

Submission to

**Primary Markets Conduct Division
Markets Conduct Department
Monetary Authority of Singapore
10 Shenton Way
MAS Building
Singapore 079117
(Email: arfp-consult@mas.gov.sg)**

On the matter of

**APEC Consultation Paper dated 16 April 2014 on
Arrangements for an Asia Region Funds Passport**

Chan & Goh LLP

(9 July 2014)

FEEDBACK ON APEC CONSULTATION PAPER ON ARRANGEMENTS FOR AN ASIA REGION FUNDS PASSPORT

On 16 April 2014, the APEC issued a consultation paper which proposed arrangements for an Asia Region Funds Passport. We have reviewed the consultation paper and would like to provide our comments on the consultation paper and our responses to the consultation questions for your consideration.

1. Home economy public offer (pages 12-13)

Please clarify why there is a need for equivalent commissions and similar contract terms to be applied to distributors for a passported fund, as is the case of other collective investment scheme? In general, commissions and contract terms are negotiated between the passport fund operator and each distributor and may vary considerably between various distributors, particularly with regard to fees. As such, it may be difficult and impractical to comply with these requirements.

2. Question 3.5

We note that there is a requirement for an offer to be made in the home economy. Would there be a minimum requirement to be met in terms of the amount that is raised in the home economy or restrictions on whether the passport fund operator can seed/provide initial capital for the fund? As long as the passport fund operator demonstrates to the host regulator that the offer made is a legitimate and bona fide one in the home economy, it should not matter what the fund size is, nor the number of investors, nor how it has performed since inception, when the fund applies to be passported. What about a passported fund where the majority of assets are seeded by the passport fund operator's group of companies as a start - would this be acceptable?

3. Operations requirements (pages 13-14)

We note that there is a requirement for a compliance auditor to be appointment to carry out an audit of the passport fund to ensure compliance with (a) the passport rules and (b) a defined set of obligations under home economy laws and regulations that help ensure the passport fund operational requirements are in place.

Please clarify why it is necessary for an audit of certain home economy laws and regulations related to the passport fund operational requirements (i.e. (b) above). Would it not be sufficient to rely on the home regulator's approval of the passport fund, given that the home regulator would have ensured that the passport fund operator satisfies all home economy laws when it reviews, assesses and approves the application in the first place and that the passport fund operator would have engaged local counsel to advise/assist as well? Further, a compliance audit would add on additional compliance costs to the passport fund. In our view, compliance audit should only relate to (a) above.

4. Question 3.16

With respect to whether professional indemnity insurance (PII) is permitted as a substitute, we would like to propose the following (similar to what has already been set out in paragraph 1.7 of Section 1 of the Standards of Qualifying CIS for ASEAN Passport framework) for your consideration:-

“The passport fund operator may, in lieu of additional capital required, procure an equivalent amount of coverage in PII if:-

- (a) it is satisfied that such PII provides at least the same level of protection to investors when compared to the procurement of the additional capital required; and
- (b) it is acceptable to home economy to do so.

(Example of capital adequacy: A passport fund operator with AUM of USD1 billion must have capital of at least USD 1.5 million (i.e. USD 1 million + (USD 1 billion – USD 500 million) x 0.1%). Assuming that the passport fund operator has shareholders’ equity of USD 1.2 million, additional capital or indemnity insurance coverage of USD 0.3 million would be required).”.

In addition, the home economy may impose a condition requiring the passport fund operator to procure a Letter of Responsibility and/or Letter of Undertaking from its parent company if the parent company is of satisfactory financial standing.

(“Letter of Responsibility” is a commitment from the applicant’s parent company that it will maintain adequate oversight over the applicant’s operations, financial position, and compliance with laws, management and other relevant issues. / “Letter of Undertaking” sets out the maximum liability of the applicant’s parent in support of any liquidity shortfall or other financial obligations.)

The requirements set out in Q3.16, requiring the manager to assess the insurer’s financial strength and for the policy to be in force for at least 1 year, do not seem practical nor necessary, so long as the home regulator is comfortable with the insurer which has provided with the PII coverage.

5. Requirement for custody arrangements (page 19)

We understand that the custodian can delegate its function to a sub-custodian so long as the passport fund operator or the custodian (primary holder) retains responsibility to investors for the acts of the sub-custodian. It is advisable to prescribe that any sub-custodian appointed must be duly licensed/approved/regulated by a competent regulatory authority in its home jurisdiction to give additional protection. The term relevant operator refers to the entity responsible for making investment decisions and generally operating the fund. However, as it is typical for the operator (manager) to appoint the Trustee, which may also act as custodian, it would be more appropriate for the custodian itself to remain responsible for the acts and omissions, and to monitor, the sub-custodians which the custodian may appoint.

6. Question 3.17

In the case of a unit trust where the Managers and the Trustee are independent entities, how can the Trustee, as the proposed independent entity providing independent oversight, monitor the operator (manager) and its personnel for compliance with constitutive and offering documents of the passport fund, and laws and regulations relating to the operation of the passport fund?

Unlike independent members appointed to the operators’ board of directors or on a compliance committee (where both the board of directors or the compliance committee are part of/within the operator), how can a Trustee gain access to the operations of the operator or check on the operator’s staff/personnel? Would the requirement for monitoring of the operator and its personnel for compliance be too onerous for the Trustee to undertake given that a

Trustee's primary role is to ensure investors' interest are protected and that the manager complies with the terms of the trust deed and offering documents?

7. Single entity limit (page 26)

We understand that if Central Clearing Counterparties (CCP) are used, the liabilities of the CCP are excluded from the single entity limit, if the passport fund believes on reasonable grounds, having regard to independent sources of information, that there is very low risk of the CCP defaulting in any of its obligations over a 5 year period.

How does a manager assess a CCP to ensure that the risk of such CCP defaulting is low? What are independent sources of information which a manager can rely on? Would this be credit rating agencies? It would be better to state that if any duly licensed CCP is used, the manager can exclude such liability exposure since the presumption is that the relevant regulator would have assessed such CCP before granting it a licence to act as a CCP.

8. Delegation (page 36)

An operator may delegate any function as allowed under its home economy laws and regulations but must comply with the limbs as set out under the "Delegation" section. It may not be feasible for an operator to have in place suitable processes to control the activities of the delegate since the operator and delegate would generally be independent entities, whether within the same group of companies or not. As long as such delegation is conducted in accordance with the home economy laws (for example, any rules relating to out-sourcing of activities to third parties), it should suffice. If 'control' is required, would this relate to operational control, management control or voting/shareholding control of such delegate?

Colin Chan / Jocelyn Yeo
Chan & Goh LLP