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Department of Fund and Intermediary Supervision  
China Securities Regulatory Commission  
Focus Plaza, 19 Jin Rong Street  
Xi Cheng District  
Beijing, P.R. China 100033

Email: [jigoubu@csrc.gov.cn](mailto:jigoubu@csrc.gov.cn)

Dear Sir/Madam,

### **RE: 2019 Consultation Drafts of QFII/RQFII Regulations**

On behalf of its members, Asia Securities Industry & Financial Markets Association ("ASIFMA")<sup>1</sup> is submitting hereby our comments and suggestions on the Consultation Drafts of the *Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors* (《合格境外机构投资者及人民币合格境外机构投资者境内证券期货投资管理办法(征求意见稿)》) (the "**Measures**") and the *Provisions on Issues Concerning the Implementation of the Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors* (关于实施《合格境外机构投资者及人民币合格境外机构投资者境内证券期货投资管理办法》有关问题的规定(征求意见稿)) (the "**Provisions**", the *Measures* and the *Provisions* are together referred to as the "**Draft Regulations**") issued by the China Securities Regulatory Commission ("CSRC") on 31 January 2019.

ASIFMA members welcome and appreciate the efforts made by CSRC to consolidate the QFII and RQFII schemes and unify their requirements in one set of rules. Our members are particularly glad to see an expansion of the QFII/RQFII's investment scope. We strongly believe that the Draft Regulations will make QFII/RQFII scheme more competitive among the available China market access channels (such as Stock Connect, Bond Connect, etc.).

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<sup>1</sup> ASIFMA is an independent, regional trade association with over 100 member firms comprising a diverse range of leading financial institutions from both the buy and sell side, including banks, asset managers, law firms and market infrastructure service providers. Together, we harness the shared interests of the financial industry to promote the development of liquid, deep and broad capital markets in Asia. ASIFMA advocates stable, innovative, competitive and efficient Asian capital markets that are necessary to support the region's economic growth. We drive consensus, advocate solutions and effect change around key issues through the collective strength and clarity of one industry voice. Our many initiatives include consultations with regulators and exchanges, development of uniform industry standards, advocacy for enhanced markets through policy papers, and lowering the cost of doing business in the region. Through the [GFMA](#) alliance with [SIFMA](#) in the United States and [AFME](#) in Europe, ASIFMA also provides insights on global best practices and standards to benefit the region.

## DEVELOPING ASIAN CAPITAL MARKETS

Our comments and suggestions on the Draft Regulations, which are aimed at furthering the attractiveness of the QFII/RQFII schemes, are organised along the following lines:

**Part 1** – Application process and quota fungibility;

**Part 2** – Overseas hedging positions reporting;

**Part 3** – QFII/RQFII investment scope;

**Part 4** – Remittance and repatriation of funds;

**Part 5** – Disclosure of interest & short swing profit rule;

**Part 6** – Tax-related issues;

**Part 7** – Other related suggestions.

## **1 Application Process and Quota Fungibility**

ASIFMA members appreciate the simplification of the QFII/RQFII approval process. However, in the Draft Regulations, foreign institutional investors are still required to submit the application for QFII/RQFII qualification through its custodian to CSRC. We would like to suggest the following revisions to the Draft Regulations for your consideration:

### **1.1 Registration as opposed to approval process**

As consistent with the more recent access programs, we would like to see the QFII/RQFII schemes move towards a registration rather than approval process at some point in the near future, as this would encourage more foreign institutional investors to participate.

### **1.2 Application Documents**

Article 6 of the Measures requires an applicant to qualify as a qualified investor to meet "other requirements set by CSRC in accordance with the principle of prudential regulation". We would appreciate greater clarity on the meaning of this Article and the additional requirements that CSRC would consider imposing and in what circumstances. This would provide greater transparency to foreign institutional investors on any additional requirements and CSRC's consideration.

We would also like to see clarified in the Provisions some technical issues when applying for the qualified investor license under the consolidated QFII/RQFII schemes, such as whether there will be a check the box exercise that will allow the applicant to select both QFII and RQFII under one application, which our members prefer. In addition, how the Measures and Provisions affect existing QFII/RQFIIs, if any.

