the custodian is responsible for holding the assets of the Passport Fund; and
 - (b) no investment officer of the custodian directly supervises any other officer of the custodian who is responsible for holding the assets of the Passport Fund; and
 - (c) each officer of the custodian that is responsible for holding the assets of the Passport Fund is independent from each investment officer of the custodian.
- (9) For subsection (8), an **investment officer** of a custodian is an officer of the custodian whose responsibilities include investment decisions or trading decisions,

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whether in relation to the Passport Fund or otherwise, other than decisions that relate to:

- (a) deposit accounts; or
 - (b) currency transactions that are conducted for the purposes of facilitating purchase and sale of assets of the Passport Fund, or other payment obligations of the Passport Fund, or the redemption, issue, subscriptions, cancellation or repurchase of interests in the Passport Fund
- (10) Subsection (4)(b) does not apply to a custodian in relation to the following assets held on trust for the members of the Passport Fund, or, if the Passport Fund is a body corporate, as an asset of the Passport Fund, if it is subject to regulatory requirements in the Home Economy in relation to holding the assets:
- (a) deposits with an entity which is subject to prudential regulation in a principal place of business of the entity under the guidelines of the Basel Committee on Banking Supervision if:
 - i. the entity holds other assets of the Passport Fund under subsection (4); or;
 - ii. the Operator reasonably considers that holding the deposit taking facility by another person would raise unreasonable operational difficulties or be impracticable;
 - (b) assets held for operational purposes that it would not be reasonably practicable for an entity other than the Operator to hold; or
 - (c) a derivative and any contractual right for the payment of any balance owing to the Operator in relation to dealings in derivatives including margining those dealings through transactions in a deposit taking facility."

14 Independent oversight entity of a Passport Fund

- (1) For these Rules, the *independent oversight entity* of a Passport Fund in a Participant is the body shown in the following table:

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Home Economy of the Passport Fund	Independent oversight entity
Australia	The independent directors of the Operator or the compliance committee of the registered scheme as required under the <i>Corporations Act 2001</i> (Cth).
Korea	The trust business entity for the collective investment scheme under the Financial Investment Business and Capital Markets Act of Korea.
New Zealand	The licensed supervisor of the managed investment scheme under the Financial Markets Conduct Act of New Zealand.
Philippines	The independent directors of the investment company or the duly licensed trustee constituted as the independent oversight committee.
Singapore	An approved trustee under the Securities and Futures Act of Singapore of an authorised scheme.
Thailand	In case of a scheme established as a mutual fund, the mutual fund supervisor appointed for the mutual fund under the Securities and Exchange Act of Thailand. In case of a scheme established as a trust, the entity approved by the Securities and Exchange Commission under the Trust for Transactions in Capital Market Act to perform such oversight function over the trust.

- (2) The independent oversight entity must:
- (a) monitor the Operator for compliance with the constituent documents of the Passport Fund, and laws and regulations relating to the operation of the Passport Fund; and
 - (b) if the Operator is required by these Rules to report the non-compliance to a Passport Regulator but fails to do so—report the non-compliance to the Passport Regulator as soon as practicable but no later than 7 days after discovering the Operator’s failure.
- (3) The independent oversight entity must perform the functions listed in subsection (2) in the interests of the members of the Passport Fund.
- (4) The Operator must provide any assistance required by the independent oversight entity to perform its functions.

15 Compliance review

Annual compliance reviews must be conducted

- (1) The Operator of a Passport Fund must ensure that a compliance review of the operation of the Passport Fund that complies with this section is conducted in relation to each period for which it prepares, or is required to prepare, a financial statement (the *review period*).

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- (2) If the Home Regulator has notified the Operator of a Passport Fund and each Host Regulator that having regard to actions taken, or to be taken by the Home Regulator, to check compliance during the review period or on an ongoing basis, and, if applicable, reports to be provided by the independent oversight entity during the review period or on an ongoing basis, this section does not apply to the Passport Fund or its Operator for the review period or until revoked as the case may be, as set out in the notice.

Requirements for the reviewer

- (3) Subject to subsection (4), the compliance review for a Passport Fund registered in the economy of a Participant listed in the following table must be conducted by a reviewer that is an entity of the kind shown in the table:

Home Economy of the Passport Fund	Entity that can conduct compliance reviews
Australia	A registered company auditor, audit firm or authorised audit company under the <i>Corporations Act 2001</i> (Cth).
Korea	A trustee under the Financial Investment Services and Capital Markets Act of Korea.
New Zealand	A licenced auditor under the <i>Auditor Regulation Act 2011</i> .
Philippines	An accredited external auditor under Group A pursuant to the Securities Regulation Code, Rule 68.
Singapore	A public accountant who is registered or deemed to be registered under the Accountants Act of Singapore.
Thailand	An auditor as defined by the Securities and Exchange Commission.

- (4) The compliance review must not be conducted by:
- (a) the Operator; or
 - (b) a related party of the Operator.

Assistance must be given to the reviewer

- (5) Each of the following entities must do all things reasonably necessary to assist the conduct of the compliance review:
- (a) the Operator;
 - (b) any delegate of the Operator;
 - (c) any custodian of the Passport Fund;
 - (d) the responsible holding party; and
 - (e) the independent oversight entity.

Requirements applying where the review must be conducted by an auditor

- (6) The Operator of a Passport Fund must ensure that a reviewer is engaged for the Passport Fund for the purposes of this section at all times.
- (7) The compliance review must be conducted in accordance with standards acceptable to the Home Regulator.

Report of the compliance review

- (8) The reviewer must prepare a report of the compliance review addressed to the Operator, the independent oversight entity, the Home Regulator and each Host Regulator.
- (9) The report must state:
 - (a) whether any matter has come to the attention of the reviewer that causes the reviewer to believe that, or to believe that it is likely that, the Passport Fund was not operated in compliance with these Rules during the period covered by the compliance review in all respects that may be material to the persons to whom it is addressed;
 - (b) if so, details of the way in which the reviewer considers the Passport Fund during that period did not comply with, or is likely not to have complied with, these Rules; and
 - (c) information about how the review was conducted including the methods applied to gather information to have an appropriate basis for the statements in the report and form an opinion on compliance.
- (10) The Operator of a Passport Fund must, within 3 months after the end of the review period, provide a copy of the report to:
 - (a) the Home Regulator;
 - (b) each Host Regulator where the fund had, during the review period, members who became members of the Passport Fund following an application made in a Host Regulator's economy and each Host Regulator of each economy in which interests in the Passport Fund were offered during the period from the beginning of the review period to the time the reports are provided to the Home Regulator; and
 - (c) the independent oversight entity for the Passport Fund.

16 Financial reporting and auditing

- (1) The Operator of a Passport Fund must, in accordance with this section:
 - (a) prepare reports containing financial statements for the Passport Fund; and
 - (b) ensure that those financial statements are audited, and that an audit report is prepared; and
 - (c) lodge those reports with the Home Regulator and each Host Regulator.

Financial statements of a Passport Fund

- (2) The Operator must, at least annually, in accordance with the prevailing practice for the preparation of audited financial statements for Regulated CIS in the Home Economy, prepare a report containing the financial statements for the Passport Fund for the period covered by the report (the *review period*).

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- (3) The financial statements of a Passport Fund must be prepared in accordance with the financial reporting requirements applying to the Passport Fund.
- (4) For this section, the *financial reporting requirements* applying to a Passport Fund registered in a Participant are those shown in the following table:

Home Economy of the Passport Fund	Financial reporting requirements
Australia	Requirements imposed under Chapter 2M of the <i>Corporations Act 2001</i> (Cth) and the accounting standards made by the Australian Accounting Standards Board under section 334 of that Act.
Korea	The accounting standards under Article 240 of the Financial Investment Services and Capital Markets Act of Korea.
New Zealand	Requirements imposed under Part 7 of the <i>Financial Markets Conduct Act 2013</i> .
Philippines	The Financial reporting requirements and the Audit Requirements are those provided in Securities Regulation Code Rule 17.1 and SRC Rule 68.1, as amended.
Singapore	The relevant accounting standards made by the Accounting Standards Council under the Accounting Standards Act (Cap. 2B) and the Recommended Accounting Practices (or its equivalent) issued by the Council of the Institute of Singapore Chartered Accountants (or its successors).
Thailand	The accounting standards made by the Federation of Accounting Profession under the <i>Accounting Profession Act</i> (2004).

