Growing Asia's Markets

China's Capital Markets

A Market in Transition

June 2023

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A. Executive Summary

As China emerges from the pandemic, we believe China's large and dynamic capital markets will continue to transition, offering more investment opportunities for both domestic and foreign investors. We appreciate and welcome the reforms undertaken by the Chinese government in recent years to further liberalise its financial markets for offshore investors and facilitate domestic access to its capital markets. Notably:

(a) the expansion of the Stock Connect, recent launch of the RMB counter in China's Hong Kong SAR (Hong Kong) as well as the anticipated launch of Chinese treasury bond futures in Hong Kong, which complement the key initiatives announced by Fang Xinghai, Vice Chairman of the CSRC, at the China International Finance Annual Forum 2022 held in September 2022;

(b) the launch and development of various mutual market access/connect (互联互通) programmes and new investment products and the removal of restrictions on foreign ownership in various financial institutions and investment quota on QFI investment in domestic securities;

(c) the launch of the Science and Technology Innovation Board (the STAR Market) by the SSE and the registration-based IPO regime across China's national exchanges;

(d) the recent launch of the SWAP Connect on 15 May 2023 which allows foreign investors to access the onshore Interest Rate Swap market through Hong Kong; and

(e) the implementation of substantial legal reforms, including the passage of China's *Futures and Derivatives Law* in 2022 and the draft *Financial Stability Law* in discussion.

On behalf of our members, ASIFMA would like to take this opportunity to recognise the contributions of Chinese regulators, as well as market participants and other relevant stakeholders, towards the path of reforms needed to build robust capital markets in China. As China continues its journey of financial development and reform, ASIFMA is pleased to continue its role as an important bridge between policy makers and market participants, providing feedback on issues arising from policy changes from the perspective of industry experts, as well as from an international perspective.

This Paper aims to identify areas of China's capital markets for further enhancement and offer insights on potential market development areas, which we believe are aligned with the relevant policies set out in the 20th CPC National Congress Report, particularly to deepen structural reform in the financial sector, strengthen and refine modern financial regulation, safeguard financial stability and improve the functions of the capital market. We summarise our recommendations by the relevant objectives below.[1]

[1] Please refer to pages 14-24 for a full List of Recommendations. References to recommendations in this Executive Summary refers to the recommendations set out in the List of Recommendations.

1) **Promoting "high-standard opening up".**

To further incentivise foreign investments in China's domestic markets and reducing the cost of onshore hedging, we recommend: (1) treating all investment managers (including offshore ones) the same way as domestic public funds and exempting them from the short swing profit rule *(Recommendation 18)*, (2) removing the quota requirement on foreign exchange profit sell-off and the risk reserve ratio requirement on forward foreign exchange sales *(Recommendations 77, 78)*, and (3) broadening access to a wider range of hedging products for currency and market exposures *(Recommendations 47, 67, 81)*.

To further enhance the attractiveness of onshore investments for global investors and incentivise foreign investors to tap into China's capital markets, we also recommend:

- equipping global investors with more access to risk management tools such as securities lending *(Recommendations 11, 14)* and higher hedging quotas for listed derivatives *(Recommendation 20)*;

- expanding access to block trading for QFIs and for Stock Connect investors *(Recommendations 23, 24)*;

- removing the pre-funding requirement for QFIs to share the benefits of the DVP reform *(Recommendation 8)*;

- providing tax incentives to foreign investors in respect of their investments under various market access schemes *(Recommendations 61, 97, 98)*;

- allowing the use of Bond Connect assets as collateral for non-centrally cleared derivatives *(Recommendation 54)*; and

- shifting the client suitability framework from a product-based approach to a holistic, portfolio-based approach *(Recommendation 87)*.

2) **Amplifying the interplay between domestic and international markets.**

There is strong market sentiment for further expansion and diversification of products available under various market access regimes (including Stock Connect, Bond Connect, Wealth Management Connect, Swap Connect, QDII, QFI and MRF schemes). For example:

- product eligibility criteria for Stock Connect should be further expanded to include the full universe of China A shares *(Recommendation 12)*;

- the holiday trading mechanism for Stock Connect should be further expanded to facilitate trading on holidays *(Recommendation 13)*;

- the scope of products available under Wealth Management Connect should be expanded to include higher risk products such as equity funds, products domiciled outside of Hong Kong and Hong Kong-domiciled funds that feed into overseas funds *(Recommendation 93)*;

- private credit funds should be made available for insurers' investment under the QDII scheme *(Recommendation 101)*;

- restrictions on the domicile of funds recognised under the MRF and delegation of investment management under the MRF should be relaxed *(Recommendation 91)*; and

- a Repo Connect scheme should be introduced to allow foreign investors to leverage their "Connect" infrastructure to access onshore liquidity and financing *(Recommendation 47)*.

To promote greater integration and connectivity between China's capital markets and offshore markets, we recommend that the investment quota under Wealth Management Connect be increased *(Recommendation 94)* and the range of eligible participants under Stock Connect (for SBL), Bond Connect and Wealth Management Connect (for distribution) be further broadened *(Recommendations 14, 38, 95)*.

Furthermore, it is recommended that foreign entities should be allowed to participate in China's capital markets more actively. For example, foreign market makers should be welcomed to promote market liquidity *(Recommendations 36, 39, 73)* and foreign bank branches should be eligible to serve as local custodians under the CIBM Direct multi-layer custodian bank model *(Recommendation 59)*. International brokers and rating agencies should also be granted further access in the onshore markets *(Recommendations 69, 75)*.

3) **Enabling cross-border data sharing to cultivate a vibrant and globally connected financial market.**

We respectfully submit that the stringent or unclear requirements on cross-border data sharing, particularly among members of the same group, in the PRC pose operational uncertainties and challenges for capital markets participants, hindering their ability to share data, particularly in the financial sector, across borders for critical business flow and efficiency. Overall, we recommend revisiting and reassessing the rules applicable to cross-border data transfers using a risk-based approach and clarifying how they should be implemented *(Recommendations 103-109)*. In terms of the financial sector, we recommend carving out certain types of data from the general prohibitions. For example, the sharing of research and investment outlook, portfolio or financial analysis, shareholding information and AML/CTF information between group companies should be allowed to meet legitimate business, compliance and risk management needs *(Recommendations 110-112)*.

4) **Fostering a "world-class business environment" and advancing law-based governance.**

We believe additional regulatory guidance or dedicated legislation on the below topics would help clarify policy and regulatory expectations and facilitate compliance by market participants: (1) program trading rules for the securities and futures market *(Recommendation 25)*, (2) trading protocols in the bond market *(Recommendation 45)*, (3) workflow for the QDLP program *(Recommendation 102)*, (4) form and scope of the personal information protection impact assessment report expected for cross-border transfers of personal information *(Recommendation 109)*, and (5) the multi-layer custodian bank model under the CIBM Direct scheme *(Recommendation 58)*.

We seek clarifications on certain aspects of the existing legal and regulatory framework, with a view to enhance investors' understanding and facilitate their informed assessment of investment opportunities and risks. For example, those relating to: (1) onshore retention of working papers and Sensitive Information transfer approval requirement in relation to overseas listing for PRC companies *(Recommendations 1, 2)*, (2) application of the uptick rules even to long sales for QFIs with outstanding borrowed securities *(Recommendation 11)*, and (3) bond investments eligible for applicable tax exemptions *(Recommendation 76)*.

We recommend that internationally recognised standards and industry documentation such as the ISDA Master Agreement for OTC derivatives transactions *(Recommendation 63)*, GMSLA for bonds' lending and borrowing transactions *(Recommendation 52)*, GMRA for repurchase transactions *(Recommendation 49)* as well as ISO standards for clearing and settlement systems *(Recommendation 9)* be more widely recognised and adopted in China's capital markets.

Furthermore, we believe standardising and streamlining processes and procedures in the share market, bond market as well as foreign exchange market will increase the accessibility and efficiency of China's capital markets. We recommend further enhancement of China's market infrastructures, such as its payment and clearing systems, including:

- development of a CNH PVP risk mitigation infrastructure to protect market participants against loss *(Recommendation 147)*; and

- update of SHCH's rules to allow a clearing member to initiate the close-out netting process in accordance with applicable clearing rules upon the clearing house's own default *(Recommendation 148)*.

5) **Implementing talent development reform and increasing international talent exchanges.**

We support the introduction of a dual-licensing regime for individuals and entities licensed in one jurisdiction within the GBA to engage in certain activities in another jurisdiction without having to obtain a separate licence in that jurisdiction *(Recommendation 90)*.

For brokers with segregated QFI and Stock Connect teams, we support allowing brokers' onshore trading desks to manage Stock Connect orders on behalf of offshore affiliates to break down barriers and provide onshore staff with greater opportunities *(Recommendation 15)*.

For asset management companies with portfolio or investment managers in the Mainland, we recommend that they be allowed to provide investment advice to their offshore affiliates and/or offshore funds of such affiliates (*Recommendation 83*).

6) **Accelerating the development of the digital economy and strengthening the safeguards for ensuring cyber and data security.**

We would like to see regulatory clarity on: (1) whether PRC entities of FIs are permitted to use public cloud *(Recommendation 113)*, (2) requirements and expectations on the use of cloud service providers in the PRC *(Recommendation 113)*, and (3) PBOC's roadmap on adopting financial community cloud *(Recommendation 114)*.

To manage cyber risks, we recommend that (1) collection of sensitive data be limited to those directly relevant and necessary for accomplishing specific purposes *(Recommendation 117)*, (2) any future material cyber events or data breaches are timely disclosed to impacted industry members *(Recommendation 118)*, (3) alternative approaches for receiving and handling of sensitive data as well as FI's demonstration of cybersecurity capabilities be explored *(Recommendations 115, 118)* and (4) the Financial Sector Profile created by the global financial industry be recognised *(Recommendation 119)*.

7) **Pursuing green and sustainable development.**

We recommend expanding the PBOC's carbon emission reduction supporting tools *(Recommendation 134)*, providing incentives to encourage financial institutions to participate in green finance product design and investment *(Recommendation 132)*, attracting blend funds to energy conservation and low-carbon sectors *(Recommendation 133)*, and further enhancing sustainability-related disclosures *(Recommendations 135-138)*.

1. List of Recommendations

Theme	Recommendations	Page[2]
Equities –Primary Market		
Overseas Listing of Domestic Companies	1. Clarify the Onshore Retention Requirement to better guide securities companies and securities service providers' capacity to comply with mainland regulations. 2. Clarify the Transfer Approval Requirements in respect of Sensitive Information. 3. Clarify that the Cooperation Approval Requirement only applies to domestic securities companies and securities service providers.	27

[2] Click to visit/look up the corresponding pages for detailed recommendations.