### **1.3 Quota fungibility**

QFII/RQFII quota is currently granted to a single entity rather than to a group of affiliated entities. To further the continued usage of the QFII/RQFII access channel, we suggest that the quota already granted to a particular entity be allowed to be transferred to an entity under common control of the quota holder and that future quotas be granted to a QFII/RQFII at the holding company level for usage by majority- or wholly-owned subsidiaries of the holding company. This would facilitate greater usage of the QFII/RQFII quota and afford ease and flexibility to large institutional investors such as global asset managers which have subsidiaries in different parts of the world that may wish to use the investment quota from time to time.

## **2 Overseas Hedging Positions Reporting**

Our members are very concerned about Article 10 of the Provisions which requires a QFII/RQFII to report its overseas hedging positions related to its domestic securities and futures investment through its custodian within 10 business days following the end of each quarter.

CSRC's Explanations of the Measures and Provisions ("Explanations") state that this reporting requirement is intended to prevent cross-border market manipulation and other abnormal trading activities. While our members fully support the prevention of market manipulation, it is unclear how the reporting required by Article 10 of the Provisions will achieve this. Market manipulation is more likely to be detected by trading activity rather than position reporting, especially where positions are reported on a quarterly basis. Instead, we would advocate greater cooperation between regulators in the various jurisdictions to identify and investigate suspicious trading activity. We note that CSRC has entered into MOUs with regulators in many jurisdictions for the exchange of information. We believe that these would form a good basis for CSRC to request information on suspicious cross-border market manipulation activities which is more useful than position reports.

Our members also think that the scope of Article 10 is very broad and that there will likely be practical, legal, regulatory and contractual impediments to meeting such reporting requirements. Therefore, we suggest that Article 10 be deleted from the Provisions or be the subject of further consultation. Otherwise, this Article may deter foreign investors from using what is supposed to be a simplified and unified qualified investor channel.

We understand that per CSRC's 12 February 2019 circular to the QFII/RQFII custodian banks that the quarterly reporting requirement was removed (leaving only an annual report), which simplify the reporting obligations of QFII/RQFII. For this reason, we find the new requirement for quarterly reporting of overseas hedging positions to be surprising.

## **3 QFII/RQFII Investment Scope**

ASIFMA applauds the expansion of the QFII/RQFII's investment scope in the Draft Regulations, especially the part that allows QFII/RQFII's to invest in private investment funds. However, wording in some of the articles in the Draft Regulations require clarification. We would like to set out those points below for CSRC's consideration.

### **3.1 Private Investment Fund**

Article 6 of the Provisions states that a qualified investor can invest in a private investment fund whose investment scope conforms to "Paragraph (1) and (2) of Article 6". This reference is creating some confusion as to whether that means only 6(1) ("stocks, depository, receipts, bonds, bond repurchases, and asset-backed securities traded or transferred on stock exchanges") and 6(2) ("shares transferred on the National Equities Exchange and Quotations") or that it covers all investments listed in Article 6 which are within the permissible investment scope of QFII/RQFII. The Chinese version of the Provisions appears to refer to all investments based on our interpretation.

We believe CSRC's intention is that QFIIs/RQFIIs are allowed to invest in a private investment fund whose underlying assets fall within the permissible investment scope of QFII/RQFII. We would suggest that CSRC amend the current wording in Article 6 accordingly for the avoidance of doubt.

It would also be helpful if CSRC can clarify in the Provisions that QFIIs/RQFIIs can also invest in: (a) a private investment fund of funds; and (b) tranche-based private investment funds, provided the underlying investment scope of these funds complies with the above requirements.