Audit of financial statements

- (5) The Operator of a Passport Fund must ensure that the financial statements of the Passport Fund are audited by a person (the *auditor*) who is permitted to audit the financial statements of a Regulated CIS in the Home Economy of the Passport Fund to satisfy the financial reporting requirements.
- (6) The auditor must:
- ensure that the audit is conducted in accordance with the audit requirements applying to the Passport Fund; and
 - prepare a report of the audit of the financial statements of the Passport Fund (the *audit report*).
- (7) For this section, the *audit requirements* applying to a Passport Fund registered in a Participant are those shown in the following table:

Home Economy of the Passport Fund	Audit requirements
Australia	Requirements imposed under Chapter 2M of the <i>Corporations Act 2001</i> (Cth), the auditing standards made by the Australian Auditing Standards Board under that Act.
Korea	The accounting standards under Article 240 of the Financial Investment Services and Capital Markets Act of Korea. The guidelines for accounting audit of collective investment property under Article 265(2) of Enforcement Decree of the Financial Investment Services and Capital Markets Act of Korea.
New Zealand	Requirements imposed under Part 7 of the <i>Financial Markets Conduct Act 2013</i> .
Philippines	Requirements under the Philippine Standards on Auditing.
Singapore	Singapore Standards on Auditing.
Thailand	The accounting standards made by the Federation of Accounting Profession under the <i>Accounting Profession Act</i> (2004).

Lodgement of reports

- (8) The Operator of a Passport Fund must, within 3 months after the end of the review period, lodge a copy of both:
- (a) the report containing those financial statements; and
 - (b) the audit report relating to those financial statements,
- with:
- (a) the Home Regulator; and
 - (b) each Host Regulator for an economy where the fund had, during the review period, members who became members of the Passport Fund following an application made in the Host Regulator's economy and each Host Regulator of each economy in which interests in the Passport Fund were offered during the period from the beginning of the review period to the time the reports are provided to the Home Regulator.

Part 5 Offers of a Passport Fund

17 Requirement of offer in Home Economy

The Operator of a Passport Fund must not offer interests in the fund in a Participant other than the Home Economy as a Passport Fund unless:

- (a) all of the following are satisfied when the interests are offered:

- (i) there is an ongoing offer of interests in the Passport Fund in the Home Economy;
 - (ii) the offer of interest in the Passport Fund is subject to the Home Economy Laws and Regulations that would normally apply to an offer of interests in a Regulated CIS to the general public;
 - (iii) the offer is bona fide and does not exclude subscription by retail investors resident in the Home Economy; or
- (b) all of the following are satisfied when the interests are offered:
- (i) there is an ongoing offer of interests in a sub fund which forms part of the same Regulated CIS as the Passport Fund;
 - (ii) the offer of interest in that sub fund is subject to the Home Economy Laws and Regulations that would normally apply to an offer of interests in a Regulated CIS to the general public;
 - (iii) the offer is bona fide and does not exclude subscription by retail investors resident in the Home Economy; or
- (c) both of the following were satisfied at the time the Operator seeks to offer interests in the Passport Fund in the Participant as a Passport Fund;
- (i) at least 30% of the value of interests in CISs for the operation of which the Operator is responsible are held by members of those CISs resident in the Home Economy; and
 - (ii) the Operator has provided a disclosure document to the Home Regulator that meets the requirements for a disclosure document for an offer of interests in the Passport Fund that would normally apply to an offer of interests in a Regulated CIS to the general public in the Home Economy.

Explanatory note:

The Working Group remains of the view that there should be a nexus between the Operator's business activities and the Home Economy. This is to give public confidence that the Home Regulator can review regulated disclosure for the scheme and that there is local connection supporting the Home Regulator in monitoring the compliance of the fund. However, the Working Group considers that this test could be met using one of three alternate tests set out in section 17.

Part 6 Passport Fund investments

Division 6.1 Operational goods and services

18 Part does not apply to operational goods and services

Goods and services acquired by a Passport Fund for operational reasons, rather than for investment purposes, are not considered assets of the Passport Fund for this Part. Nothing in this Part prevents a Passport Fund from acquiring and holding goods or services for operational reasons.

Division 6.2 Permitted investments

19 Permitted assets and arrangements

- (1) A Passport Fund must not acquire assets, or enter into a derivative or securities lending arrangements, other than in accordance with this Part.
- (2) Subject to this Part, a Passport Fund may only acquire assets of the following kinds:
 - (a) currency;
 - (b) deposits;
 - (c) depository receipts over gold;
 - (d) transferable securities; and
 - (e) money market instruments.
- (3) Subject to this Part, a Passport Fund may enter into derivative and securities lending arrangements.

20 Jurisdiction requirement for assets

A Passport Fund may hold an asset listed in section 23(2) only if it is issued in an IOSCO jurisdiction.

21 Requirements for deposits

- (1) A Passport Fund may make a deposit only with a deposit-taking institution that is regulated under the guidelines of the Basel Committee on Banking Supervision.
- (2) A Passport Fund may make a deposit only if:
 - (a) the amount deposited can be withdrawn under the terms of the deposit on no more than 31 days' notice; and
 - (b) it is not subject to loss of interest or to penalty if the amount is withdrawn more than 12 months after it was deposited.

22 Meaning of *depository receipts over gold*

For these Rules, *depository receipts over gold* means an acknowledgement, from an entity that is authorised in its principal place of business to carry on banking business (the issuer), that the issuer holds gold:

- (a) of a specified amount that is allocated to the receipt holder and that will be made available at the holder's direction; or
- (b) which is sufficient in amount and available to enable performance of an obligation undertaken by the issuer under the acknowledgement to make available at the holder's direction a specified amount of gold and any other obligations of the issuer in relation to gold held by the issuer.

23 Requirements for transferable securities

- (1) For these Rules, each of the following is a *transferable security* only if title to the security can be transferred from one party to another or redeemed from the issuer:
 - (a) a share or stock in a body corporate;

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- (b) a bond or other form of debt security (other than a money market instrument);
 - (c) an interest in a CIS;
 - (d) any interest in an asset covered by paragraph (a), (b) or (c); and
 - (e) a right to be issued an asset covered by subsection (1)(a), (b), (c) or (d) on payment of a specified amount for that asset that is granted by the issuer of that asset.
- (2) A Passport Fund must not acquire a transferable security if liability could arise from holding it under the terms of the security.

Note For example, a Passport Fund must not acquire a transferable security that is partly paid.

24 Requirements for money market instruments

A Passport Fund may acquire a money market instrument only if the Operator reasonably believes the following conditions are satisfied:

- (a) the instrument:
 - (i) has maturity at issuance or a residual maturity of up to and including 397 days; or
 - (ii) may be reasonably expected to undergo regular yield adjustments that are in line with money market conditions at least once every 397 days; and
- (b) on any business day in the economy in which it is acquired by the Passport Funds, the instrument:
 - (i) can be reliably valued; and
 - (ii) can be closed out or sold for that value.

25 Requirements for derivatives

- (1) A Passport Fund may enter into a derivative arrangement only if:
- (a) the underlying asset or index from which the value of the derivative is determined is one or more of the following:
 - (i) an asset that the Passport Fund may hold under subsection 19(1);
 - (ii) a rate of interest;
 - (iii) a rate of inflation on which a rate of interest is based;
 - (iv) an eligible index; and
 - (b) either the market price or the fair value of the derivative in the economy in which it is acquired by the Passport Fund can readily be determined, in accordance with Division 7.2; and
 - (c) other than in exceptional circumstances, the derivative can be closed out or sold for that value, in that economy, on any business day in the economy of the counterparty or if the derivative is traded on a financial market, when the financial market is open for trading of derivatives.

Explanatory note:	References to a financial market throughout the Passport Rules would cover a regulated non-exchange market, for example, a facility under which dealers place orders common in bond markets.
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- (2) Subject to subsection (3), a Passport Fund must not enter into a derivative arrangement if a decrease in the value of the underlying asset or index from which the value of the derivative is determined will result in an increase of the value of the derivative to the Passport Fund.
- (3) Subsection (2) does not apply to a derivative that is used in:
 - (a) a relevant netting arrangement; or
 - (b) a relevant hedging arrangement.