Theme	Recommendations	Page[2]
Registration-based IPO System Reform	4. Remove the currently mandatory IPO sponsor co-investment requirement for STAR Market and ChiNext in a phased manner.	30
Pricing and Placement Reform	5. Grant more flexibility to issuers and underwriters in the pricing and allocation process. 6. Remove "top price quote exclusion" rule and special disclosure requirement for pricing higher than the lowest among "the four indicators". 7. Optimise the strategic placement process.	32
Equities –Secondary Market		
QFI	8. **(DVP and Pre-funding)** Remove the pre-funding requirement. 9. **(Post-trade and Regulatory Reporting)** Adopt ISO standards for clearing and settlement. 10. **(Multi-broker Model)** Reform the trading rules of SSE and SZSE to allow the multi-broker model. 11. **(SBL)** Clarify how the uptick rule applies to QFIs, and avoid impeding the ability of the long holder to trade.	35
Stock Connect	12. **(Trading Universe)** Expand scope of eligible investment (in terms of both stocks and ETFs). 13. **(Holiday Trading)** Expand trading calendar to all market trading days on the host market. 14. **(SBL)** Include affiliates of Exchange Participants and Qualified Institutions as eligible SBL participants, and expand the category of Qualified Institutions to encompass accredited and regulated institutions such as Agent Lenders and Custodians. 15. **(Onshore Trading Desk to Manage Northbound Orders)** Allow brokers' onshore trading desks to manage Stock Connect orders on behalf of offshore affiliates. 16. **(Bilingual Stock Connect Rules of SSE/SZSE)** Issue both Chinese and English Stock Connect rules and ideally the English version to be binding or at least available on the official websites of SSE and SZSE. 17. **(Aggregation of Positions Across Custodians)** Allow Stock Connect investors to aggregate positions across accounts opened at different custodians at same beneficial owner level.	39
Short Swing Profit Rule	18. Treat all investment managers (including offshore ones) the same way as domestic public funds and exempt them from the short swing profit rule and look at the shareholdings of funds and/or clients that are managed under separate agreements by the same asset manager separately.	51
Access to Onshore Derivatives	19. Diversify derivative product suite (e.g., bond futures and ETF options) accessible to QFIs. 20. Remove the hedging-only restrictions or increase flexibility on hedging quota calculations.	52

Theme	Recommendations	Page[2]
	21. Provide offshore investors without a QFI license, including those under the Stock Connect scheme, access to PRC onshore derivative products. 22. Start listing SSOs.	
Block Trades	23. Provide Stock Connect participants a mechanism to conduct block trading. 24. For QFI investors, extend the execution order confirmation period of block trading on SSE Main Board and SZSE.	55
Program Trading	25. Establish and implement program trading registration and report mechanism for stock trading; establish a unified and dedicated legislation on program trading applicable to both securities and futures markets. 26. Pay particular attention to timely registration and reporting, systems security, and security of normal trading order of the exchange.	56
Fixed Income		
CIBM	27. Expedite CIBM market-maker application process and begin approval of foreign firms. 28. Simplify administrative procedures on non-trade transfer of CGB between CIBM Direct and QFII of the same registered investor. 29. Raise or remove dual currency ratio. 30. Allow omnibus account structure with recognition of foreign nominee concept.	62
Northbound Bond Connect	31. Allow only change in settlement date for rolling settlement. 32. Not treat a change in settlement date as a failed trade thereby obviating the need to file a failed trade settlement report. 33. Allow failed trade settlement to be reported electronically. 34. Allow CFETS accounts to be registered in both the name of the asset manager and the client (as with the QFI account structure). 35. Allow non-trade transfers when there is a change in asset manager but not client.	65
Southbound Bond Connect	36. Increase quota and number of market makers. 37. Broaden scope of eligible assets and clarify what is in scope. 38. Enlarge eligible investors base. 39. Allow additional custodians and market makers to join the programme.	68
Bond Connect generally	40. Simplify operational and trading processes. 41. Simplify and streamline documentation process for onshore currency hedging under Bond Connect. 42. Decouple CIBM market-maker status from Bond Connect market-maker status so that eligible foreign banks and foreign securities firms operating in China can apply for the Bond Connect market maker directly.	69

Theme	Recommendations	Page[2]
	43. Align access channels to the same markets (such as CIBM Direct and Bond Connect to the CIBM). 44. Approve the launch of Inter-connection between CIBM and Exchange Bond Market as soon as possible. 45. Develop trading protocols onshore, specifically the ability to request and quote two-way prices and the ability for market participants to counter levels dynamically. 46. Continue the panda bond market reforms to attract more international issuers and investors.	
Bond repo and bonds lending and borrowing	47. Allow international investors to access the bond repo market from offshore through a Northbound Connect channel. 48. Allow triparty agents to post bonds held in CIBM as collateral to receive RMB onshore. 49. Recognise the Global Master Repurchase Agreement (GMRA) as a legally valid standard repo master agreement in broader PRC law. 50. Include the enforceability of close-out netting in respect of bond repo transactions in statute. 51. Clarify the handling of pledged bonds with CCDC in the event of a reverse repo party's bankruptcy in a repo transaction. 52. Provide similar framework for bonds' lending and borrowing transactions under both local and international master agreements (GMSLA), i.e., encouraging the recognition of the GMSLA as the master agreement in use in China and the inclusion of enforceability of close-out netting for SBL in law-making. 53. Introduce daily margin as well as mark-to-market regime in China repo market.	74
Use, custody, and settlement of onshore bonds	54. Allow use of Bond Connect assets as collateral for UMR (Unclear Margin Rules) purposes and SWAP Connect margining requirements (and extended to other derivative transactions and purposes). 55. Develop triparty services and connect CCDC and SHCH platform to international triparty (and bilateral) collateral managers, allowing a broader use of Chinese fixed income assets as collateral both on- and off-shore. 56. Allow ICSDs and custodian banks to open an omnibus account at the level of CCDC / SHCH and offshore settlement within the ICSD's /custodian bank's books under CIBM Direct. 57. Adopt international best practices with respect to BSAs (Bond Settlement Agent) and require that trading and settlement functions be separated under CIBM Direct. 58. Nail down detailed guideline for multi-layer custodian bank model under CIBM Direct.	77

Theme	Recommendations	Page[2]
	59. Allow foreign bank branches to become qualified local custodian under multi-layer custodian model under CIBM Direct. 60. Allow foreign bank branches to conduct custody business to look through the parent company's capital capability in order to fulfil applicable net asset requirement.	
OTC Derivatives	61. Income to be derived by Hong Kong market investors from Interest Rate Swap transactions conducted via the Swap Connect be non-taxable from both PRC Corporate Income Tax and PRC Value Added Tax perspectives. 62. Streamline the CIBM Direct, Bond Connect and QFI channels in terms of permissible investment instruments, so that all investors can have access to hedging tools and funding products such as futures, interest rate swaps and bond repo. 63. Broader adoption of ISDA/CSA (vs NAFMII) for OTC derivations following the enactment of the FDL. 64. Implement exchange of initial margin under UMR to align with practices of other markets and allow foreign investors to comply with their home jurisdiction requirements when transacting cross-border with their China based counterparts. 65. Finalize and publicize the *Guiding Opinions on Promoting the Regulation of Derivatives Business (Consultation Paper).*	80
CGB Futures	66. Launch HKEx's Chinese bond futures product as soon as possible. 67. Accelerate foreign investors direct access to onshore CGB futures. 68. Remove restriction for QFIs to trade financial futures for hedging purpose only. 69. Allow US futures brokers to become Overseas Intermediaries / Overseas Brokers to onshore futures exchanges. 70. Harmonise rules and contracts between Overseas Intermediaries (OI) and QFI. 71. Simplify registration process and streamline documentation requirements for foreign investors of OI. 72. Approve US entities to be eligible to apply as a foreign investor via an OI. 73. Introduce concept of market makers in the futures / listed space.	84
Other Fixed Income Matters	74. Market alignment with international best practices – synchronisation of onshore clearing infrastructure with offshore bond market. 75. Further grant access to international rating agencies and guarantee the level playing field with their domestic peers. 76. Expand the scope of bonds eligible for exemption from CIT and VAT under Circular 108 for interest income derived by foreign investor to include all debt instruments with the same	88

Theme	Recommendations	Page[2]
	characteristics as bonds, including Asset backed notes ("ABN"), Asset-backed securities ("ABS"), Private Publication Notes ("PPN") and Interbank Certificates of Deposit ("CD") and provide withholding mechanism for debt instruments traded in China market that are not in scope.	
Foreign Exchange		
	77. Remove quota requirement on FX profit sell-off (which currently prevent bank from actively managing FX risks). 78. Remove the 20% risk reserve ratio for forward foreign exchange sales. 79. Extend API connectivity to all CFETS trading modes and protocols to the industry. 80. Simplify document checking requirement for client-facing trades. 81. Bring new products to the market that offer end-users with a cost-effective means to hedge their currency exposure, e.g., barrier CNYFCY options. 82. Increase coordination among regulators and loosen certain ratio requirements which constrain the capacity of banks to serve offshore investors.	101
Onshore Operations		
Onshore Operations of Foreign Firms	83. **(FMC)** - lift or relax restrictions on the sharing of research and other information between an FMC and its foreign shareholder. - allow FMCs to manage, trade for and/or advise on the investments of foreign portfolios or funds that invest in the mainland market (in which case, provide clarification that such activity onshore will not subject such foreign portfolios or funds to taxes in China as this is currently unclear). 84. **(PFM)** allow PFMs to manage, trade for and/or advise on the investments of foreign portfolios or funds (besides their affiliated QFIs) investing in the China market, and provide tax clarity that they will not create a taxable presence of such foreign portfolios or funds in China. 85. **(Broker Rating)** revise the broker rating system to bring more symmetry between the reward and penalty structure. 86. **(Derivatives License)** attach less importance to registered capital and net capital, and clarify the existing Tier 1 approval process. 87. **(Investor Suitability Assessment)** re-align the liability standard to better reflect the practical and commercial reality that asset managers may rely on distributors to conduct investor suitability assessments, and shift the client suitability	109

Theme	Recommendations	Page[2]
	framework from a product-based approach to a holistic, portfolio-based approach. 88. **(Custodian Settlement Qualification)** allow foreign bank branches to conduct QFI settlement business by leveraging parent company's capital capabilities. 89. **(Third-Party Connection)** remove the prerequisite that a broker must be rated grade A or higher for the past two out of three years in the draft *Interim Administrative Provisions on External Connection with Trading Information Systems of Securities Companies.*	
Dual Licensing	90. Introduce a dual-licensing regime, allowing individuals and entities licensed in one jurisdiction within the GBA to engage in activities within a defined scope in another jurisdiction without having to obtain a separate license in that jurisdiction, would greatly enhance the cross-border human capital flow across the GBA and facilitate the integration of the financial markets across the GBA.	116
Other Connects		
MRF	91. Allow more flexibility in the location where a fund is domiciled for the northbound MRF, which would not only offer Mainland investors more choices but also enhance the attractiveness of the MRF to global fund managers who may not have set up Hong Kong domiciled funds. In the absence of overseas domiciled funds being eligible for the MRF, allow delegation of investment management by Hong Kong fund managers to offshore managers, which would help expand the fund choices to Mainland investors which can benefit from access to funds with more diversified investments.	120
WMC Scheme	92. Remove the requirement for face-to-face account opening with Mainland banks under the Northbound Scheme or waive such requirement for investors who are existing clients of the relevant Mainland banks in Hong Kong. 93. Broaden the scope of products available under the WMC Scheme to cover higher risk products, including equity funds and products domiciled outside of Hong Kong or Hong Kong-domiciled funds that feed into overseas funds. 94. Increase individual investment quota, or distinguish investors by two categories, namely retail investors and professional investors, and increase their individual quota respectively. 95. Broaden the range of eligible distributors by allowing securities companies and fund management companies to distribute products under the WMC Scheme. 96. Relax the non-solicitation model such that educational and information sessions can be conducted by product issuers across the different jurisdictions within the GBA, and if necessary, in the presence of or together with the distributor.	122