### **3.2 Entrustment of asset**

We would also suggest that the Measures reinstate the current provision in Article 19 of the *Measures for the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors* (《合格境外机构投资者境内证券投资管理办法》) issued by CSRC on 1 September 2006, which allows QFIIs/RQFIIs to entrust investment management entities in China such as securities companies and fund management companies to manage their domestic securities investments as this is broader than Article 17 of the Measures which limits the entrustment of QFII/RQFII assets to asset management schemes set up by asset management institutions such as securities companies and fund management companies. In addition, we respectfully suggest adding to Article 17 of the Measures entrustment to private securities investment fund management companies.

### **3.3 Stock index futures**

#### **(i) Stock index future trading amount limitation**

According to Article 4 of the *Guidelines for Qualified Foreign Institutional Investors to Participate in Stock Index Futures Trading* (《合格机构投资者参与股指期货交易指引》) issued by CSRC on 4 May 2011, QFIIs participating in stock index futures trading shall meet the following requirements: (a) at the end of any trading day, the value of stock index futures contracts held by a QFII shall not exceed its investment quota; (b) during any trading day, a QFII's trading amount of stock index futures (except closing positions) shall not exceed its investment quota. Since these Guidelines are superseded by the Provisions (based on Article 18), we would like CSRC to clarify whether it means a QFII's/RQFII's trading in stock index futures will no longer be limited by the investment quota of such QFII/RQFII.

We believe this is also in line with *the Measures of the China Financial Futures Exchange on Hedging and Arbitrage Trading* (《中国金融期货交易套期保值与套利交易管理办法》) issued by China Financial Futures Exchange ("CFFEX") on 3 February 2012 and further amended on 30 August 2013 and 12 February 2018, where there is no mention of futures trading being limited by the investment quota of QFII/RQFII. We hope this will also mean that in the near future, the quota for futures trading would take into account the appreciation of the QFII/RQFII portfolio.

(ii) CFFEX hedging rules

We would like to know how CFFEX hedging rules would accommodate the rules under the Measures and the Provisions. Given consolidation of QFII and RQFII schemes, we respectfully request CSRC to clarify whether hedging rules will also be applied on a consolidated basis. For example, CFFEX hedging rules require that short index futures value should not exceed the value of corresponding stock. We respectfully request that CSRC confirm which of these calculations will apply: (a) RQFII + QFII corresponding stock do not exceed RQFII + QFII short futures; (b) Stock held under RQFII quota do not exceed RQFII short futures, or (C) stock held under QFII quota do not exceed QFII short futures.

**3.4 Securities lending**

Article 6 of the Provisions allows QFII/RQFII to participate securities lending. We would like some clarity such as:

- (i) whether there will be secondary regulation or rules on how securities lending will work;
- (ii) while the English translation of Provisions only mentions "securities lending" the original Chinese version refers to both securities lending and borrowing. We would like CSRC to clarify whether QFII/RQFIIs are allowed to conduct both securities lending and borrowing. Securities borrowing is essential for the carrying out of short sell as naked short selling is strictly prohibited. However, on the other hand, given there is no relaxation as of now of short sell to be extended to QFII, borrowing won't be of use. On this point, we would like CSRC to confirm whether it also plans to relax and permit QFIIs to conduct short sell.

**3.5 Financial futures contracts**

According to Article 8 of the Provisions, qualified investors shall only trade financial futures contracts for hedging purpose. We would like to know whether CSRC and/or CFFEX have any plan to relax this restriction.

**3.6 Other financial instruments**

Paragraph 1 (9) of Article 6 of the Provisions provides that qualified investors may invest in other financial instruments as approved by CSRC. We would like to know whether these include beneficiary certificates issued by securities companies ("券商受益凭证").