Consultation Question 3: The Passport rules currently do not allow Passport funds to short sell, both synthetically and physically. Nevertheless, the Working Group acknowledges the importance of using financial derivative instruments for hedging and netting off existing exposure. Exceptions are therefore provided for a Passport fund to take a short position in derivatives that are subject to hedging or netting arrangements.

The Working Group notes this proposed Passport rules may be stricter than some existing cross border frameworks for retail CIS and is considering the conditions and what additional safeguards should be introduced to ensure short selling will not result in the Passport funds taking excessive risks.

The Working Group would like to seek industry input on whether physical or synthetic short selling should be restricted, and if so, what safeguards would be appropriate to mitigate risks associated with physical or synthetic short selling:

(1) Synthetic short selling – Are the current safeguards relating to derivatives, such as global exposure limit (section 39), cover rule (section 42), quality of counterparty to derivatives (section 27), and general requirements for derivatives (section 25) sufficient to mitigate the risk of synthetic short selling? What other safeguards should be considered?

(2) Physical short selling – Some existing cross border frameworks for retail CIS jurisdictions do not currently permit retail CIS to carry out physical short selling, citing increased settlement risk involved in and absence of requirements governing such transactions. Should Passport Funds be permitted to engage in securities borrowing and physical short selling transactions? Accordingly, what requirements and safeguards should be introduced to ensure that Passport Funds minimise the risks arising from securities borrowing and physical short selling transactions, if such transactions were to be allowed? For example, what are some of the safeguards available to ensure that a Passport Fund's short positions in such transactions are fully covered at all times?

Meaning of 'derivative'

- (3) For these Rules, a **derivative** is an arrangement between an entity and another party (the **counterparty** for the derivative):
 - (a) where the arrangement is not:
 - (i) currency;
 - (ii) a deposit;
 - (iii) a loan of moneys or securities;
 - (iv) a transferable security;

- (v) a money market instrument; or
- (vi) a depository receipt over gold; and
- (b) under the arrangement:
 - (i) one party must, or may be required to, provide consideration of a particular kind to the other on a future day;
 - (ii) the consideration or, if arrangements of that kind are commonly sold or closed out before performance, the value of the arrangement on sale or close out, is ultimately determined by or modified by reference (wholly or in part) to a variable;
 - (iii) no substantial part of the consideration provided by either party under the contract is the provision of services;
 - (iv) the consideration is not the provision of goods that the fund is to use for operational purposes; and
 - (v) no party will be under an obligation to deliver an asset that is not a permitted asset under subsection 19(2).

26 Requirements for embedded derivatives

- (1) A Passport Fund may acquire a transferable security or money market instrument that embeds a derivative only if the embedded derivative satisfies:
- (a) section 25; and
 - (b) section 27 where the counterparty risk of the embedded derivative is or may be transferred to the Passport Fund;
- as if the Passport Fund were a direct party to the embedded derivative.

Meaning of 'embeds' and 'embedded derivative'

- (2) For these Rules, a transferable security or money market instrument in question ***embeds a derivative***:
- (a) if it includes a component (the ***embedded derivative***) that:
 - (i) results in some or all of the cash flows that would otherwise be payable under the transferable security or money market instrument which functions as the host contract to be modified by reference (wholly or in part) to a variable other than, for shares or stock, the discretion of the corporation as to payment of dividends or repayment of capital or amounts payable on its winding up;
 - (ii) has benefits and risks that are not closely related to economic characteristics of the transferable security or money market instrument which functions as the host contract;
 - (iii) has a significant impact on the risks in holding, and the price of, the transferable security or money market instrument in question; and
 - (iv) is not transferable independently of the transferable security or money market instrument or is not treated by the Passport Fund as a separate asset; or
 - (b) if it would be a derivative but for being a transferable security or a money market instrument, and the terms were designed to meet the specific needs of a Passport Fund.

27 Counterparties to derivatives

- (1) A Passport Fund may enter into a derivative arrangement that is to be cleared through a central clearing counterparty only if it is an assessed central clearing counterparty.
- (2) A Passport Fund may enter into a derivative arrangement that is not cleared through a central clearing counterparty only if:
 - (a) the counterparty to the derivative:
 - (i) is subject to prudential supervision broadly under the guidelines of the Basel Committee on Banking Supervision by a financial supervisory authority in a principal place of business of the counterparty; or
 - (ii) is both:
 - (A) regulated by a member or associate member of IOSCO; and
 - (B) subject to obligations in relation to holding financial resources and having adequate arrangements to manage risk; and
 - (b) where the counterparty to the derivative is a related party to the Operator—there are adequate arrangements in place to manage conflicts of interest.
- (3) For these Rules, a central clearing counterparty to a derivative is an ***assessed central clearing counterparty*** if:
 - (a) it is regulated as a central clearing counterparty in an economy that is:
 - (i) a Participant; or
 - (ii) a member of the OECD; or
 - (b) all of the following conditions are satisfied:
 - (i) it is regulated as a central clearing counterparty in an IOSCO jurisdiction;
 - (i) the Operator of the Passport Fund believes on reasonable grounds, having regard to independent sources of information, that there is very low risk of the central clearing counterparty defaulting in any of its obligations over the subsequent 5 year period; and
 - (ii) the Operator of the Passport Fund records in writing its reasons for holding that belief.

28 Counterparties and collateral for securities lending arrangements

- (1) For these Rules, a ***securities lending arrangement*** is an arrangement under which an asset of the Passport Fund is transferred to another party and there is an obligation on that party to transfer that asset, or an equivalent asset, back to the Passport Fund.
- (2) A Passport Fund may enter into a securities lending arrangement only if:
 - (a) the counterparty to the transaction:
 - (i) is subject to prudential supervision broadly under the guidelines of the Basel Committee on Banking Supervision by a financial supervisory authority in a principal place of business of that counterparty; or

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- (ii) is both:
 - (A) regulated by a regulatory authority that is a member or associate member of IOSCO; and
 - (B) subject to obligations relating to holding financial resources and having adequate arrangements to manage risk; and
 - (b) there is an agreement between the Passport Fund and the counterparty to the transaction that provides that:
 - (i) the counterparty will provide to the Passport Fund collateral, which will be acquired as an asset of the fund free of any encumbrance, that exceeds the value of the asset lent by the Passport Fund under the transaction; and
 - (ii) if the current value on any business day of the collateral where all the collateral was tendered in cash does not exceed the value of the asset to be transferred to the Passport Fund, or if the collateral tendered included a money market instrument—exceeds 105% of the market value of the asset on that business day, the counterparty must provide additional collateral to the Passport Fund no later than the close of the next business day in the economy of the counterparty;
 - (c) where the counterparty to the transaction is a related party to the Operator—there are adequate arrangements in place to manage potential conflicts of interest; and
 - (d) the Operator has assessed in writing the risk, from entering into the arrangement or of entering into arrangements that include the arrangement, having regard to the counterparty, the collateral, the terms of the arrangement and any other relevant matter, is very low.
- (3) Any collateral relied on by the Passport Fund to satisfy subsection (2) must be:
 - (a) cash; or
 - (b) money market instruments:
 - (i) that do not embed derivatives;
 - (ii) that have been assessed by the Operator of the Passport Fund as having acceptable risk; and
 - (iii) whose value exceeds 105% of the amount of cash collateral that would otherwise be required to satisfy subsection (2).
- (4) The Passport Fund must not sell, reinvest, or encumber securities lending collateral other than as permitted by this section or following default in compliance by the counterparty to the securities lending arrangement.
- (5) The Passport Fund may reinvest securities lending collateral provided as cash in money market instruments if:
 - (a) the money market instruments have been assessed by the Operator of the Passport Fund as having acceptable risk; and
 - (b) the value of the money market instruments that the Passport Fund holds exceeds 105% of the amount of the securities transferred under the securities lending arrangement.

- (6) For the avoidance of doubt, collaterals posted in a derivative or securities lending arrangement would be deemed as assets acquired by the Passport Fund for the requirements under Division 6.3.

Explanatory note: For meaning of acceptable risk (used in subparagraph 28(3)(b)(ii) and 28(5)(a)), please see Dictionary in section 55.