Theme	Recommendations	Page[2]
	97. Implement broad tax exemption, including exemptions on corporate income tax, individual income tax and value added tax on any income, capital gains and distributions derived from all investments made under the WMC Scheme. 98. Provide clarity that cross-border activities undertaken under the WMC Scheme in the GBA by participating Hong Kong banks or asset managers do not create any taxable presence in China for them from both corporate and individual income tax perspectives. 99. Enhance the cross-border payment and settlement systems within the GBA by automating processes and implementing a set of standards, protocols and procedures to be applied consistently across different jurisdiction within the GBA.	
QDII	100. Continue promoting the QDII scheme as a key cross-border channel that would provide domestic investors' access to the offshore product suites and foster knowledge exchange of global best practices. 101. Broaden the scope of overseas eligible investments for insurers to include private credit funds (e.g., senior, mezzanine and special situations debts).	127
QDLP	102. Fine tune the regional guidance on QDLP approval process, and promote standardization of the QDLP workflow.	127
Cross-Border Data		
Data Export Paths	103. Define CII and important data on the basis of balancing cyber/data security and need of free data flows for efficient business operations and adopt a risk-based management approach. 104. Establish online application channels to streamline the application process for the data export security assessment and promote the communication between enterprises and regulatory authorities. 105. Embrace flexibilities in the data export security assessment report and application materials submitted by data processors, such as requirements on disclosure of hard-to-access information. 106. Confirm whether a more streamlined and less stringent process is available for data transfers to Hong Kong. 107. Clarify how a China based entrusted party legitimises its necessary data transfer to overseas recipient if the Standard Contract would be adopted for the data export. 108. Allow the Standard Contract's wording to be modified provided the substance of all prescribed safeguards is maintained. 109. Provide further guidance on the PIPIA for personal information export, including but not limited to introducing a "white-list" or similar mechanism in connection with the assessment	130

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	factor of whether laws and policies of the overseas recipient's jurisdiction will impact the performance of the Standard Contract.	
Cross-Border Sharing of Data in Financial Sector	110. Allow research sharing and exchange of investment outlook as well as portfolio or financial analysis between international asset managers and their onshore subsidiaries. 111. Allow sharing of shareholdings in a PRC listed company within a group (including offshore subsidiaries) for compliance with PRC disclosure obligations. 112. Allow sharing of AML/CTF information within a group (including offshore subsidiaries) for internal control and compliance purposes.	136
Technology and Cybersecurity		
Public Cloud in China	113. Clarify that FIs' entities in China can continue to use global systems and applications, and for onshore applications, clarify what are the requirements and expectations among which cloud providers can be accessed for such onshore applications. 114. Clarify PBOC's plan on cloud in the context of reported financial community cloud.	141
Multi-Level Protection Scheme	115. Allow for global technical support such that global FIs could fully leverage expertise available firmwide. 116. Allow global firm to leverage international industry best practice and have consistent technology stack in China.	143
Cyber Supervisory Requirements	117. Limit collection of sensitive data to that which is directly relevant and necessary to accomplish specific purposes and explore alternative methods by adopting appropriately secured methods and practices to receive or sight the sensitive data from firms. 118. Provide timely disclosure of future material cyber events or data breaches to impacted industry members and information on what sensitive data they have gathered from the industry may have been compromised. 119. Reconsider regulatory-led or regulator-commissioned third-party-led pen testing. 120. Work with FIs to identify alternative approaches that FIs could demonstrate their cybersecurity capability. 121. Recognize the Financial Sector Profile of Cyber Risk Institute.	144
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Draft VAT Law	122. Provide taxpayer with flexibility on adopting or waiving the exemption treatment. 123. Promote the development of fully digitalised invoice in the financial industry. 124. Provide a transition period for the financial industry. 125. Clarify the principles arising under the place of consumption rule.	148

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	126. Clarify the non-creditable items or provide a simple and reasonable input tax portion method to reduce the VAT management burden and compliance cost of taxpayer. 127. Provide exemption for offshore investors in relation to gains from trading of and payments relating to financial products and derivatives in the draft VAT Law. 128. Clarify the scope of exempted financial products and derivatives to include OTC derivatives. 129. Clarify definition of "listing" in the VAT Law or VAT implementation rules in respect of gains from trading of financial products by adopting the definition widely accepted by financial service industry. 130. Specify principal for distinguishing taxable activities and non-taxable activities or add back the "fallback clause" of "other circumstances as prescribed by the competent fiscal and taxation authorities of the State Council". 131. Continue to provide VAT incentives that is currently in force, yet not specifically included in the draft VAT Law.	
Sustainable Finance		
National Policies and Regulations	132. Provide policy incentives, or interest subsidies, and other appropriate incentives to encourage financial institutions to actively participate in the design, issuance and investment of green financial products. 133. Attract blend funds to energy conservation and low-carbon sectors.	153
Regulatory Framework for Green Credit	134. Further expand the PBOC's carbon emission reduction supporting tools.	154
Sustainability-related Disclosures	135. Introduce domestic disclosure frameworks economy-wide by 2025, aligning with or adopting global standards. 136. Consider adopting a "phased-in" approach to disclosure reporting – this recognizes the need for initial flexibility and allows time for methodologies to mature, for greater standardization to be developed and data to become more readily available. 137. Leverage parent level disclosures to meet local requirements. 138. Align transition plan under the TCFD and ISSB frameworks.	157
Carbon Market	139. Develop the compliance carbon markets in China as the key driver for carbon pricing and support the further integration of these markets, the exploration of a futures market and participation of foreign financial institutions to assist in building liquidity, hedging and carbon pricing (as well as other price discovery mechanisms such as auctions). 140. Develop voluntary carbon markets (VCM) in China, aligned with international standards, such as Integrity Council on Voluntary Carbon Markets (ICVCM) to reduce the risk of	158

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	fragmented markets and to facilitate international flow of capital. 141. Develop a connect scheme between mainland exchanges and HK Core Climate - an initial step in connecting with international markets.	
China's Role on Global Sustainable Finance Stage	142. Encourage further development of the Taxonomy to complete the remaining sectors comparison – this could serve as a template for further comparison between regional taxonomies and be helpful on the journey to interoperability/equivalence. 143. Ongoing engagement and policy discussions between the Chinese financial policymakers and the industry – in both formal and informal dialogue. 144. Support for capacity building, as addressing climate change is an industry wide challenge.	160
Sustainability in Asset Management	145. Observe regional and international sustainability developments. 146. Focus on non-prescriptive disclosure rules which can protect the interests of end investors but without restricting the evolving dynamics of the nascent sustainable investment market.	163
Market Infrastructure		
Payments	147. Permit the development of CNH PVP risk mitigation infrastructure for the protection from the loss of principal on payments for all market participants, both mainland Chinese and international entities.	166
Clearing	148. SHCH updates its legal opinion after such amendments have been made to its close out methodology set out in its revised clearing guidelines.	168
Overseas FMIs	149. Develop a licensing or registration process authorizing the provision of cross-border services, with detailed requirements including scope and mechanism for reporting to ensure covered FMIs have a clear understanding of the regulatory expectations.	172

B. Equities - Primary Market

1. China's Primary Market

There has been a growing trend of IPO market reform around the region in recent years, as markets and Asian regulatory authorities seek to strike a balance between allowing companies to access global capital markets whilst ensuring investor protection. Regulators and exchanges have been actively engaging market participants to explore such reforms in Singapore, South Korea, Hong Kong, and the Chinese mainland. The emphasis on IPO regulations has increased due to the growing competition for capital, as well as the rising number of companies seeking to list on international markets. Regional regulatory bodies have been consulting the public and implementing new rules and guidance aimed at improving market transparency, corporate governance, and reducing risks to investors. Additionally, there has been a greater push for international cooperation among regulatory bodies to ensure consistency in the application of rules across different jurisdictions. These reforms aim to create a more stable and secure environment for companies seeking to list globally while ensuring greater investor confidence in the markets.

Amidst this backdrop, China has been particularly active, with Chinese enterprises successfully accessing capital both onshore and offshore via the domestic and overseas exchanges, respectively. The past three years have witnessed significant reforms to the primary markets both on the Mainland and in Hong Kong. Over the past few years, regulatory reforms in the Mainland have been carried out to strengthen the governance of how Chinese enterprises (be they private or state owned) tap global capital markets while ensuring compliance with central government policies about sectoral reforms. In recent reports on the work of the government[3], the central government reiterated the objectives to promote high-quality development and cooperation by making full use of international and domestic markets and resources, observing market principles and international rules, etc. The key IPO reforms of the mainland market regulations in recent years include:

- China extended the successful pilots on Shanghai Stock Exchange (SSE)'s STAR Market, Shenzhen Stock Exchanges (SZSE)'s ChiNext, and recently established Beijing Stock Exchange (BSE) to the main boards of SSE and SZSE, as well as the National Equities Exchange and Quotations, introducing a registration based IPO framework for the mainland Chinese exchanges. For a comparison of the latest criteria for listing on the three national Exchanges and relevant key rules, please refer to Annex 1 to this Paper;

[3] English version of the *Report on the Work of the Government* delivered at the fifth session of the 13th Nationa l People's Congress, http://english.www.gov.cn/premier/news/202203/12/content_WS622c96d7c6d09c94e48a68ff.html.
English version of the *Report on the Work of the Government* delivered at the first session of the 14th National People's Congress, http://english.www.gov.cn/news/topnews/202303/15/content_WS64110ba2c6d0f528699db479.html.

- the China Securities Regulatory Commission (CSRC) launched the *Trial Administrative Measures of Overseas Securities Offering and Listing by Domestic Companies* (《境内企业境外发行证券和上市管理试行办法》, the "New Filing Rules"), which now officially recognizes VIE structures, which had previously operated in a regulatory grey zone for many years.

And some key IPO reforms in Hong Kong include:

- the Hong Kong Stock Exchange (HKEX) enhanced its Listing Rule 19C to help facilitate the homecoming of Chinese companies listed in overseas markets, including grandfather exemptions for those with existing Weighted Voting Rights (WVR);

- HKEX has also more recently launched a Specialist Technology Board (Listing Rule 18C), offering corporate issuers a new alternative venue to NASDAQ and to the STAR Market;

- To address investor concerns around price discovery and price stability, Hong Kong Securities and Futures Commission (SFC) also introduced a new Code of Conduct around the IPO book building process.

With respect to overseas listings, China and the U.S. have achieved a breakthrough in audit cooperation and also CSRC issued rules to better monitor overseas listings:

- 2022 ushered in a solution to the long overhanging issues around the Public Company Accounting Oversight Board (PCAOB) audits of US-listed Chinese companies. Based on the principle of reciprocity, China and the U.S. reached an audit oversight cooperation agreement in August 2022 between the CSRC, and the Ministry of Finance and the PCAOB (the "Audit Inspection Cooperation Agreement"), which allows American officials to review audit documents of Chinese companies listed in the U.S. In December 2022, the PCAOB confirmed with the SEC that they were allowed to successfully inspect the work of auditors in China with unfettered access,[4] and in May 2023 released inspection reports for two firms inspected in 2022[5]; and

- The increasingly active dialogue and collaboration between CSRC and SEC have highlighted the need to close legacy gaps in the regulation and supervision of Chinese Red Chip companies (often incorporated offshore via VIE structures) which have historically not been on CSRC's radar screen when they apply to list on an overseas exchange. Consequently, the CSRC issued a consultation on changes to the rules governing overseas listing and published new

[4] PCAOB news release and SEC statement, https://pcaobus.org/news-events/news-releases/news-release-detail/fact-sheet-pcaob-secures-complete-access-to-inspect-investigate-chinese-firms-for-first-time-in-history; https://www.sec.gov/news/statement/gensler-determination-statement-20221215.

[5] PCAOB news release, https://pcaobus.org/news-events/news-releases/news-release-detail/pcaob-releases-2022-inspection-reports-for-mainland-china-hong-kong-audit-firms.

regulations on the overseas securities offering and listing by domestic companies. Pursuant to such regulations, the CSRC requires domestic Chinese companies, which are seeking overseas offering and listing, to file applications and complete the review process, so as to ensure they are compliant with Chinese regulations and policy. The definition of a domestic Chinese company going forward will be based on substance (location of assets and revenues, location/nationality of management team and customer base) rather than on form (location of company incorporation). The CSRC is authorized to accept or reject any overseas offering and listing application, and will serve as a gatekeeper to monitor and to better safeguard the interests of overseas investors.