#### **4 Remittance and Repatriation of Funds**

- 4.1** QFII/RQFIIs welcomed the removal by the State Administration of Foreign Exchange ("SAFE") of the 20% cap on monthly repatriation in June 2018 as the ability to freely remit and repatriate funds in and out of China has always been a concern for foreign investors. However, Article 26 of the Measures provides that the remittance and repatriation of the funds by QFIIs/RQFIIs will be subject to the "macro prudential management" by the People's Bank of China ("PBOC") and SAFE based on China's economic and financial conditions, supply and demand on the foreign exchange market and the balance of international payments. This Article creates the kind of uncertainty for foreign investors that have driven many of them to the Stock Connect channel. If the intention of the Draft Regulations is to make the QFII/RQFII scheme more attractive vis a vis the other access channels, we suggest that Article 26 of the Measures be deleted.
- 4.2** According to Articles 2 and 24 of the Measures, to facilitate RMB internationalization, qualified investors are encouraged to invest with offshore RMB funds; upon registration with or approval from SAFE, a qualified investor may remit its investment principal in RMB. We would like the Measures or Provisions to confirm how this rule applies to a current QFII which has already obtained a USD quota. For example, can these QFIIs remit or repatriate funds in RMB now? If so, whether such QFIIs can purchase RMB through offshore RMB participating banks and remit or repatriate like RQFII under the *Notice of the People's Bank of China on Issues Concerning the Improvement of the Management of the RMB Purchase and Sale Business* (《中国人民银行关于完善人民币购售业务管理有关问题的通知》) issued by PBOC on June 2018.

#### **5 Disclosure of Interest & Short Swing Profit Rule**

##### **5.1 Disclosure of interest**

We note that Article 11 of the Provisions distinguishes between the obligation of a qualified investor and that of a foreign investor for whom the former invests when it comes to disclosure of interest. The disclosure of interest obligation rests with the foreign investor who has to report through the qualified investor. However, the qualified investor is also obliged to ensure that the foreign investors under its name strictly comply with relevant information disclosure rules, which is very onerous.

As a foreign investor may be investing in domestic securities through various access channels (e.g. QFII/RQFII and Stock Connect) and through multiple qualified investors (i.e. different asset managers), a qualified investor would not be in a position to know all the domestic securities holdings of a particular foreign investor other than those managed by it, nor would it be able to control or dictate the actions of such foreign investor. Therefore, we would like CSRC to revise this Article to require a qualified investor to only be held responsible for the investments of a foreign investor that it manages, which would be more reasonable and practicable to implement than requiring a qualified investor to ensure that the foreign investors under its name strictly comply with the information disclosure rules.

## 5.2 Short swing profit rule

Article 19 of the Measures provides that when a foreign investor performs its disclosure obligations, it is obligated to aggregate its equity holdings in a company, including the same company's shares listed in domestic stock exchanges or admitted on the National Equities Exchange and Quotations, and the foreign shares listed overseas. The foreign investors shall also disclose relevant securities investments of persons acting in concert according to information disclosure rules of the listed companies. This Article raises the issue of whether and how the aggregation would apply for the purpose of the short swing profit rule.

We understand that to prevent insider trading, Article 47 of the *Securities Law of the People's Republic of China* (《中华人民共和国证券法》) provides that the profit made by directors, supervisors, senior managers and holders of 5% or more of the shares of a listed company who sell their shares in the listed company within six months of purchasing them or who purchase shares in the listed company within six months of selling them belongs to the listed company and that the listed company's Board of Directors shall get back such profit or shareholders may institute legal action to get back such profit if the Board of Directors fail to do so within 30 days of a shareholder's request.

We appreciate that it is possible that shareholders holding 5% or more of the shares of a listed company is an insider who is able to exercise control over the listed company. However, asset/fund managers who manage assets for different clients or funds are not usually an insider privy to inside information even though their percentage of shareholding in a listed company, when aggregated across all clients and/or funds that they manage, reaches or exceeds 5%. This is particularly true in the case of large global asset managers which have many clients and funds.

Article 12 of the *Administrative Measures for Takeover of Listed Companies* (《上市公司收购管理办法》) issued by CSRC on 17 May 2006, as amended on 27 August 2008, 14 February 2012 and 23 October 2014 (the "**Takeover Measures**") provide that a shareholder's interest in a listed company includes not only the shares registered in its name but also shares over which it controls the voting rights and that the interests held by such shareholder and persons "acting in concert" with such shareholder should be aggregated for share disclosure purposes.