Division 6.3 Restrictions on portfolio allocation

29 Exceeding limits in this Part

- (1) A Passport fund must not acquire an asset or enter into a derivative or securities lending arrangement if it would result in a limit in this Part being exceeded or exceeded to a greater extent.
- (2) A Passport Fund that exceeds a limit in this Part must cease to exceed the limit as soon as practicable but no later than three months from the date the limit was exceeded.
- (3) The period in subsection (2) may be extended for a period or further period of no more than one month by notice in writing to the Operator by the independent oversight entity if the Operator satisfies the independent oversight entity that it is in the best interests of the members of the Passport Fund for extension.
- (4) A Passport Fund does not breach a rule in this Part if it exceeds a limit otherwise than by the acquisition of an asset or the entry into a derivative or securities lending arrangement and it complies with this section.

Note See also the reporting requirements under section 12.

30 Single entity limit

Explanatory note: Section 30 should be read in conjunction with paragraph 50 of the Feedback Statement.

- (1) No more than 5% after considering any reduction in risk due to offsetting exposures or the value disregarding the offsetting effects of derivatives, if higher, of the adjusted value of the assets of a Passport Fund may be held in assets or arrangements that:
- (a) relate to the same entity, that is not an entity that is an assessed central clearing party or subject to prudential supervision broadly under the guidelines of the Basel Committee on Banking Supervision by a financial supervisory authority in a principal place of business of the counterparty; and
 - (b) are of any one or more of the following types:
 - (i) transferable securities other than:
 - (A) interests in financial asset regulated CISs or UCITS; and
 - (B) risk-assessed government securities;
 - (ii) money market instruments other than risk-assessed government securities;
 - (iv) securities lending arrangements.

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Consultation question 4: Should the single entity limit be 10% in all cases, as opposed to the graduated approach as drafted under section 30? Would this significantly reduce the extent to which diversification is used in Passport Funds to reduce risk? Does the wording in the text give rise to practical problems?

- (2) No more than 15%, after considering any reduction in risk due to offsetting exposures or the value disregarding the offsetting effects of derivatives, if higher, of the adjusted value of the assets of a Passport Fund may be held in assets or arrangements that:
- (a) relate to the same entity that is subject to prudential supervision broadly under the guidelines of the Basel Committee on Banking Supervision by a financial supervisory authority in that counterparty's principal place of business; and
 - (b) are of any one or more of the types mentioned in paragraph (1)(b):

Consultation question 5: The Working Group is seeking feedback on whether the proposal in subsection 30(2) to increase the single entity limit to 15% for banks regulated under Basel Guidelines is preferable to having a separate limit for derivatives from other forms of counterparty exposure.

- (3) No more than 20%, after considering any reduction in risk due to offsetting exposures of the adjusted value of the assets of a Passport Fund may be held in assets that:
- (a) relate to the same entity; and
 - (b) are of any one or more of the following types:
 - (i) the types mentioned in paragraph (1)(b);
 - (ii) deposits.

Explanatory note: A Passport Fund will need to comply with the requirements under both subsections 30(2) and (3). For example, if a Passport Fund invests 15% and 20% of the adjusted value of its assets in money market instruments and deposits with the same bank respectively, while it will comply with subsection (2) which does not include deposits, the Passport Fund will exceed the limit for the purposes of subsection 30(3) because the adjusted value referred to in subparagraphs 30(3)(a) and (b) will total 35%.

- (4) No more than 35%, after considering any reduction in risk due to offsetting exposures the value disregarding the offsetting effects of derivatives, if higher, of the adjusted value of the assets of a Passport Fund may be held in assets that are risk-assessed government securities relating to the same government entity.
- (5) For this section, an asset or arrangement *relates* to an entity if the asset is of a type listed in the following table and has the connection with the entity shown:

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Item	This type of asset or arrangement...	...relates to the entity if:
1	transferable security	it is issued or guaranteed by the entity
2	money market instrument	it is issued or guaranteed by the entity
3a	derivative the price or value of which depends on the price of a transferable security or money market instrument as the reference asset; or	the reference asset is issued or guaranteed by the entity
3b	asset that embeds such a derivative	
4a	derivative whose counterparty is not an assessed central clearing counterparty; or	the entity is the counterparty
4b	asset that embeds such a derivative, if the counterparty risk is, or may be, transferred to the Fund	
5	securities lending arrangement	the entity is the counterparty
6	Deposit	is with the entity

Note An asset may relate to more than one entity. It must be counted for purposes of the application of subsections (1) to (4) to each of those entities.

Meaning of ‘government securities’

(6) For this section, an asset is a **government security** if:

- (a) the asset is:
 - (i) a transferable security other than an interest in a financial asset Regulated CIS; or
 - (ii) a money market instrument; and
- (b) the entity to which it relates is:
 - (i) the government of an economy;
 - (ii) a central bank; or
 - (iii) a supranational organisation.

Meaning of ‘risk-assessed government security’

(7) For these Rules, a government security is a **risk-assessed government security** if the Operator has assessed the holding as having an acceptable risk within the period of one month before the last acquisition of an asset or arrangement in the holding.

5% Single Entity Limit – permitted increase

(8) The maximum holding of assets or arrangements set out in subsection (1) is 10% of the adjusted value of the assets of Passport Fund, after considering any reduction in risk due to offsetting exposure or the amount disregarding the offsetting effects of derivatives if higher, for the relevant assets or arrangements if:

- (a) the relevant assets or arrangements have been assessed as having an acceptable risk within a period of no more than one month before the last acquisition of the asset in holding by the Operator; or

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- (b) the total value of the assets and arrangements held or entered into by the Passport Fund which exceeds the 5% single entity limit, other than where the assets or arrangements that have been assessed as having an acceptable risk within the last month previous by the Operator, does not exceed 40% of the adjusted value of the assets of the Passport Fund.

Explanatory note: For meaning of acceptable risk (used in subsection 30(7) and 30(8)), please see Dictionary in section 55.

Consultation question 6: Should the acceptable risk assessment apply even if the total of holdings that exceed the limit in subsection 30(1) was less than 40%? Would this significantly reduce the risk of such exposures? What, if any, costs of practical problems would arise?

31 Group limit

- (1) No more than 20%, after considering any reduction in risk due to offsetting exposure or the value disregarding the offsetting effects of derivatives, if higher, of the adjusted value of the assets of a Passport Fund may be held in assets that:
- (a) relate to the same group of entities; and
 - (b) are of any one or more the following types:
 - (i) the types mentioned in paragraph 30(1)(b); and
 - (ii) deposits.

Consultation question 7: For the entity limits (subsection 30(1), 30(2), 30(4), 30(8) and 31(1)), the Working Group has taken the approach to disregard the offsetting effects of derivatives as this is a more conservative approach. Would this be unduly restrictive for industry?

Meaning of 'relate' to group of entities

- (2) For this section:
- (a) two entities are **linked** if one entity is the controller of the other; and
 - (b) two entities are also **linked** if both entities are linked to a third entity; and
 - (c) a set of entities forms a **group of entities** if each entity in the set is linked to each other entity. (3) For this section, an asset **relates** to a group of entities if:
 - (i) the asset is not a government security; and
 - (ii) the asset is of a type listed in the following table and has the connection with a group of entities shown:

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Item	This type of asset...	...relates to the group of entities if:
1	transferable security	it is issued or guaranteed by an entity that is in the group of entities
2	liquid debt instrument	it is issued or guaranteed by an entity that is in the group of entities
3a 3b	derivative the price or value of which depends on the price of a transferable security or money market instrument as the reference asset; or asset that embeds such a derivative	the reference asset is issued or guaranteed by an entity that is in the group of entities
4a 4b	derivative whose counterparty is not an assessed central clearing counterparty; or asset that embeds such a derivative, if the counterparty risk is, or may be, transferred to the Fund	the counterparty is in the group of entities
5	securities lending arrangement	the counterparty is in the group of entities
6	deposit	is with an entity that is in the group of entities

32 Valuation of derivatives and securities lending arrangements

- (1) For sections 30 and 31 the value of a derivative arrangement as it relates to an entity is assessed as follows:
- (a) if it relates to the entity in the manner described in item 3a and 3b of the tables in subsection 30(5) or 31(2), the value is assessed in accordance with Appendix B and may be a negative value in case of a permitted short exposure; or
 - (b) if it relates to the entity in the manner described in item 4a and 4b of the tables, the value is assessed in accordance with Appendix A and may be determined:
 - (i) after netting off any liability of the Passport Fund to the entity where there is a netting arrangement where:
 - (A) the Passport Fund has a netting arrangement with its counterparty which creates a single legal obligation, covering all included transactions, such that, in the event of the counterparty's failure to perform owing to default, bankruptcy, liquidation or any other similar circumstance, the Passport Fund would have a claim to receive or an obligation to pay only the net sum of the transactions subject to the netting arrangement; and

- (B) the Operator is reasonably satisfied that the netting arrangement is legally effective under the law of each of the law of the jurisdiction in which the counterparty is incorporated and, if a foreign branch of an entity is involved, also under the law of the jurisdiction in which the branch is located the law that governs the individual included transactions and the law that governs the netting agreement, and
- (ii) after deducting the market value of any collateral held by the Passport Fund under the arrangement, which is held by the Passport Fund as an asset of the fund and without encumbrance that it:
 - (A) cash; or
 - (B) money market instruments that have been assessed by the Operator of the Passport Fund as having acceptable risk.