Our members applaud the significant developments of IPO market reform per above, but would like to make some recommendations regarding the new rules, including Overseas Listing of Domestic Companies *(section 1a.)*, Registration-based IPO System Reform *(section 1b.)* and Pricing and Placement Reform *(section 1c.)*.

1a. Overseas Listing of Domestic Companies

ASIFMA welcomes the finalization of the long-waited new rules regulating domestic firms' overseas listings, including mainly the New Filing Rules and the *Provisions on Strengthening Confidentiality and Archives Administration in Respect of Overseas Issuance and Listing of Securities by Domestic Enterprises* (《关于加强境内企业境外发行证券和上市相关保密和档案管理工作的规定》) (the "Archive Rules"). The new rules support the need of some Chinese companies to seek capital through an overseas listing, but provide more clarity of procedures and practice for firms to follow. The industry also greatly appreciates the removal of historical regulatory uncertainties on the VIE structures.

Global firms have played a critical role connecting global capital markets to China and this has proven to be of value in propelling the China economy forward ever since China initiated its opening-up and reform four decades ago. The engagement of global firms as well as local firms of China in raising capital for Chinese enterprises should continue to be the approach given the efficacy that global firms can bring to the price discovery process, including access to a larger institutional investor base that is broad and diversified across the global markets. However, many of these global firms (comprising our members) have raised some concerns around the new rules, which we highlight below:

- **Onshore Retention Requirement**

ASIFMA members take note of and respect CSRC's emphasis on the importance of preserving state secrets and matters concerning national security based on their reading of the New Filing Rules. Article 9 of the Archive Rules further requires that working papers produced onshore by securities companies and securities service providers in the process of rendering their services related to overseas offerings and listings by domestic companies shall be retained in the Mainland (the "Onshore Retention Requirement"), and where such documents need to be transferred to outside the Mainland, relevant approval procedures stipulated by national regulations shall be followed (the "Transfer Approval Requirement").

ASIFMA members believe that interpretations and clarifications of the Onshore Retention Requirement will better guide securities companies and securities service providers' capacity to comply with mainland regulations, including particularly the below:

- Neither the Archive Rules nor the New Filing Rules currently provides specific guidance on what constitute "working papers produced onshore by securities companies and securities service providers" (证券公司、证券服务机构在境内形成的工作底稿) for an overseas offering and listing under the Onshore Retention Requirement. In practice, due to the movement and involvement of onshore and offshore personnel working on the transaction and locations of where meetings are held, it is extremely difficult in practice to distinguish when "working papers" are "produced onshore" and when they are not, especially where a substantial portion of the records and papers are now often prepared and generated in electronic form, rather than in hardcopy form.

- In addition, some securities companies which render services related to overseas offerings and listings by domestic companies do not have any physical presence and do not maintain any office, system, or server in Mainland China. There is no official premises or practical way for them to retain or store such working papers produced in Mainland China should it be required under the Onshore Retention Requirement.

- International investment banks, securities companies, and their respective personnel are subject to laws, rules, regulations, standards, and codes of conduct in the locations where the overseas offerings and listings are undertaken and in many other jurisdictions which are applicable to their group of companies, as well as their internal policies in respect of record keeping for any offering and listing, for the purpose of disclosure to and cooperation with overseas regulatory authorities to which they are subject. This means that they are required to retain documentation outside of the Mainland.

Recommendation:

In light of the above, it would seem that the securities companies and securities service providers should be able to take a reasonable approach by continuing to observe the local laws, rules, regulations, standards, and codes of conduct in the locations where the overseas offerings and listings take place in maintaining documentation and retaining files and records offshore as necessary to carry out their duties and obligations as required for the overseas offerings and listings in the relevant jurisdictions. ASIFMA recommends interpretations and clarifications of the Onshore Retention Requirement to better guide securities companies and securities service providers' capacity to comply with mainland regulations.

- **Transfer Approval Requirement**

It is of paramount importance for securities companies to be allowed to keep all records of their work performed in the overseas offerings and listings in locations that are within their possession and control (including locations outside of the Chinese mainland), and are readily accessible, in order to ensure compliance with the relevant local laws, rules, regulations, standards, and codes.

Recommendation:

Some market views believed that (i) the Transfer Approval Requirement only applies to those working papers that involve state secrets and matters concerning the national security of the PRC (the "Sensitive Information"), to the extent approval procedure for the transfer or transmission of such Sensitive Information by the securities companies is stipulated under the applicable PRC laws and regulations; and (ii) where Sensitive Information is involved, the domestic issuers must comply with the applicable PRC laws and regulations in their handling of such Sensitive Information, and the securities companies are cognizant of obtaining confirmation from the domestic issuers in respect of their compliance with such laws and regulations. The market would be grateful if PRC regulators may confirm whether such understanding is correct.

- **Cooperation Approval Requirement**

Article 11 of the Archive Rules also provides that, where an overseas securities regulator and a competent overseas authority requests to inspect, investigate or collect evidence from a domestic company concerning its overseas offering and listing, or to inspect, investigate, or collect evidence from the domestic securities companies and securities service providers that undertake relevant businesses for such domestic companies, such inspection, investigation and evidence collection shall be conducted under a cross-border regulatory cooperation mechanism, and the CSRC or other competent Chinese authorities will provide necessary assistance pursuant to bilateral and multilateral cooperation mechanisms. The domestic company, securities companies and securities service providers shall first obtain approval from the CSRC or other competent Chinese authorities before cooperating with the inspection and investigation by the overseas securities regulator or competent overseas authority, or providing documents and materials requested in such inspection and investigation (the "Cooperation Approval Requirement").

Recommendation:

It is the preferred view that the Cooperation Approval Requirement only applies to domestic securities companies and securities service providers, which are subject to the direct supervision and regulation by the CSRC, when they face inspection, investigation, or evidence request by overseas securities regulators or authorities (i.e., this Cooperation Approval Requirement does not apply to any offshore entities within the investment bank or securities companies group or any other overseas securities companies and securities service providers that are not directly regulated by the CSRC). The market would be grateful if PRC regulators may confirm whether such understanding is correct.

1b. Registration-based IPO System Reform

On 17 February 2023, in total 165 revised or new rules and regulations were released by mainly CSRC and stock exchanges to expand the registration-based regime across all listing boards, products and activities. This followed the regime's prior pilot implemented on the SSE STAR Market, SZSE ChiNext Board and BSE respectively one after another since 2019.

The registration-based IPO system aims to reference the experience and practices of the pilot registration system, generally consistent with the STAR Market and ChiNext Board in terms of structure, conditions to offering, information disclosure, approval procedures, and supervisory penalties. With the focus on information disclosure as the theme of regulation, the reform targets to provide more convenience for direct financing, while further enhancing risk prevention and control.

With a long history of approval-based IPO system in China, the newly issued *Administrative Measures for the Registration of Initial Public Offerings of Stocks* (《首次公开发行股票注册管理办法》, the "Administrative Measures") represents a significant change in Chinese primary market activities. It clarifies the different positioning of the main boards, STAR Market, and ChiNext as well as supervisory responsibilities between exchanges and the CSRC. Further, it lays out clear responsibilities of issuers, sponsors, and securities service agencies, including mainly that issuers should ensure accurate and truthful information disclosure and fully disclose foreseeable and material, direct or indirect risks; sponsors should prudently review application documents and take responsibilities; and securities service agencies should be accountable for relevant contents to their professional duty.

The Administrative Measures provide clear requirements with respect to conditions to offering and registration procedures including exchange review, CSRC registration, expected timeline, and transparency in workflow. The accountability system has been enhanced to regulate the activities violating the relevant rules.

ASIFMA members are broadly supportive of the new rules, as they represent a market-oriented development in the Chinese IPO market to improve the price discovery process, as well as to enhance the clarity and transparency of the IPO application review and registration procedures. By extending the successful pilot measures on the STAR Market and ChiNext to the Main Boards of SSE and SZSE, capital raising capabilities of the onshore exchanges will be enhanced while protecting the interests of investors and market stakeholders.

Whilst the IPO market reform is strongly supported by the industry, ASIFMA would like to share the below recommendations to better align the practices among Main Board, STAR Market and ChiNext Board and sync with the global standards.

- **Sponsor Co-Investment Requirements on the STAR Market and ChiNext**

The new rules do not require co-investment by relevant subsidiary of the sponsor institution in IPOs on the main boards. On this basis, ASIFMA would continue to recommend the gradual cancellation of the mandatory co-investment requirements for IPOs on the STAR Market and IPOs of four types of issuers on the ChiNext Board[6], and to ultimately align sponsors' responsibility requirements across all listing boards.

Specifically, the sponsor co-investment requirement for the STAR Market and ChiNext is a unique phenomenon in the Chinese market. ASIFMA would welcome a discussion with the CSRC to better understand the risks which the sponsor co-investment requirement is trying to address and to explore if alternative solutions might be equally or even more effective. Sponsor participation in IPOs typically requires additional scrutiny by overseas stock exchanges and home jurisdiction regulators owing to concerns around potential conflicts of interest.

Recommendation:

To further attract more international market participants to the Chinese mainland IPO market, it may be beneficial to consider if the currently mandatory IPO sponsor co-investment requirement for STAR Market and ChiNext can be removed in a phased manner to become both in line with the main boards as well as with international practice, e.g., Hong Kong regulations exercise caution regarding the independence of underwriters to the issuer, where a declaration to the HKEx of independence shall be made, as well as disclosure of interests; in Singapore, disclosure before the listing of the securities is required if underwriters and connected clients acquire any of the interest in the securities being marketed. The details of our recommendation are as follows:

- First, relax the co-investment requirements on the STAR Market, aligning with the ChiNext practice of implementing such mechanism only on four types of stocks – unprofitable, red-chip structure, weighted voting rights and shares issued at high prices.

- Second, in the four scenarios where co-investment is required, further limit the scope of red-chip companies to those that have not been listed overseas.

- Finally, with the continuous deepening of the registration-based IPO reform, gradually cancel the co-investment requirement on all listing boards in the long-term.

[6] The *Detailed Rules for the Implementation of Securities Issuance and Underwriting Business of the Shanghai Stock Exchange* (《上海证券交易所首次公开发行证券发行与承销业务实施细则》) and the *Detailed Rules for the Implementation of IPO Securities Issuance and Underwriting Business of the Shenzhen Stock Exchange* (《深圳证券交易所首次公开发行证券发行与承销业务实施细则》).

1c. Pricing and Placement Reform

- **Grant more flexibility to issuers and underwriters in the pricing and allocation process**

ASIFMA continues proposing more empowerment of issuers and underwriters in pricing and share allocation in IPOs, and the lift of the minimum preferential allocation ratio for certain institutional investors such as public funds, social security funds, and pension funds. Our members acknowledge that the latest rules raised the minimum ratio from 40% to 70% of off-net shares (网下发行证券) to be preferentially allocated to such institutional investors and added QFIs to the list.[7]

Recommendation:

ASIFMA continues recommending that due consideration should be given to more risk-taking investors. In so doing, securities companies can make pricing and allocation decisions based on the development stage of the issuer, the qualifications and background of institutional investors, quotations, the voluntary commitment of the lock-up period, voluntary deposits, and market conditions. In the meantime, regulators can enumerate the factors that they want issuers and brokers to consider when setting prices, so as to provide certain guidance on pricing behavior. In this way, it is possible to give full play to the pricing function of the market, enable the construction of a market-based pricing mechanism, and facilitate the formation of a more reasonable price discovery mechanism.