It is unclear whether or not the aggregation of shares held by persons "acting in concert" for disclosure purposes under the Takeover Measures apply in the case of the short swing profit rule. Our members would like confirmation that the aggregation requirements under the Takeover Measures do not apply to QFIIs/RQFIIs, in particular the holdings of all funds and client accounts managed by the same QFII/RQFII for purposes of the short swing profit rule. For the reasons cited, we believe it is imperative that the aforementioned aggregation requirement not apply to QFIIs/RQFIIs and asset/fund managers which manage securities investments for multiple clients and/or funds because while individually, each such client or fund may not hold more than 5% of a listed company, the 5% ownership threshold may easily be reached if the shareholdings of all clients and funds managed by the same QFII/RQFII or asset manager have to be aggregated.

The application of the aforementioned aggregation rule to asset/fund managers would have a particularly adverse impact on large asset/fund managers as they may be forced to limit the shareholding of all of their clients and/or funds so as not to trigger the short swing profit rule. Otherwise, the large asset/fund managers will be fined and the clients and funds of such asset/fund managers will be disadvantaged because the profit from any purchase and sale of shares of a listed company by the asset manager within a six-month period will have to be returned to the listed company regardless of whether any single client or fund holds 5% or more of the shares of the listed company in its own right.

### **5.3 Waiver/exemption to short swing profit rule/disclosure of interest**

We note that in those jurisdictions which have a similar short swing profit rule (such as the U.S.), there is an exemption for asset/fund managers because of the recognition that most asset/fund managers will not be sitting on the Board of Directors of a listed company and will not have access to insider information, which we believe is the reason for having a short swing profit rule in the first place.

An exemption for asset/fund managers managing third party assets from the short swing profit rule is more important now than ever given the expected large inflow of funds with MSCI A-share inclusion this year. If a complete exemption is not possible, at least funds offered to the public, whether within or outside China, should be excluded from the calculation of the holdings of the asset/fund manager for purpose of the short swing profit rule.

In addition, many global financial groups have QFII/RQFII license holders. Given the broad application of the concert party presumption, all affiliates of a global financial group will be technically treated as "persons acting in concert" and therefore the shares held by each such affiliate in the same listed company should be aggregated for disclosure of interest or short swing profit rule purpose. Whilst we are aware that many financial groups would like to apply for a waiver to disapply concert party presumptions among different members of the same financial group, there is a lack of information/guidance on how such an application should be made to CSRC and what standards or conditions CSRC would apply in granting any such waiver. We strongly urge CSRC to address the aggregation or "acting in concert" requirement in the formal QFII/RQFII regulations as this is a major cause of concern for large asset/fund managers.

## **6 Tax-related Issues**

While we understand that tax matters are not within the scope of the Draft Regulations nor within the jurisdiction of the CSRC, we would like to set out some tax issues specifically relating to QFII/RQFIIs.

### **6.1 Tax treatment on the new products**

It is important to have clarification on the tax treatment of the new products that QFIIs/RQFIIs will be allowed to invest under the Draft Regulations. Considering that there are still many tax treatments for foreign investors that are still unclear, we would like CSRC to work with other competent authorities to clarify those tax issues that are specific to qualified investors.

## **6.2 Tax filing certificate**

Removal of the requirement for a tax certificate issued by the local tax bureau for repatriation purposes will improve foreign investors' experience with repatriation and capital mobility.

According to the record filing requirement stipulated in the *Announcement of the State Administration of Taxation and the State Administration of Foreign Exchange on Issues Concerning the Record-filing of the Taxation on External Payments for Trade in Services and Other Items* (《国家税务总局、国家外汇管理局关于服务贸易等项目对外支付税务备案有关问题的公告》) issued by SAFE and the State Administration of Tax ("SAT") currently QFIIs/RQFIIs need to perform record filing with local tax bureau before repatriating profit from China. QFIIs/RQFIIs shall submit the tax record filing forms with local tax bureau's stamp to the remitting bank to support their profit repatriation, which imposed administrative burden to QFIIs/RQFIIs players. In addition, local tax bureaus' resource constrains as well as their different restrictions on the implementation of this requirement make repatriation of QFII/RQFII less flexible and even delay the process of profits remittance.