Explanatory note:	For meaning of acceptable risk (used in paragraph 32(b)(ii)), please see Dictionary in section 55.
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33 Application of certain restrictions to index funds and benchmark funds

- (1) This section applies to a Passport Fund that is an index fund or a benchmark fund.
- (2) If the assets of the Passport Fund or the underlying assets of the derivatives of the Passport Fund are constituents of the index then the limitation on the exposure of the fund to the entity, or group of entities, to which the asset or assets relate is the higher of:
 - (a) the percentage set out in section 30 for the respective types of asset or assets (5%, 10%, 20% or 35%); and
 - (b) the lower of:
 - (i) the percentage of the index that the asset or assets represent as constituents, plus 2%; and
 - (ii) 25%.

34 Restrictions on portfolio allocation—non-Passport Financial Asset Regulated CISs and UCITS

- (1) No more than 10% of the adjusted value of the assets of a Passport Fund may be held in any Financial Asset Regulated CIS or sub-fund of Financial Asset Regulated CIS that is not a Passport Fund.
- (2) No more than 10% of the adjusted value of the assets of a Passport Fund may be held in any individual UCITS fund or compartment of a UCITS fund.
- (3) No more than 20% of the value of the assets of a Passport Fund may be held in UCITS funds.
- (4) No more than 30% of the value of the assets of a Passport Fund may be held in assets that are:
 - (a) Financial Asset Regulated CISs that are not Passport Funds; or
 - (b) UCITS funds.

35 **Restrictions on portfolio allocation—Limit on unquoted transferable securities**

No more than 10% of the adjusted value of the assets of a Passport Fund may be held in unquoted transferable securities other than Financial Asset Regulated CISs and UCITS funds.

36 **Restrictions on portfolio allocation—Limit on investments conferring significant management influence**

- (1) A Passport Fund must not hold a legal or equitable interest in votable transferable securities accounting for more than 20% of the voting rights in that entity when added to any voting rights held by any of the Passport Fund's related parties of which it is aware or has reason to believe are held.
- (2) For this section, *votable transferable securities* of an entity means transferable securities that:
 - (a) relate to the entity; and
 - (b) carry voting rights in the entity that may be cast on a resolution at a meeting of members of the entity generally or that are otherwise able to be voted in determining the directors of the entity.

37 **Limit on share of transferable securities or money market instruments on issue**

- (1) A Passport Fund must not hold more than 10% of the non-voting securities of an entity.
- (2) A Passport Fund must not hold more than 10% of the debt securities of an entity.
- (3) A Passport Fund must not hold more than 10% of the money market instruments for which an entity is, or may be, liable.

38 **Limit on depository receipts over gold**

No more than 25% of the adjusted value of the assets of a Passport Fund may be held in depository receipts over gold.

Division 6.4 Limits on exposures

39 **Derivative and securities lending arrangements—global exposure limit**

- (1) The global exposure of a Passport Fund to derivatives, securities referred to in paragraph 23(1)(e) and securities lending arrangements must not be more than:
 - (a) 100% of the adjusted value of the assets of a Passport Fund that:
 - (i) is an index fund; and
 - (ii) uses derivatives traded on a financial market regulated by an ordinary or associate member of IOSCO for the purposes of index replication, where derivatives are used predominantly to reflect the returns on the index; or
 - (b) 20% of the adjusted value of the assets of the Passport Fund otherwise.

- (2) For this section, the *global exposure* of a Passport Fund to derivatives, securities referred to in paragraph 23(1)(e) and securities lending arrangements is the sum of the following amounts:
- (a) the sum of the absolute values (calculated according to Appendix B) of the exposures of each derivative or security referred to in paragraph 23(1)(e) held by the Passport Fund that is not involved in relevant netting arrangements or relevant hedging arrangements;
 - (b) the sum of the absolute values (calculated according to Appendix B) of the net exposures of each derivative entered into by the Passport Fund that is involved in relevant netting arrangements or relevant hedging arrangements, after taking into account those arrangements.
 - (c) the value of collateral received in derivative and securities lending arrangements which are reinvested other than in a deposit account that can be withdrawn without prior notice during business hours;
 - (d) if the Passport Fund holds any transferable security or money market instrument that embeds a derivative—the sum of the values of the exposures of the embedded derivatives calculated as if the derivative were held as a separate asset.

40 Netting and hedging arrangements

- (1) For these rules, a *relevant netting arrangement* is the netting of positions between:
- (a) derivatives with the same underlying assets or index (disregarding any difference in the maturity dates of the derivatives); or
 - (b) derivatives and the assets to which the derivative relates; or
 - (c) derivatives and all of the assets that are components of the relevant underlying index to which the derivatives relate that are held by the fund in the proportions that each of those assets are weighted in the index.
- (2) For the rules, a *relevant hedging arrangement* is any holding of a derivative that:
- (a) the Operator of the Passport Fund reasonably expects will reduce either:
 - (i) both of the following types of risks:
 - (A) the general market risk for a class of assets held by the Passport Fund; and
 - (B) specific risks arising from holding assets in that class; or
 - (ii) the risk of receiving application moneys or having to pay redemption in a currency that differs from that in which the assets of the fund are denominated;
 - (b) the Operator of the Passport Fund concludes with the sole purpose of offsetting those risks; and
 - (c) does not provide an offsetting exposure that is greater than 105% of the exposure at the point of entering into the arrangement.
- (3) For these Rules, the net exposure of a relevant netting or hedging arrangement is determined by calculating the net value of the exposures of the derivatives and assets to which the arrangements applies, using where applicable Appendix B and the exposures under any holding of the assets to which the arrangements applies.

- (4) The Operator of a Passport Fund must document the reasons on which any expectations referred to in subsections (2) are based.

41 Securities lending limit

No more than 50% of the adjusted value of the assets of a Passport Fund may be held in assets that are transferred under securities lending arrangements.

42 Derivative—covering exposures

- (1) If a Passport Fund enters into a derivative arrangement that gives rise, or may give rise, to a future commitment of the Passport Fund, the Passport Fund must hold at all times assets that the Operator of the Passport Fund reasonably believes will be available and able to be converted into sufficient assets:
- (a) in the case of a derivative that will, or may, be cash-settled—to enter an offsetting derivative so as to eliminate the exposure or have the counterparty to the derivative agree to terminate it; or
 - (b) in the case of a derivative that requires, or may require, physical delivery of the underlying asset—to be delivered as required to meet the actual or potential delivery obligation.

Division 6.5 Other restrictions

43 Prohibition on provision of loans, guarantees and underwriting

- (1) A Passport Fund must not lend money.
- (2) For subsection (1), a Passport Fund does not lend money if it holds a deposit as permitted under Division 6.2.
- (3) A Passport Fund must not act as guarantor for another person or entity.
- (4) A Passport Fund must not underwrite securities.
- (5) For this section, a Passport Fund *underwrites* securities if it agrees to acquire securities if they are not acquired by another person under an offer or to ensure a certain amount is raised from an offer.