- **Remove "top price quote exclusion" rule and special disclosure requirement for pricing higher than the lowest among "the four indicators"**

According to the latest rules, the ≤3% "top price quote exclusion" (最高报价剔除) requirement[8] and special risk disclosure requirement when offering price exceeds the lowest among the "the four indicators" (四个值)[9] in the STAR Market/ChiNext Board apply to Main Board IPOs. Our members maintain that the registration-based IPO regime could narrow the gap between the issuance price of new shares and the secondary market price. Investors will also gradually become aware of the risks and make decisions based on rational judgement. There will thus be less need for underwriters to artificially adjust quotations and prices by eliminating the highest quotations in the long run.

[7] Article 26 of the *Detailed Rules for the Implementation of Securities Issuance and Underwriting Business of the Shanghai Stock Exchange* (《上海证券交易所首次公开发行证券发行与承销业务实施细则》) and Article 25 of the *Detailed Rules for the Implementation of IPO Securities Issuance and Underwriting Business of the Shenzhen Stock Exchange* (《深圳证券交易所首次公开发行证券发行与承销业务实施细则》).

[8] Article 16 of the *Detailed Rules for the Implementation of Securities Issuance and Underwriting Business of the Shanghai Stock Exchange* (《上海证券交易所首次公开发行证券发行与承销业务实施细则》) and Article 14 of the *Detailed Rules for the Implementation of IPO Securities Issuance and Underwriting Business of the Shenzhen Stock Exchange* (《深圳证券交易所首次公开发行证券发行与承销业务实施细则》).

[9] Article 19 of the *Detailed Rules for the Implementation of Securities Issuance and Underwriting Business of the Shanghai Stock Exchange* (《上海证券交易所首次公开发行证券发行与承销业务实施细则》) and Article 16 of the *Detailed Rules for the Implementation of IPO Securities Issuance and Underwriting Business of the Shenzhen Stock Exchange* (《深圳证券交易所首次公开发行证券发行与承销业务实施细则》).

Recommendation:

Therefore, ASIFMA continues to suggest the removal of the "top price quote exclusion" rule and the special disclosure requirement for pricing higher than the lowest among “the four indicators” across all markets and sectors. This will enable investors who quote a reasonable and relatively high price to obtain the placement rather than being excluded.

- **Optimize the strategic placement process**

According to the relevant practices of the STAR Market and the ChiNext Board, strategic investors oftentimes need to sign the strategic investment agreement before knowing the potential issuance price range. In addition, the strategic investment lock-up period stipulated by regulations is longer, resulting in a relatively higher risk exposure of the investment. The lack of key information also often makes it difficult for sophisticated institutional investors to pass the internal approval process, thereby dampening the enthusiasm of investors to participate in strategic placements.

Recommendation:

Therefore, ASIFMA recommends optimizing the strategic placement process. Our members maintain the importance that the strategic investment agreement be signed when / after the issuing price range is determined, so as to ensure the transparency of investment risk exposure and potential returns for investors and increase their enthusiasm and certainty for investments.

Recommendations for Equities – Primary Market
In respect of **Overseas Listing of Domestic Companies:** 1. Clarify the Onshore Retention Requirement to better guide securities companies and securities service providers’ capacity to comply with mainland regulations. 2. Clarify the Transfer Approval Requirements in respect of Sensitive Information. 3. Clarify that the Cooperation Approval Requirement only applies to domestic securities companies and securities service providers. In respect of **Registration-based IPO System Reform:** 4. Remove the currently mandatory IPO sponsor co-investment requirement for STAR Market and ChiNext in a phased manner. In respect of **Pricing and Placement Reform:** 5. Grant more flexibility to issuers and underwriters in the pricing and allocation process. 6. Remove “top price quote exclusion” rule and special disclosure requirement for pricing higher than the lowest among “the four indicators”. 7. Optimise the strategic placement process.

C. Equities - Secondary Market

1. QFI

1a. Key Developments since 2020

Substantial developments have been made to the Qualified Foreign Investor (“QFI”) regime since 2020, including mainly the below:

- **Removal of securities investment quotas**: Both Qualified Foreign Institutional Investors ("QFIIs") and RMB Qualified Foreign Institutional Investors ("RQFIIs") are no longer subject to domestic securities investment quotas under the *Administrative Provisions on Funds for Domestic Securities and Futures Investments by Foreign Institutional Investors* issued by the People’s Bank of China (PBOC) and State Administration of Foreign Exchange (SAFE) on 7 May 2020;

- **Merger of QFII and RQFII schemes**: The QFII and RQFII schemes were formally merged into a single QFI scheme when the long-awaited *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和人民币合格境外机构投资者境内证券期货投资管理办法》) and *Provisions on 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和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》) (the “New QFI Regulations”) were issued in September 2020;

- **Eligible institutions:** Eligibility requirements were substantially relaxed under the New QFI Regulations. Among others, the specific AUM and years of operations requirements for QFIs were removed and replaced with general requirements such as financial soundness, good credit records, experience in securities and futures investment, sound and effective governance structure, internal control, compliance management regime and procedures, and no record of major regulatory penalties in the latest three years or since establishment;

- **Investment scope**: The investment scope of QFIs was substantially expanded to additionally cover, among others, derivatives on bonds, interest rates and foreign exchange on the CIBM, financial futures listed and traded on China Financial Futures Exchange Co., Ltd. (CFFEX), commodity futures contracts listed and traded on approved futures exchanges, options listed and traded on approved exchanges, and private investment funds whose investments fall within the QFI investment scope, i.e., essentially private securities investment funds;

- **Brokers**: QFIIs and RQFIIs were limited to trading through a maximum of three brokers on each of the SSE and SZSE. Moreover, shares purchased through one broker must be sold through the same broker. The New QFI Regulations removed the limit on the number of brokers that QFIs may use but they still need to sell the securities they acquired through the same broker; and

- **BSE started operations in November 2021:** As an enhancement to the investment scope, stocks on BSE have been accessible to QFIs since it started operations on 15 November 2021. More details on BSE and how it compared with the other mainland exchanges can be found in Annex 1 to this Paper.

The aforesaid changes are welcomed by foreign financial market participants and since then the number of QFIs has substantially increased. As of April 2023, CSRC has granted licenses to a total of 768 QFIs (including QFIIs and RQFIIs), among which 266 QFIs were approved after the New QFI Regulations came into effect on 1 November 2020.[10]

Substantial developments have also been made to the Stock Connect regime (see section C.2 below), and please refer to Annex 2 to this Paper for a comparison between the current QFI scheme and Stock scheme.

1b. DVP and Pre-Funding

Delivery vs Payment (DVP) is a core settlement mechanism commonly adopted by most international markets, requiring for settlement of shares at the same time (or on the same day) as cash in order to better protect trading counterparties against settlement risks.

ASIFMA members welcome the DVP reform by CSRC and implemented by CSDC in 2022. Prior to DVP, CSDC delivered shares to investors on T date but did not receive cash settlement until T+1. With DVP in place, settlement risk exposure to CSDC has been mitigated.

However, investors continue to be required to prefund their share purchase transactions, and do not sufficiently share in the benefits of DVP. Pre-funding is generally required for China A-share purchases via brokers as A-share is a no-fail market. Further, QFIs generally have to pre-fund their buy orders by transferring the necessary funds onshore by T-1. However, now with DVP in place to protect CSDC from settlement fails, institutional investors would greatly appreciate the elimination of the current prefunding requirement, so that they too may enjoy the benefits of DVP as well.

The DVP reform is conducive to enhancing the security of the settlement system from the institutional investor perspective and further attracting foreign funds to enter the Chinese market. Removing the prefunding requirement would further enable institutional investors to share in the benefits of DVP and improve the efficiency of fund utilization. This benefit to investors would not compromise the counterparty risk to CSDC with DVP now in place.

[10] List of QFIs, http://www.csrc.gov.cn/csrc/c101900/c1029652/content.shtml.

Recommendation:

We suggest the removal of the pre-funding requirement which would improve asset safety concerns of institutional investors without compromising risk for CSDC and which would improve liquidity.

1c. Post-trade and Regulatory Reporting (Settlement Cycle)

Complementing the need for modern trading technology, post-trade infrastructures modernisation should also be considered and not be left behind as has often been the case in economies across the region. The existence of multiple clearing and settlement infrastructures (China Central Depository & Clearing Co., Ltd. (CCDC), China Securities Depository and Clearing Corporation (CSDC/CSDCC), China Foreign Exchange Trade System (CFETS) and Shanghai Clearing House (SHCH)) covering different sometimes overlapping products makes the Chinese post-trade environment complex and costly considering the different practices, communication channels and protocols that the market participants have to maintain. A mitigating factor to such an environment is the adoption of international communication standards such as the ISO 20022 universal financial industry message scheme and data standards such as the International Securities Instrument Number (ISIN) and the Unified Transaction Identifier (UTI).

Recommendation:

Opening up the China capital market to foreign players and vendors shall enable easier access through international standards and global vendor options. The adoption by China's regulators, clearing houses and institutions of ISO standards for clearing and settlement – and the globally established market practices that have been developed around them – would be hugely convenient both for China's investors establishing a global presence and for international investors expanding their investments into China.

The ISO 20022 data model is also a good flexible base for new technologies like distributed ledger technology (DLT) and APIs to leverage to enable interoperability with messaging standards. This can enable easier fintech entrants into the China post-trade space.

ISO 20022 has also been mandated for derivatives trade reporting in certain Asia-Pacific jurisdictions like Singapore, Hong Kong, Japan and Australia – with go-live expected in 2024. This is in line with development in the EU and US markets. We recommend that the Mainland align with the rest of these Asia-Pacific jurisdictions and ease foreign reporting parties' reporting burdens with standardization.

1d. Multi-broker Model

Under the New QFI Regulations which came into effect in November 2020, the limit on the number of brokers was removed. However, in practice, if a QFI purchases shares through one broker, in essence it cannot sell the shares through another broker due to the following stock exchange rules:

(1) SSE Rules: In accordance with the *Trading Rules of the Shanghai Stock Exchange* and the *Implementing Rules of the Shanghai Stock Exchange on Designated Trading*, each securities account can designate only one broker and participate in securities trading through such broker's dedicated Participant Business Unit ("PBU"). A securities account may not change its designated broker without completing the corresponding change procedures. Such rule is reiterated in the *Guidelines No.1 on the Application of Securities Trading Rules of the Shanghai Stock Exchange for Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors* on October 30, 2020, which provides that "where a QFI opens multiple securities accounts or derivatives contract accounts to participate in the trading of the securities and derivatives of the SSE, each account can only designate one domestic securities company or futures company";

(2) SZSE Rules: Article 4.1.2 of the *Trading Rules of Shenzhen Stock Exchange* provides that the investor may either sell securities through the PBU through which it has purchased such securities, or issue an instruction of custody transfer to the original PBU and sell securities through the new PBU it has transferred into after the completion of the custody transfer.

As a result, the shares purchased through a broker can only be sold through the broker via which the QFI purchased the shares, unless a broker re-designation or custody transfer process is conducted. Such restriction is different from the global practice and the Stock Connect scheme — generally, overseas investors are free to buy or sell any of their stocks through any broker of their choice — and increases the concentration risks of overseas investors, as the investor's investment philosophy and transaction details are easily grasped by one broker. Besides, a single broker may have difficulty in meeting the best execution requirements in terms of research capability and transaction execution capability. This restriction also increases the operation complexity and compliance costs of overseas investors. The aforementioned restriction has become one of the main factors why foreign investors have chosen to utilise the Stock Connect scheme over the QFI scheme.

Recommendation:

Reform the trading rules of SSE and SZSE to allow the multi-broker model. As to the specific improvement measures, the trading system of China B-share or HKEX can be referred to.