We understand this record filing requirement is actually a foreign exchange control requirement, albeit the regulation was jointly issued by SAFE and SAT. It will be good if the regulator can consider alternatives to facilitate the process. For example, in a meeting China Banking Association had with SAT in 2018, the industry suggested SAT to set up online data sharing platform with SAFE/remitting banks so that taxpayers don't need to go through tax record filing process (or at least simplify the process) when making outbound payments. SAT's response is they are supportive to this suggestion. It is highly appreciated if regulators can consider this suggestion to enhance the QFII/ RQFII platform.

## **6.3 CIT exemption**

According to the *Notice of the Ministry of Finance and State Administration of Taxation on Several Preferential Policies in Respect of Enterprise Income Tax* (《财政部、国家税务总局关于企业所得税若干优惠政策的通知》) ("Caishui 2008 No. 1"), investors receive distributions from securities investment funds are temporary exempted from Corporate Income Tax ("CIT"). It would be helpful to have confirmation that non-resident investors like QFIIs/RQFIIs would qualify for the CIT exemption. In addition, current tax regulation is silent on how to treat the foreign exchange gains or loss on the investment principal. The local practice may also vary for difference locations. We appreciate more clarity on this.

## **7 Other Suggestions**

Set out below are some other suggested related changes for your consideration.

### **7.1 Use of more than three brokers and offer QFII/RQFII investors the options to buy/sell through more than a single broker so as to better ensure best execution (currently must sell through the same broker through whom shares were purchased)**

According to Article 14 of the Provisions, each QFII/RQFII is currently restricted to trade through up to three brokers on each of the two exchanges in China (Shanghai and Shenzhen). The

industry respectfully requests CSRC to consider: (1) expanding the limit beyond the current 3 to an unlimited number so as to encourage more open competition between brokers and to offer better service to institutional investors. Moreover, additional entrants to the brokerage industry are to be expected in light of the lifting of equity ownership caps and licensing scope for foreign securities firms in China. But the current limit of 3 brokers will protect incumbents and hinder new entrants to the market; (2) the requirement to only sell through the same broker through which the shares were purchased (per Detailed Implementing Rules for Securities Trading by QFII/RQFII) add to the operational complexity and compliance costs for institutional investors needing to track such. Note that we are not aware of any such practice in any other market and investors are free to buy and to sell any of their shares through any broker. We ask CSRC to consider relaxing this requirement to better align with global practice.

**7.2 Move to T+1 or T+2 settlement cycle where cash and stock settle simultaneously (e.g. DVP) to protect investors and to remove the prefunding requirements to align with global practice**

For better serving global institutional investors who often trade in baskets and who need to shift their investments from one market to another, we ask CSRC to consider harmonizing towards a T+1 or T+2 settlement cycle with DVP. Harmonization around the same timing cycles for the settlement of securities and cash leads to greater efficiency for global institutional investors as well as encourage investment.

**7.3 Investment advisory services provided by Affiliated PFM**

Article 6 of the Provisions allows QFIIs/RQFIIs to appoint its affiliated onshore PFM to provide investment advisory services. we would like the Provisions to provide that (a) the onshore PFM may also provide discretionary investment services to affiliated QFIIS/RQFIIs and (b)QFIIs/RQFIIs may also appoint unaffiliated PFMs for the same services.

**7.4 Transitional Arrangements**

Finally, it would be helpful to know if there will be any transitional arrangement for existing QFIIs/RQFIIs.

ASIFMA greatly appreciates CSRC's consideration of the points and questions raised in this letter and would be pleased to discuss them in greater detail as appropriate. If you have any questions, please contact Eugenie Shen at [eshen@asifma.org](mailto:eshen@asifma.org) or Tel: 2531 6570. This submission was prepared by PRC law firm Han Kun Law Offices, ASIFMA member, based on feedback from the wider ASIFMA membership.

Yours sincerely,



Mark Austen  
Chief Executive Officer  
Asia Securities Industry & Financial Markets Association