44 Borrowing

- (1) A Passport Fund may borrow only if all of the following conditions are satisfied:
- (a) the total amount of borrowings of the Passport Fund does not exceed 10% of the adjusted value of the Passport Fund assets at the time of borrowing;
 - (b) the purpose of the borrowing is:
 - (i) to enable payment of redemption requests that:
 - (A) have been made; or
 - (B) are reasonably expected to be made; or
 - (ii) to enable payment of expenses properly payable by the Passport Fund other than:
 - (A) fees payable from the Fund to an Operator; or

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- (B) fees payable from the Fund to the independent oversight entity; or
 - (C) expenses associated with making an additional investment;
 - (c) there is a material risk that, without the borrowing, the Passport Fund will be unable to:
 - (i) meet redemption requests; or
 - (ii) pay expenses of the kind mentioned in subparagraph (1)(b)(ii) above;
 - (d) the borrowing is in the form of a trade credit, loan or overdraft from a financial institution licensed or regulated in the institution's principal place of business;
 - (e) the Passport Fund intends to repay the amount:
 - (i) in full in less than 31 days; and
 - (ii) without relying on other borrowings or financed amounts;
 - (f) the Passport Fund has documented cash flow projections prepared on reasonable assumptions that show that the amount will be repaid within that period.
- (2) Any amount payable to the Passport Fund by the lender is not taken to reduce the amount borrowed.
- (3) A Passport Fund must not enter into a securities lending arrangement for the purpose of acquiring any collateral provided to the Passport Fund.

Explanatory note:	A securities lending arrangement entered into for the purpose of acquiring any collateral for the Passport Fund will be construed as a borrowing transaction, and is, therefore, prohibited.
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45 Short-selling prohibited

- (1) A Passport Fund must not sell a Passport Fund asset unless, at the time of the sale:
- (a) the Passport Fund has a presently exercisable and unconditional right to give title to the asset to the buyer (a *transferable title*); or
 - (b) the Passport Fund has an agreement to buy the asset to be sold that:
 - (i) will enable the Passport Fund to acquire a transferable title to the asset before it is to be transferred; and
 - (ii) is conditional only on:
 - (A) payment of the consideration; or
 - (B) the exercise of an option on the part of the Passport Fund; or
 - (C) receipt of the proper instrument of transfer or receipt of the title documents.
- (2) For subsection (1), a transferable title to an asset, or an agreement to buy an asset that meets the conditions in subsection (1)(b), may only support one sale of the asset.

46 Liability of members

- (1) A Passport Fund must ensure that no member of the Passport Fund has a monetary liability to the Passport Fund in that person's capacity as a member of the Passport Fund.

47 Performance fees

- (1) A Passport Fund or its Operator must not permit a fee to be paid in relation to the Passport Fund based on any returns of the Passport Fund or increase in the value of any assets of the Passport Fund relative to a measure, unless:
 - (a) taking into account the arrangements to manage risk of the Passport Fund, the basis for the fees charged does not result in excessive risks being taken by the Operator in relation to the Passport Fund, or that the Passport Fund's investment objectives will not be followed, to obtain or increase fees;
 - (b) the calculation of the fees is verified by the Operator as consistent with the agreed basis for the fee and can be verified by the independent oversight entity; and
 - (c) the independent oversight entity has during the previous 13 months stated in writing to the Operator that the independent oversight entity has reason to believe any fees payable in relation to the Passport Fund will comply with written policies and procedures for fees of the Operator for the Passport Fund designed to ensure compliance with subsection (1)(a) and (1)(b).

Consultation question 8: Would the proposed Passport Rules on the charging of performance fees be unduly burdensome? What impact, if any, would this have on current commercial arrangements?.

Part 7 Redemption and valuation for pricing

Division 7.1 Redemption

48 Rights to redemptions—exchange traded Passport Funds

- (1) This section applies to a Passport Fund if:
 - (a) it is an index fund or benchmark fund; and
 - (b) it is traded on one or more relevant financial markets.
- (2) The Operator must take reasonable steps to ensure that each member of the Passport Fund is able to sell the member's interests in the fund on the relevant financial markets at a price that is not materially different from the net asset value per interest of the Passport Fund.
- (3) Subject to this Division, a member of the Passport Fund may request a redemption of the members' interests under section 49 if trading of the interests has been suspended on all the relevant financial markets for 5 consecutive days on which one or more of the financial markets is open for business (not counting days on which the redemptions of interests in the Passport Fund are suspended under section 51).
- (4) Subsection (3) does not apply to a Passport Fund if the Regulated CIS constituting it became a Regulated CIS or a sub fund of a Regulated CIS before the date on which this section is applied in the Home Economy.

- (5) For this section, a financial market is *relevant* to a Passport Fund if:
- (a) it is operated in a Participant; and
 - (b) under its operating rules, interests in the Passport Fund are admitted, and remain admitted, to trading status.

49 Rights to redemptions—other Passport Funds

- (1) This section applies to a Passport Fund other than one to which section 48 applies.
- (2) A member of the Passport Fund may at any time request a redemption of the member's interests under section 50.
- (3) Subsection (2) does not apply if the Operator has suspended redemptions in accordance with section 51.

50 Processing redemption requests

- (1) When the Operator of a Passport Fund receives a request for redemption under section 48 or 49, the Operator must, within the redemption period, process the redemption request and pay the member at a price per interest (the *redemption price*) that is:
 - (a) the valuation entity's estimation of the net asset value per interest of the Passport Fund, taking into account any redemption fees or transaction costs associated with redemption that have been disclosed to the member before the request;; and
 - (b) calculated using a valuation of the assets of the Passport Fund that is conducted after the request for redemption is received from the member.
- (2) The *redemption period* for request for redemption ends 15 days after the request is received by the Operator, unless the Operator has notified any member that it will be a shorter period or there is a suspension permitted under section 51 or redemption is deferred under section 52.
- (3) If a notification by the Operator under subsection (2) is in effect, the Operator may not increase the redemption period without reasonable notice to members.
- (4) In the case of a request under section 48, the Operator may not charge a redemption fee that is more than reasonably proportionate to the fee charged to any person who is entitled, under an arrangement with the Operator, to redeem interests other than under section 48.
- (5) The Operator must give the member the option of having the redemption price paid out in the currency in which the member paid for its interests in the Passport Fund, subject to any reasonable costs based on a reasonable estimate of costs for any foreign exchange that the Operator considers reasonably necessary for the purpose.

51 Suspension of redemptions

Operator of a Passport Fund must suspend or restrict redemptions in certain circumstances

- (1) The Operator of a Passport Fund must suspend redemptions in the Passport Fund if it is directed to do so by the Home Regulator.
- (2) The Operator of a Passport Fund must suspend redemptions in the Passport Fund if the Passport Fund is in the process of being wound up.

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- (3) The Operator of a Passport Fund must suspend redemptions in the Passport Fund if:
- (a) the Operator considers that a suspension is in the best interests of members; and
 - (b) the Operator considers that a suspension is fair as between members; or
 - (c) either:
 - (i) the Operator considers that:
 - (A) a proportion of the assets of the Passport Fund is not able to be reliably valued; and
 - (B) that proportion is such that, in the reasonable opinion of the Operator, there is an unreasonable risk that the redemption price will contain an error; and
 - (C) the error in the redemption price is likely to affect the decision of members of the Passport Fund about whether or not to redeem their interests; or
 - (ii) the Operator reasonably expects that more than 20% of the assets of the Passport Fund could not be realised at or above the market value of the assets within the period for satisfying redemption requests.

Other Passport Funds must not otherwise suspend or restrict redemptions

- (4) The Operator of a Passport Fund must not suspend redemptions in circumstances other than those set out in subsections (1), (2), and (3).

Note: Funds to which section 48 applies (exchange-trade Passport Funds) are only required to provide redemptions in the circumstances set out in that section.

Consultation question 9: Would the proposed Passport Rules over suspension of redemptions be too restrictive? What impact, if any, would this have on current commercial arrangements?

52 Deferral of redemptions

- (1) This section applies in relation to a Passport Fund if, on a dealing day:
- (a) the redemption request is due for redemption; and
 - (b) any deferred redemption requests under subsections (5) and (6); together amount to more than 10% of the interests in the Passport Fund.
- (2) The Operator may decide to limit the interests that will be redeemed on the day to a proportion of the interests in the Passport Fund (the ***daily limit***) that is at least 10%.
- (3) The Operator must divide the requests into priority classes based on the days on which they were received, giving higher priority to requests received on earlier days.
- (4) The Operator must process the requests by priority class.
- (5) If redeeming all the requests in a priority class would take the interests redeemed on that day beyond the daily limit, the Operator must:
- (a) redeem the same proportion of each request in the priority class; and
 - (b) treat each request in the priority class as a ***deferred redemption request*** for the remainder of the interests requested, to be dealt with on the next dealing day.