1e. SBL

QFI reforms which were enacted in November 2020 permitted participation of QFIs in the securities borrowing and lending (SBL) mechanism in China. This was widely welcomed as a significant step forward to improve liquidity in the secondary market and provide QFI asset owners more accessibility to hedging tools. The lending mechanism has also improved significantly with a move away from fixed pricing terms for lending to variable pricing terms for lending. This evolution is encouraging and it provides for a more dynamic secondary market, greater flexibility for all participants and better returns for long investors both onshore and QFIs.

Still, QFIs' participation in SBL is limited by the uptick rule under relevant exchange rules[11], and the industry suggests a review of such rules. The current uptick rules require that as long as there are borrowed shares held by "an investor" (投资者), all of that investor's sell orders in that stock which are held through "securities accounts owned or controlled" by the investor (其所有或控制的证券账户) must be sold at a price not lower than the most recent execution price of that stock "except for the portion in excess of the borrowed shares" (超出融券数量的部分除外).

Recommendation:

The industry would welcome clarifications on how the aforesaid uptick rule applies to QFIs. Particularly,

- Offshore institutions like QFIs may operate multiple client accounts and also manage proprietary positions. Such accounts are essentially segregated, and thus the industry wonders whether they have to be deemed as "securities accounts owned or controlled" by the investor;

- Further, the industry would recommend the segregation of different trading desks. For many offshore institutions, even within the same entity, there may be a number of independent trading desks which may engage in separate investment strategies simultaneously.

The industry considers the above clarifications as reasonable because a rigid interpretation of the uptick rule would impede the ability of the long holder to trade and would not be in the spirit of the market. The segregation of client accounts and proprietary positions, and segregation of different trading desks, would add fluidity to the market and fairness to all investors, without causing risks of malicious short-selling.

2. Stock Connect

The Stock Connect programme was first conceptualised by China as another channel for opening up China's capital market. In November 2014, mutual market access between the SSE and HKEX was established representing the first time that two stock exchanges have linked up in this way, followed in December 2016 by a similar link between HKEX and SZSE. The typical route for investors to buy stocks in another jurisdiction is through a relationship between the broker in its originating jurisdiction and a correspondent broker in the target jurisdiction. Stock Connect, by contrast, is a direct link between exchanges. The link enables brokers who are members of the HKEX to execute orders through a link to the SSE or SZSE, rather than to broker members of the SSE and SZSE.

[11] Article 12 of the *SSE Detailed Rules for the Implementation of Margin Trading* (《上海证券交易所融资融券交易实施细则》) and Article 2.10 of the *SZSE Detailed Rules for the Implementation of Margin Trading* (《深圳证券交易所融资融券交易实施细则》).

As the Mainland's capital account is restricted, foreign investors are not allowed to open accounts at Mainland financial institutions except for specific approved purposes. Stock Connect enables Chinese authorities to allow money to flow in and out of shares through a single controllable conduit. Investors must purchase offshore RMB ("CNH") in Hong Kong or have their broker arrange a purchase on their behalf. When a foreign investor sells shares through Stock Connect, the RMB proceeds are delivered in Hong Kong. Stock Connect creates a "closed loop", segregating the RMB used to buy shares from the rest of the Chinese economy.

Stock Connect allows any investor in the world, institutional or retail, access to A-shares. There are no lock-up periods or repatriation restrictions for Stock Connect.

2a. Stock Connect Trading Universe

- **Eligible Stocks**

Unlike QFI which has a much broader investment scope such as all A-shares, Stock Connect's investment scope is limited to a smaller pool of eligible A-shares listed on SSE and SZSE. The scope of eligible stocks under the Stock Connect programme has been substantially expanded as from 13 March 2023 upon the implementation of relevant SSE and SZSE rules (i.e., the *Implementation Measures of the Shanghai Stock Exchange for Shanghai-Hong Kong Stock Connect Business (2023 Revision)* (《上海证券交易所沪港通业务实施办法（2023 年修订）》) and the *Implementation Measures of Shenzhen Stock Exchange for the Shenzhen-Hong Kong Stock Connect (Revised in 2023)*) (《深圳证券交易所深港通业务实施办法（2023 年修订）》) and *Rules of the Exchange* of SEHK (Chapter 14A and 14B). As of 15 June 2023, 1268 out of the 2263 stocks listed on SSE (increased by 674) and 1374 out of the 2830 stocks listed on SZSE (increased by 480) are eligible for northbound trading under Stock Connect.[12] The key changes regarding eligible stocks for northbound trading include mainly the below[13]:

Table 1: Expansion of SSE/SZSE Eligible Stocks

	Shanghai Stock Connect	Shenzhen Stock Connect
Eligibility		

[12] List of SSE Securities/China Connect Securities and List of SZSE Securities/China Connect Securities, https://www.hkex.com.hk/Mutual-Market/Stock-Connect/Eligible-Stocks/View-All-Eligible-Securities?sc_lang=en.
Market Overview of SSE, http://www.sse.com.cn/market/view/.
Market Overview of SZSE, http://www.szse.cn/market/overview/index.html.

[13] The *Implementation Measures of the Shanghai Stock Exchange for Shanghai-Hong Kong Stock Connect Business* (《上海证券交易所沪港通业务实施办法》), the *Implementation Measures of Shenzhen Stock Exchange for the Shenzhen-Hong Kong Stock Connect* (《深圳证券交易所深港通业务实施办法》) and the *Rules of the Exchange* of SEHK.

<table>
<tr><th></th><th>Shanghai Stock Connect</th><th>Shenzhen Stock Connect</th></tr>
<tr><td colspan="3">Criteria</td></tr>
<tr><td>Benchmark Indexes</td><td>- expanded from SSE 180 Index and SSE 380 Index to SSE A-share Index
- expanded from large and mid-cap stocks on the SSE to also mid and small-cap stocks
- stocks available in each sector will no longer be subject to quantity restrictions</td><td>- expanded from Shenzhen Component and SZSE Small/Mid Cap Innovation Index to SZSE Composite Index
- constituent stocks of the benchmark index basically cover all stocks listed on SZSE</td></tr>
<tr><td>Inclusion Criteria</td><td colspan="2">A constituent stock of the SSE A Share Index / SZSE-listed A shares that is a constituent stock of the SZSE Composite Index fulfils:
- a daily average market capitalization in the last six months of RMB5 billion or above;
- a daily average turnover in the last six months of RMB30 million or above;
- ratio of trading suspension days lower than 50% in the last six months; and

- additional criteria for the first time inclusion of a stock with Differentiated Voting Rights (DVR stock):
o listed on SSE/SZSE for no less than six months and twenty SSE/SZSE trading days;
o a daily average market capitalization in the last 183 calendar days of RMB20 billion or above;
o an aggregated turnover in the last 183 calendar days of RMB6 billion or above; and
o never been publicly censured by SSE/SZSE due to any breach of any requirements under the SSE/SZSE rules applicable to DVR stocks

- A+H shares

provided that:
(i) they are not traded on SSE/SZSE in currencies other than RMB; and (ii) they are not under risk alert (ST/*ST companies or shares subject to the delisting process, etc.)</td></tr>
<tr><td>Eligible Stocks for Sell-only</td><td colspan="2">At any half-yearly review, an eligible stock (which is non-A+H stock) which met any of the following criteria will become a sell-only stock:
- a daily average market capitalization in the last six months has fallen under RMB4 billion;
- a daily average turnover in the last six months has fallen under RMB20 million; or</td></tr>
</table>

	Shanghai Stock Connect	Shenzhen Stock Connect
	- ratio of trading suspension days accounts for 50% or more in the last six months	
Review Mechanism		
Adjustment Mechanism	**Half-yearly Review** - at the end of May and November each year, to inspect constituent stocks of the SSE A-share Index/A shares of the SZSE Composite Index - list of eligible stocks shall be effective in June and December respectively **Monthly Review** - at the end of each month, to inspect (1) stocks newly included in the SSE A-share Index/SZSE Composite Index; and (2) stocks released from risk alert in the calendar month, for that month - list of eligible stocks shall be effective in the following month	

Due to the removal of some of the SSE and SZSE stocks from the indices which make up the eligible stocks under Stock Connect, these stocks can only be sold. If all A-shares are made eligible under Stock Connect, then market participants would not have to worry about stocks being removed from the eligible list and investors be subject to sell-only restrictions of such stocks.

Recommendation:

Foreign investors would like to see the Stock Connect investment scope to be expanded to all A-shares as soon as possible and in the future to on par with the QFI investment scope. A greater variety of products and features will improve pricing and liquidity in onshore capital markets by allowing offshore investors to better hedge trades, manage trading costs, and execute more complex trading strategies. These tools will be key to attracting inflows from foreign institutional investors looking to increase and hedge their exposures to onshore capital markets. We look forward to these changes being implemented as soon as possible.

- **Inclusion of ETFs**

Before the recent expansion of eligible stocks under Stock Connect, Exchange Traded Funds (ETFs) were included in the Stock Connect from 4 July 2022. The eligibility requirements for ETFs included for Northbound and Southbound Stock Connect trading are set out below[14]:

Table 2: Eligibility Requirements for Stock Connect ETFs

	Eligibility for Northbound Mainland ETFs	Eligibility for Southbound Hong Kong ETFs
Daily average AUM in the last six months	RMB 1.5 billion or more	HKD 1.7 billion or more
Trading Currency	RMB	HKD
Minimum listing duration of the ETF	Six months	
Type of ETF	All types	All types but synthetic ETF or Leveraged and Inverse Product
Benchmark index tracked by the ETF	Launched for one year or more	
Minimum weighting of stocks in benchmark index	90% or more in SSE/SZSE-listed A shares	90% or more in SEHK-listed stocks
Minimum weighting of Stock Connect constituent stocks in benchmark index	80%	- 70% for HSI, HSCEI, HSTECH and HSHKBIO - 80% for other indices
Constituents in benchmark index	- **Broad-based indices**: A constituent stock must be no more than 30% of index's weighting - **Non-broad-based indices**: (1) have at least 30 constituent stocks; (2) each constituent stocks' weighting does not exceed 15%; (3) top five weighted constituents' total weighting does not exceed 60%; and (4) constituent stocks comprising of over 90% of the index's weighting must rank top 80% by Average Daily Turnover (ADT) on its exchange	

[14] Articles 25 and 76 of the *Implementation Measures of Shenzhen Stock Exchange for the Shenzhen-Hong Kong Stock Connect* (《深圳证券交易所深港通业务实施办法》) and Articles 26 and 76 of the *Implementation Measures of the Shanghai Stock Exchange for Shanghai-Hong Kong Stock Connect Business* (《上海证券交易所沪港通业务实施办法》).

The initial list of eligible ETFs includes 83 Mainland ETFs[15] and 4 Hong Kong ETFs[16]. This was increased to 97 Mainland ETFs (60 SSE-listed and 37 SZSE listed)[17] and 5 Hong Kong ETFs after the first review in November 2022 for Southbound and January 2023 for Northbound. Such reviews take place every six months. However, as of March 2023, the total trading volume of Mainland ETFs through Stock Connect represented only 0.37% of the total Northbound turnover while the total trading volume of Hong Kong ETFs represented about 5% of the total Southbound turnover.

Even though the inclusion of the ETFs under Stock Connect opened new opportunities for investors accessing Mainland and Hong Kong ETFs, the access thereto is limited due to, among other things, the ETF eligibility requirements. As of the end of 2022, the AUM of the eligible Northbound ETFs under Stock Connect represented about 4% of China's total ETF market. While the AUM of the eligible Southbound ETFs represented about 52% of the Hong Kong ETF market, it is limited to five very large ETFs out of the 145 ETFs in Hong Kong, with one of the five accounting for 35% of the total AUM.

Prior to the inclusion of ETFs in the Stock Connect which allows investors to trade ETFs listed in the other market (i.e., Mainland or Hong Kong), China had introduced cross-listings of ETFs, initially between SSE and Tokyo Stock Exchange (TSE) in June 2019 followed by cross-listings of ETFs between SSE/SZSE and SEHK, SZSE and TSE, and SZSE and Singapore Exchange (SGX). Unlike ETFs under Stock Connect, under the ETF cross-listing schemes, foreign investors can invest in TSE-, or SEHK- or SGX-listed ETFs that invest 90% or more of their assets in an ETF listed in the Mainland while Mainland investors can invest in similar ETFs listed on SSE or SZSE which invest more than 90% of their assets in an ETF listed in Japan, or Hong Kong or Singapore. As of the end of 2022, the SSE-TSE link has 4 SSE ETFs and 5 TSE ETFs cross-listed on the other market, while the other links have only one or two ETFs cross-listed on the other market. One reason why cross-listings of ETFs have not been successful is because it involves a fund-of-funds structure which carries additional costs.

Recommendations:

Given the increasing interest in ETFs in both the Mainland and Hong Kong, expanding the scope of eligible ETFs will attract further investment in ETFs and promote competition among ETF issuers, which will ultimately be in the best interest of investors.

Accordingly, we recommend that the scope of ETFs be expanded to include all ETFs listed in the Mainland and Hong Kong whose underlying exposures consist of a majority of Stock Connect eligible stocks. Such an expansion will not only increase cross-border capital flow through ETFs but also boost trading in underlying stocks via the Stock Connect.

[15] Initial List of ETFs Eligible for Northbound Trading, https://www.hkex.com.hk/Mutual-Market/Stock-Connect/Reference-Materials/Inclusion-of-ETFs-in-Stock-Connect?sc_lang=zh-HK.
[16] Initial List of ETFs Eligible for Southbound Trading, http://www.sse.com.cn/services/hkexsc/disclo/announ/c/c_20220628_5704774.shtml.
[17] List of Eligible Securities under Stock Connect, https://www.hkex.com.hk/Mutual-Market/Stock-Connect/Eligible-Stocks/View-All-Eligible-Securities?sc_lang=zh-HK.

For example, while keeping all other eligibility criteria the same, the expansion of the scope of benchmark indices could potentially increase the total number of ETFs and AUM eligible under the ETF portion of Stock Connect as follows:

ETF listing venue	# of eligible ETFs		AUM of eligible ETFs (billions)	
	Current	After expansion	Current	After expansion
SSE	53	74	RMB 497	RMB 600
SZSE	30	44	RMB 143	RMB 246
HKEX	5	13	HKD 200	HKD 263

**These estimates are based on data as of 30 November 2022, including all currency counters of the ETFs where applicable, and on the assumption that Stock Connect eligible securities make up the majority of the underlying securities of broad-based indices providing exposure to HK and/or the mainland.*

Separately, removing the minimum AUM requirement or lowering it to HKD 500 million for Southbound ETFs and RMB 440 million for Northbound ETFs will also allow a wider range of ETFs to be eligible under the Stock Connect. To a certain extent, maintaining the AUM requirement could ensure the liquidity of the ETFs. However, the liquidity of an ETF ultimately comes from the underlying index and is agnostic to fund size as each investor of each unit/share of an ETF gets the same slice of the index. Therefore, removing or lowering the AUM requirement will not cause liquidity issues.

ETFs are different from single stock securities as ETFs are fund products which may have differences in fees, hedging, liquidity, etc. even if they may have similar exposures or track the same index. Thus, it is important for ETF issuers to be able to educate end investors about these nuances and differences of their ETFs as opposed to stocks. This can be done by creating a framework where ETF managers whose ETFs are included under the Stock Connect can educate investors about their products.

2b. Stock Connect Holiday Trading

When Stock Connect was launched in 2014, due to different holiday arrangements and settlement cycles between the mainland and Hong Kong, some trading days preceding certain holidays were closed. In August 2022, CSRC and the SFC issued a joint announcement to launch the enhancement of the trading calendar of the Stock Connect allowing Stock Connect trading on all the days which are trading days in both markets. According to the calculation of the CSRC, after the trading calendar is enhanced, it is expected to reduce the number of days that currently cannot be traded by about half. Some specific working arrangements were also set up between clearing corporations in both mainland China and Hong Kong (i.e. CSDC and HKSCC) during the added trading days. Exchanges and clearing corporations in both mainland and Hong Kong will make adjustments to clearing and settlement arrangements, and equity registration dates, and formulate corresponding risk management measures.

An illustrative example for trading and settlement calendar for northbound trading after the adjustment is shown below[18]:

Figure 1: Example of Updated Stock Connect Trading and Settlement Calendar

Northbound	Hong Kong	Mainland	Trading Day (T day)	Securities Settlement (for T day's trades)	Money Settlement (for T-1 day's trades)
5 May 2022 (Thu)	Business Day		✓	✓	✓
6 May 2022 (Fri)	Business Day		✗ -> ✓	✗ -> ✓	✓^
9 May 2022 (Mon)	Public Holiday	Business Day	✗	✗	✗
10 May 2022 (Tue)	Business Day		✓	✓	✓#

^ *Process money settlement for China Connect Clearing Participants ("CCCP") with net payable Continuous Net Settlement ("CNS") money positions in regard to their Northbound China Connect Trades conducted on T day (i.e. 6 May 2022), if any.*
# *Process money settlement for CCCPs with net receivable CNS money positions in regard to their Northbound China Connect Trades conducted on previous T day (i.e., 6 May 2022), if any and also process money transactions in relation to nominee's activities conducted on or before the first Hong Kong business day after the Hong Kong public holiday (i.e., from 9-10 May 2022) with respect to SSE/SZSE Securities.*

Source: HKEX

Further to the joint announcement by CSRC and the SFC, SSE, SZSE and HKEX have issued notices to specify the actual trading days[19]. The additional trading days in 2023 are illustrated as follows:

Table 3: Additional Stock Connect Trading Days in 2023

Southbound Trading	Northbound Trading
April 27 (Thursday)	
April 28 (Friday)	
	25 May (Thursday)
June 20 (Tuesday)	
June 21 (Wednesday)	

[18] Trading Calendar Enhancement for Stock Connect FAQ, https://www.hkex.com.hk/-/media/HKEX-Market/Mutual-Market/Stock-Connect/Reference-Materials/Trading-Calendar-Enhancement-for-Stock-Connect/FAQ-for-Trading-Calendar-Enhancement-for-Stock-Connect.pdf.
[19] For more details, please refer to the *SSE's Notice on Relevant Arrangements for the New Hong Kong Stock Connect Trading Days under the Shanghai Hong Kong Stock Connect in 2023* (《关于 2023 年沪港通下新增港股通交易日有关安排的通知》), *SZSE's Notice on the Arrangements for the New Hong Kong Stock Connect Trading Days in 2023 and Updating the Hong Kong Stock Connect Trading Days under the Shenzhen Hong Kong Stock Connect in 2023* (《关于 2023 年新增港股通交易日及更新 2023 年深港通下的港股通交易日有关安排的通知》) and the HKEX's Circular on *Launch of Trading Calendar Enhancement for Stock Connect* (《实施优化互联互通交易日历》).

September 27 (Wednesday)	
September 28 (Thursday)	
	October 20 (Friday)
	December 22 (Friday)

As stated by the CSRC[20], the enhancement of the trading calendar of the Stock Connect can better meet the reasonable needs of onshore and offshore investors to participate in the allocation of equity assets in the two capital markets, enhance the attractiveness of the two capital markets and consolidate the status of Hong Kong as an international financial center.

Recommendation:

Foreign investors would like to see the Stock Connect trading calendar to be expanded to all market trading days on the host market.

There are still 4-5 days per year where QFI trading is open yet northbound Stock Connect is closed due to Hong Kong being on public holiday. We would thus request the completion of work to align the holiday trading days between QFI and Stock Connect. Finalizing the alignment of QFI and Stock Connect holiday trading days would be achieved by enabling Hong Kong holiday trading through northbound Stock Connect.

2c. SBL

Under the Rules of the Exchange of SEHK, Rules 14A16(5) to (7) and Rules 14B16(5) to (7), only Exchange Participants (i.e., CCASS participants) and Qualified Institutions (i.e., funds, unit trusts or collective investment schemes that are managed by persons licensed or registered to carry out Type 9 (asset management) regulated activity in Hong Kong) may engage in SBL under Stock Connect. However, these participants are not ordinarily in the business of Securities Lending as evidenced by the lack of SBL activity registered through Stock Connect since its inception. The industry believes that broadening participation in Stock Connect Northbound SBL will improve liquidity and strengthen market resilience. Greater liquidity will reduce market volatility and support long-term price stability to the benefit of wider China markets.

Recommendation:

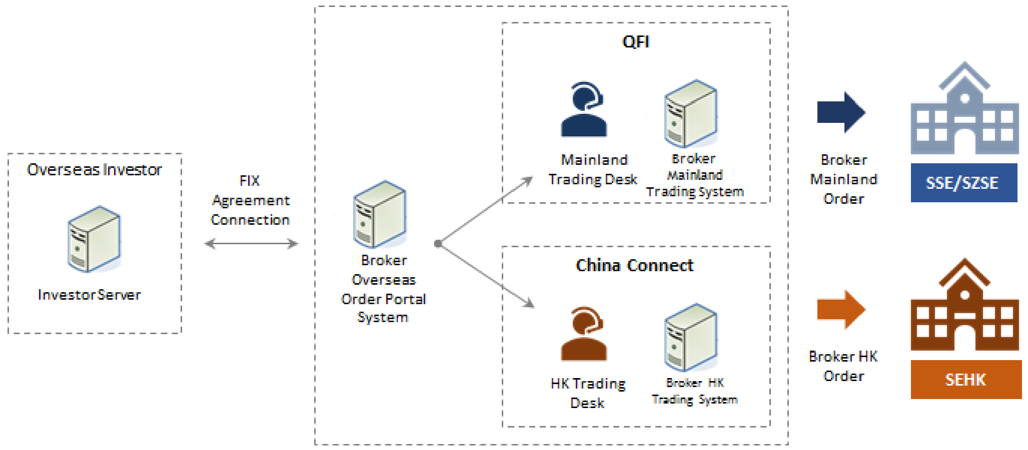
The industry encourages relevant authorities to include affiliates of Exchange Participants and Qualified Institutions as eligible SBL participants, and to expand the category of Qualified Institutions to encompass accredited and regulated institutions such as Agent Lenders and Custodians as many asset managers outsource their stock lending activities to such agents.

[20] Announcement of CSRC on Launch of Trading Calendar Enhancement for Stock Connect, http://www.csrc.gov.cn/csrc/c100028/c7161565/content.shtml.