(6) If the daily limit is filled before a priority class is reached, the Operator must treat the whole of each request in that priority class as a *deferred redemption request*, to be dealt with on the next dealing day.

(7) For this section:

dealing day, in relation to a Passport Fund, means a day on which the members of the Fund have a right to redeem their interests in the Fund including following a deferral under this section.

Division 7.2 Valuation of assets for pricing

53 Valuation of Passport Fund assets

(1) For this section, the *valuation entity* for a Passport Fund registered in a Participant is the entity shown in the following table:

Home Economy of the Passport Fund	Valuation entity
Australia	The Operator
Korea	The Bond Assessment Company registered with the Financial Services Commission under Article 263 of the Financial Investment Services and Capital Markets Act of Korea.
New Zealand	The Operator
Philippines	The Operator
Singapore	The manager of the collective investment scheme authorised by the Monetary Authority of Singapore under the Securities and Futures Act
Thailand	The Operator

(2) When calculating the value of the assets of the Passport Fund for pricing, the valuation entity must ensure that the valuation is calculated in accordance with this section.

(3) Subject to subsection (4), the value of a quoted asset of the Passport Fund is its market price.

(4) The value of an asset of the Passport Fund that is:

(a) an unquoted asset; or

(b) a quoted asset of a Passport Fund in relation to which the valuation entity is satisfied that the market price is either unavailable or does not reasonably represent the value of the asset;

is the fair value of that asset.

(5) The value of a derivative that is not regularly traded on a financial market must not be calculated in a way that relies solely on a valuation provided by the counterparty to the derivative.

Part 8 Effect of Deregistration

54 Effect of deregistration

- (1) A Regulated CIS or a sub fund of a Regulated CIS that has been deregistered as a Passport Fund must be operated in accordance with these Rules until the Regulated CIS or sub fund does not have any members who:
 - (a) became members:
 - (ii) when the deregistered fund was a Passport Fund; or
 - (iii) on the expectation that the fund would become a Passport Fund; and
 - (b) are not:
 - (i) the current Operator or any previous Operators; or
 - (ii) related parties of the entities listed in subparagraph (b)(i).
- (2) After a Regulated CIS or a sub fund of a Regulated CIS is deregistered, neither the Regulated CIS nor sub fund or its Operator may charge any fee on withdrawal of a member who satisfies subsection (1)(a) and (b).

Part 9 Dictionary

55 Definitions

For these Rules:

adjusted value of the assets: means the value of the assets of a Passport Fund less the value of any holding in a financial asset Regulated CIS, UCITS or Passport Fund.

assessed as having an acceptable risk: in relation to a holding of assets and arrangements by a Passport Fund means when the Operator has:

- (a) assessed the creditworthiness of the issuers, guarantors or counterparties of the assets or arrangements in accordance with written policies and procedures which include having regard to independent sources of information; and
- (b) assessed the risk for members of the Passport Fund of holding the proposed concentration of the assets given the creditworthiness of the issuers, guarantors or counterparties; and
- (c) concluded there was no disproportionate risk relative to the risks associated with the Passport Fund's investment strategy; and
- (d) documented the assessments and the reasons for the conclusion.

assessed central clearing counterparty: see section 27.

benchmark fund means a Passport Fund that has publicly disclosed that it has an investment strategy of seeking to achieve returns that meet or exceed an eligible index.

Collective Investment Scheme or ***CIS*** means a scheme with the following features:

- (a) at least two persons (***members***) contribute money or money's worth for the right to the benefits produced by the scheme;

- (b) the contributions are pooled to produce financial benefits or an interest in property for the contributors or persons directly or indirectly acquiring their rights from the contributors (members);
- (c) not all the members (in their capacities as members) take part in day to day management of the scheme; and
- (d) the pool is managed as a whole for the benefit of the members collectively.

conflict: includes an actual or potential conflict

constituent document: see section 4.

control: see section 57

custodian: see section 13.

depository receipt over gold: see section 22.

derivative: see section 25.

eligible index: an index is an **eligible index** for a Passport Fund if:

- (a) it predominantly relates to financial assets or commodities that are regularly traded; and
- (b) it has a clearly defined objective or the market or sector which it aims to represent is clearly defined; and
- (c) it represents a reasonable benchmark for a market or market sector for which it is widely used; and
- (d) it is made up entirely of constituents that, with the exception of those related to commodity prices, are investments that a Passport Fund would be permitted to hold; and
- (e) it is defined and calculated by a person who is not a related party of the Operator of the Passport Fund unless, where the two parties are related parties, there are adequate arrangements in place for managing the specific conflicts of interest that might arise in this situation; and
- (f) it has no:
 - (i) constituent, or
 - (ii) for commodity indexes – group of constituents relating to substantially the same commodity, exceeding 25 per cent of the index; and
- (g) information about it (including information about the composition of the index and the methodology used to construct and rebalance the index) is readily accessible to the public.

embeds a derivative and **embedded derivative:** see section 25.

fair value, of an asset or interest of a Passport Fund, means the value that the Operator would reasonably expect to receive if it were sold on the current market.

financial asset CIS means a CIS that predominantly holds assets that a Passport Fund is permitted to hold under Division 6.2.

financial asset Regulated CIS means a Regulated CIS:

- (a) that predominantly holds assets that a Passport Fund is permitted to hold under Division 6.2; and

- (b) whose members are generally able to redeem their interests from the arrangement or sell their interests on a financial market for a price that is not materially different from the net asset value per interest.

Home Economy, in relation to a Regulated CIS, means the Participant or the first Participant in which it is a Regulated CIS.

Home Economy Laws and Regulations means the laws of the Home Economy, associated regulations, and any other regulatory requirements that apply to Regulated CISs in that economy administered by the Home Regulator.

Home Regulator, in relation to a Regulated CIS, means the Passport Regulator of its Home Economy.

Host Economy, in relation to a Passport Fund, means a Participant, other than the Home Economy, in which the Passport Fund is:

- (a) permitted to be offered; or
(b) proposed to be permitted to be offered;

as a Passport Fund.

Host Economy Laws and Regulations means the requirements that apply to a Passport Fund under the laws of a Host Economy and associated regulations, and any other source of regulation administered by the Home Regulator.

Host Regulator means the passport regulator of the Host Economy of a Passport Fund.

Interest means the right to a benefit produced by a CIS

index fund means a Passport Fund that has publicly disclosed that it has an investment strategy of seeking to achieve returns that track an eligible index.

independent oversight entity: see section 14.

IOSCO means the International Organization of Securities Commissions.

IOSCO assessment methodology means the IOSCO Methodology for Assessing Implementation of the IOSCO Objectives and Principles of Securities Regulation published in September 2011, as revised from time to time.

IOSCO financial services related business means an entity that carries on business in a financial, capital markets or financial services industry and is regulated in an IOSCO jurisdiction or an entity that provides legal, accounting or compliance, services related to that kind of business or consultation services relating to, and addressing particular issues arising in, the operation of CIS.

IOSCO jurisdiction means a jurisdiction in which the securities regulator is an ordinary or associate member of IOSCO.

IOSCO Principles means the Objectives and Principles of Securities Regulation published by IOSCO, as revised from time to time. **market price**, in relation to an asset or an interest, is the prevailing price at which it was last transacted or bid for on a financial market on which it is quoted. **member**: see definition of **Collective Investment Scheme** or **CIS**

money market instrument: see section 24.

net asset value per interest of a Passport Fund means the value of the assets of the Passport Fund, calculated in accordance with Division 7.2 less any liabilities, divided by the number of interests in the Passport Fund and if there is more than

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one class of interest in a Passport Fund on the basis of the assets, liabilities and interests attributable to the class.

officer of an entity includes a director and a Chief Executive Officer of the entity, or their equivalents.

Operator of a Regulated CIS: see section 56.

Participant means an economy that is a party to the MOU.

Passport Fund means a Regulated CIS, or a *sub fund* of a Regulated CIS, that is registered as a Passport Fund by its Home Regulator.

Passport Regulator, for a Participant, has the meaning shown in the following table:

Participant	Passport Regulator
Australia	Australian Securities and Investments Commission
Korea	Financial Supervisory Service
New Zealand	Financial Markets Authority
Philippines	Securities and Exchange Commission
Singapore	Monetary Authority of Singapore
Thailand	Securities and Exchange Commission

Regulated CIS: see section 56.

relevant netting arrangement see section 40.

relevant hedging arrangement see section 40.

related party: see section 57.

risk-assessed government securities: see section 30.

security includes:

- (a) a share or stock in a body corporate;
- (b) a bond or other form of debt security other than a money market instrument
- (c) an interest in a CIS;
- (d) any interest in an item covered by paragraph (a), (b) or (c);
- (e) an option to acquire by issue an item covered by paragraph (a), (b), (c) or (d).

securities lending arrangement: see section 28.

Sub fund means a Regulated CIS or a CIS forming part of a Regulated CIS that also includes another CIS under which assets of the first-mentioned CIS cannot be lawfully applied under any laws of the Home Economy except in meeting liabilities or otherwise for that CIS or the entitlements of members in that CIS.

transferable security: see section 23.

UCITS fund means a CIS that is regulated in accordance with Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) or any amended or replacement of that Directive.

unquoted transferable security means a transferable security that:

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- (a) is not quoted on a financial market regulated by an ordinary or associate member of IOSCO; and
- (b) is not approved for quotation on a financial market regulated by an ordinary or associate member of IOSCO.

Explanatory note: The reference to a financial market in the definition of an unquoted transferable security would cover a regulated non-exchange market, for example, a facility under which dealers place orders common in bond markets.

Value of the assets of a Passport Fund: means the value of the assets of the Passport Fund after deducting any liabilities of the Passport Fund other than liabilities to members as members.

56 Meaning of *Regulated CIS* and *Operator*

For these Rules:

- (a) a **Regulated CIS** in a Participant listed in the table below is a scheme that:
 - (i) was established in the Participant; and
 - (ii) has the legal character specified in the table below; and
- (b) its **Operator** is the entity shown in the table.

Table:

Home Economy of the Passport Fund	Legal character of CIS	Operator
Australia	A registered scheme under the <i>Corporations Act 2001</i> (Cth) of Australia.	The responsible entity of the registered scheme
Korea	A collective investment scheme under the Financial Investment Business and Capital Markets Act of Korea.	The collective investment business entity of the collective investment scheme
New Zealand	A managed investment scheme under the <i>Financial Market Conduct Act 2013</i> of New Zealand.	The manager of the managed investment scheme
Philippines	A duly registered and licensed investment company under the Investment Company Act (Republic Act No. 2629).	The Investment Company Manager or Advisor and/or Distributor of the investment company
Singapore	A collective investment scheme authorised under the Securities and Futures Act of Singapore.	The manager of the authorised scheme
Thailand	A collective investment scheme under the Securities and Exchange Act of Thailand.	The securities company approved to manage the mutual fund

Note The Operator will be a body corporate.

57 Meaning of *control* and *related party*

- (1) For these Rules, an entity *controls* a second entity if the first entity holds a majority of the voting shares of the second entity or the first entity has the capacity to determine the outcome of decisions about the second entity's financial and operating policies.
- (2) In determining whether the first entity has this capacity:
 - (a) the practical influence the first entity can exert (rather than the rights it can enforce) is the issue to be considered; and
 - (b) any practice or pattern of behaviour affecting the second entity's financial or operating policies is to be taken into account (even if it involves a breach of an agreement or a breach of trust).
- (3) The first entity does not control the second entity merely because the first entity and a third entity jointly have the capacity to determine the outcome of decisions about the second entity's financial and operating policies, unless the first entity controls the third entity or vice versa or there is an entity that controls both the first entity and the third entity.
- (4) If the first entity:
 - (a) has the capacity to influence decisions about the second entity's financial and operating policies; and
 - (b) is under a legal obligation to exercise that capacity for the benefit of someone other than the first entity's members;
- (5) For these Rules, each of the following is a related party of an entity (the first entity):
 - (a) a director of the first entity;
 - (b) an entity which has a director in common with the first entity;
 - (c) an entity (the controlling entity) that controls the first entity, whether directly or by intermediate entities that it controls;
 - (d) a director of the controlling entity;
 - (e) the persons that comprise the controlling entity, if the controlling entity is not a corporation;
 - (f) other entities controlled by any of the above;
 - (g) a relative of the persons listed in paragraphs (a), (d) or (e);
 - (h) an entity that is reasonably likely to become a related party; or
 - (i) an entity that was a related party in the past 6 months.

Appendix A

- (1) For these rules, the maximum potential loss of a derivative or securities lending arrangement is the sum of:
- (a) the current replacement cost at market price; and
 - (b) for derivative arrangements – the greater of the notional principal amount or the market value of the underlying multiplied by the percentage in table below subject to subsection (2).
- (2) The market value of the underlying is:
- (a) if the underlying is an asset – the market value of the asset;
 - (b) if the underlying is an interest rate or rate of inflation on which an interest rate is based – the notional value of principal; or
 - (c) if the underlying is an index – the market value of the assets represented in the index.

Residual Term	Interest rate contracts	Currency Exchange rate contracts	Equity derivative contracts	Total return swaps and Credit default swaps	Other contracts
1 year or less	0%	1%	6%	10%	10%
> 1 year and < 5 years	0.5%	5%	8%	10%	12%
> 5 years	1.5%	7.5%	10%	10%	15%

- (3) In the case of credit default swaps where the Passport Fund is entitled to payments unaffected by a credit event of the person liable under the underlying, the relevant percentage is 0% unless the credit default swap contract incorporates a provision on closeout upon insolvency in which case the amount to be added is 10% of any unpaid amount that may become payable to the Passport Fund at the time of the calculation that is not covered by collateral at market value.

Appendix B

- (1) The value of a derivative arrangement is:
- (a) if the derivative is listed in the table below – as specified in the table;
 - (b) if the derivative is not listed in the table below or if a value specified in the table does not give a reasonable relative estimation of the market risk – by determining a value which in the reasonable opinion of the Operator has appropriate relativity to the values of other derivatives calculated in accordance with paragraph (a), taking into account the market value of the equivalent position in the underlying asset.

Example: A value calculated in accordance with the table may not give a reasonable relative estimation of the risks for certain binary options or whether the notional contract value is determined in an un-assumed manner.

Consultation question 10: Should the value referred to in subsection (1)(b) above be market value or notional value of the equivalent position in the underlying asset, whichever is the more conservative?

- (2) If the commitment value of a derivative arrangement is calculated in accordance with subsection (1)(b), the Operator must:
- (a) document why the value is appropriate; and
 - (b) keep a copy of that documentation for 7 years.

Types of derivatives	Commitment value
Plain vanilla options (including bought/sold puts and calls)	
Bond option	Notional contract value x market value of underlying reference bond x delta
Currency option	Notional contract value of foreign currency leg(s) x delta
Equity option	Notional contract size x market value of underlying equity share if the contract size is determined by the number of underlying shares x delta
Index option	Notional contract value x index level x delta or point value x index level x delta if appropriate
Interest rate option	Notional contract value x delta
Warrant and Rights	Number of shares/bonds x market value of underlying referenced instrument x delta
Futures	

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Bond future	Notional contract size x market price of the cheapest-to-deliver reference bond
Currency future	Number of contracts x notional contract size
Equity future	Notional contract size x market price of underlying equity security
Index future	Notional contract size x index level
Interest rate future	Number of contracts x notional contract size
Commodity future	Notional contract size x market price of underlying commodity
Swaps	
Contract for differences	Number of shares/bonds x market value of underlying referenced instrument
Credit default swap	Protection buyer: market value of the underlying reference asset Protection seller: the higher of the market value of the underlying reference asset or the notional value of the credit default swap
Currency swap	Notional value of foreign currency leg(s)
Interest rate swap	Market value of underlying (the notional value of the fixed leg may also be applied)
Total return swap	Market value of underlying reference asset(s)
Forwards	
Forward rate agreement	Notional value
FX forward	Notional value of foreign currency leg(s)

- (3) For this Appendix, *delta* means the proportionate amount that Operator reasonably believes the value of the derivative to the Passport Fund would fall if there was a marginal adverse change in amount of the underlying for that derivative.
- (4) For this Appendix all values are to be calculated in the currency of the Home Economy by applying the exchange rate reasonably determined by the Operator