2d. Onshore Trading Desk to Manage Northbound Orders

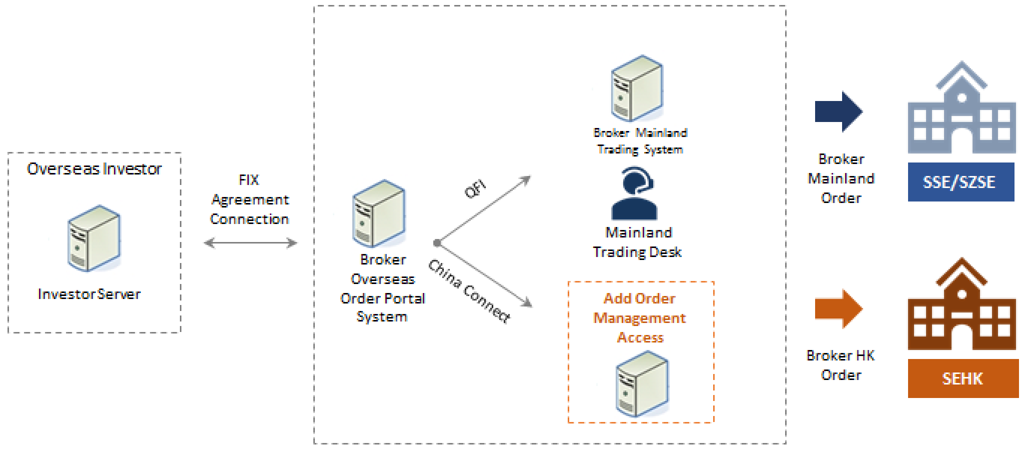
International investors usually access China A-share markets via both QFI and Stock Connect, and it's common for such investors to consider and demand for overall risk control and management across the two channels. For example, an investor could be buying 'stock A' via both channels at the same time, and the investor would like to keep its aggregate shareholding in 'stock A' across the two channels below a certain percentage. Assuming the investor uses a broker that has both onshore and offshore trading desks, currently, the investor's QFI and Stock Connect orders are managed by that broker's onshore trading desk and offshore trading desk, respectively:

Figure 2: Status Quo – Mainland and HK Traders Handling QFI and China Connect Orders Respectively



Onshore and offshore teams would need to manually coordinate with each other to control the pace and manage orders across the two channels. We suggest allowing Mainland trading desks to handle Hong Kong trading desks' northbound Stock Connect orders:

Figure 3: Proposal – Mainland Traders to Handle Both QFI and China Connect Orders



The ability to allow one single onshore team to manage and surveillance the orders would:

- allow better efficiency and productivity to have one single team managing all A-share related orders;
- allow better risk management and surveillance. The onshore team is close to local markets and has the first-hand information to react and manage if there is any contingency;
- promote fair trading and better execution performance with one single team managing both channels;
- facilitate developing Mainland asset management talent.

Recommendation:

We would appreciate it if regulators could issue clear guidance that brokers' onshore trading desks are allowed to manage Stock Connect orders on behalf of offshore affiliates.

2e. Bilingual Stock Connect Rules of SSE/SZSE

As of the end of May 2023, on the websites of SSE and SZSE, major Stock Connect rules of SSE and SZSE are published and available only in Chinese, including the *Implementing Measures of the Shanghai Stock Exchange for the Shanghai-Hong Kong Stock Connect (Revised in 2023)* (《上海证券交易所沪港通业务实施办法（2023 年修订）》) and the *Implementing Measures of the Shenzhen Stock Exchange for the Shenzhen-Hong Kong Stock Connect (Revised in 2023)* (《深圳证券交易所深港通业务实施办法（2023 年修订）》).

However, it is notable that the northbound Stock Connect scheme is specifically designed to attract international investors to invest in the Shanghai- and Shenzhen-listed stocks via Hong Kong as the entry point (through the Hong Kong Exchange) without the need to have a presence in the Mainland. Therefore, it is important for northbound Stock Connect rules to be published bilingually in both Chinese and English because international investors are not expected to be proficient in the Chinese language and the official languages in Hong Kong are Chinese and English.

Ideally, these SSE and SZSE rules shall be published simultaneously in both languages and both are binding. For such purpose, the three exchanges should coordinate and arrange for the timely and consistent translation.

Even if the English version is not binding, both versions should be issued and available before the rules come into effect (and preferably at the same time). Also, the English version/translation should come from one official source so that all investors are put on an equal footing – the market cannot function properly with multiple English translations coming from multiple unofficial sources. At the very least, we urge all northbound Stock Connect rules to be available bilingually prospectively.

Recommendation:

We recommend issuing both Chinese and English Stock Connect rules and ideally the English version shall also be binding. At the very least, the English translation of Stock Connect rules shall be available prospectively on the official websites of SSE and SZSE.

2f. Aggregation of Positions Across Custodians

We welcome the Master Special Segregated Account (Master SPSA) service launched by HKEX in July 2020, which allows pre-trade checking to be conducted at a fund manager, or aggregate level, to help increase their operational efficiencies while maintaining the same post-trade settlement processes at the individual SPSA level for consistency.[21]

We suggest adopting the similar approach to allow aggregation of positions across custodians. Due to the nature of set up in the Hong Kong market, investors/beneficial owners may have accounts directly at a custodian but may also open up other accounts at triparty agents for financing purposes (under SPSA accounts). For such investors, managing positions for same-day trades then becomes operationally burdensome and difficult from a trading perspective. One same investor's positions should be (like in many other markets) aggregated to enable efficient same-day trades of its assets across custodians. Not doing so limits the liquidity of these assets making participation more expensive, particularly in smaller names/where investors have high volumes of these assets.

[21] HKEX to Launch Master SPSA Service on 10 July, https://www.hkex.com.hk/News/News-Release/2020/200709news?sc_lang=en.

As to the concern over investor ID transparency, proper investor ID identification measures, such as the Northbound Investor ID Model, helps to essentially address such concern and verify the same beneficial owner.

Recommendation:

We suggest that Mainland regulators work with HKEX to allow Stock Connect investors to aggregate positions across accounts opened at different custodians at the same beneficial owner level (similar to the Master SPSA service which allows aggregating positions across underlying funds at the fund manager level). Investors may have multiple accounts, and allowing them to manage their inventory across accounts to meet trade obligations helps to achieve efficient and stable trading. If a pre-sale check is still required, this could be done at the aggregate level.

3. Short Swing Profit Rule

The *Securities Law* which took effect in March 2020 kept the requirement commonly known as the "short swing profit rule" which requires, among others, profits made by a shareholder who holds 5% or more of the shares of a listed company by selling its shares in the listed company within six months of purchasing them or by purchasing shares in the listed company within six months of selling them be disgorged to the listed company[22]. We understand this requirement is intended to establish a precautionary and deterrent effect against potential insider trading by shareholders as well as other persons subject to this rule.

However, the *Securities Law* does not provide for how a shareholder's shareholding in a listed company is to be calculated for purposes of the short swing profit rule. Aggregation of shareholdings of a shareholder and persons "acting in concert" with it is often required based on various regulations issued by the CSRC, such as the *Listed Company Takeover Measures* which were last revised in March 2020[23] and the New QFI Regulations[24]. Hence, if an asset manager or asset manager group manages multiple funds and/or client mandates, it may have to aggregate the shares of all the funds and client mandates that it manages and over which it exercises voting rights as all such funds and client mandates may be considered to be "acting in concert".

Currently, there is an exemption for a domestic public fund's shareholding to be calculated separately at the fund level and need not be aggregated with other shareholdings at the fund manager level for purpose of the short swing profit rule. However, it is unclear if such exemption applies to foreign public

[22] Article 44 of the *PRC Securities Law*.
[23] For example, Article 13 of the *Listed Company Takeover Measures*.
[24] Article 16 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和人民币合格境外机构投资者境内证券期货投资管理办法》).

or retail funds or private funds. As a result, many global asset managers currently limit the individual holdings of each of the funds and/or client mandates that they manage so that in the aggregate the shareholdings of all of them in a listed company do not exceed the 5% shareholding threshold that would trigger the short swing profit rule.

It was reported in October 2022[25] that CSRC is working on a similar exemption for foreign public funds so that the shareholdings in a listed company of such funds will be treated the same way as domestic ones for purposes of the short swing profit rule. We look forward to CSRC confirming the foregoing.

Recommendation:

Investment managers who manage assets for different funds or client mandates are generally not insiders nor are they privy to inside information even where their percentage of shareholding in a listed company, when aggregated across all clients and/or funds managed by them and their group, exceeds 5%. We suggest that China can treat all investment managers (including offshore ones) the same way as domestic public funds and exempt them from the short swing profit rule and look at the shareholdings of funds and/or clients that are managed under separate agreements by the same asset manager separately and not require such shareholdings to be aggregated at the fund manager level. This would also be consistent with the approach in many other jurisdictions.

4. Access to Onshore Derivatives

Foreign investors applaud the expansion of onshore derivatives access to QFIs to facilitate better hedging and investment risk management. But, given the increasing allocation to Chinese assets and the need for investors to hedge their risks, the foreign investment community would like to recommend PRC regulators consider the following to further open up the market.

4a. Accessibility to Onshore Derivatives by QFIs

- **Types of Derivative Products**

QFIs have been permitted in principle to access various types of derivative products. Currently, QFIs may trade stock index futures and options on CFFEX (4 futures and 3 options currently, covering SSE 50 and CSI 300/500/1000)) and specified commodity futures and options. Bond futures traded on CFFEX and ETF options on SSE/SZSE are still not available for trading by QFIs. These products are still pending the CSRC's approval upon the exchanges' application. We also welcome creation of more listed onshore derivatives for hedging (e.g., index products covering ChiNext and STAR and single stock options – see section 4c. below for more discussions on single stock options).

- **Hedging Restrictions for CFFEX Index Futures and Options**

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[25] Shanghai Securities News, CSRC Working on Specific Short Swing Profit Rule Applicable to Foreign Investors, https://news.cnstock.com/news,yw-202210-4968198.htm.

We welcome constant efforts by CFFEX to improve its hedging requirement. Still, QFIs are subject to hedging requirements in respect of, e.g., notional value of hedge positions and turnover of hedging transactions, and must apply with CFFEX for hedging quota.

The foresaid restrictions can prevent QFIs from fully hedging their entire portfolio risk and the prior quota application requirement hinders QFIs' ability to transact immediately or otherwise execute trading or portfolio opportunities as they occur.

ASIFMA respectfully requests considering easing or even ideally removing the hedging requirement and/or the trading limits for those QFIs to the extent comparable with certain types of PRC domestic investors that are not subject to the hedging requirement.

4b. Accessibility to Onshore Derivatives by Stock Connect/Other Offshore Investors

Except for QFIs, offshore investors including those trading under the Stock Connect scheme are currently not granted access to PRC onshore derivative products on CFFEX. While the industry appreciates that offshore investors can access offshore derivative products (e.g., the SGX FTSE China A50 index futures), the correlation of offshore derivative products with PRC onshore assets is not as strong for investors as onshore derivative products would be. It would be ideal if the onshore derivative products on CFFEX could be specified by CSRC pursuant to the *Interim Administrative Measures for Trading in Specified Futures Varieties in China by Foreign Traders and Foreign Brokerage Agencies* (《境外交易者和境外经纪机构从事境内特定品种期货交易管理暂行办法》) to be open for trading by foreign investors without necessarily needing to secure a QFI license.

4c. Future Product Developments – SSOs

We would suggest for Mainland exchanges to start listing single stock options (SSOs) to satisfy market demand and build the SSO market from the ground up.

Most major global derivatives exchanges offer SSOs to investors. For example,

- The US is the largest SSO market with option listings of more than 600 underlying cash securities. In the US, the trading volume in equity options (excluding ETF options) is roughly 22 million contracts per day, or 5.6 billion contracts for 2022. The estimated daily average trading turnover in SSOs is around USD600 billion in notional terms;

- In the APAC, India and Hong Kong also have active SSO markets, followed by Australia;

- Other APAC markets such as Taiwan, Korea, and Japan also offer equity options.

Such a proposal is beneficial to China’s financial market from the following perspective:

- SSOs are a staple in global financial markets, and a useful tool for investors to manage their risks (e.g., long stock portfolios) or gain exposure to China's economic growth. The benefits associated with SSOs are similar to the ETF options already available on China's stock exchanges. For example:
  - Enhanced investment flexibility and returns, including lower upfront investment which improves return on capital, and limited risk for various strategies.
  - Tailored hedging and risk management solutions for individual underlying stocks;

- Investors globally can access a wider range of investment opportunities, which lead to more capital investment into China and increased market efficiency;

- By developing an SSO market, China can fill the gap in its Financial Market Infrastructures (FMIs) and better align with global market offerings;

- This will promote greater institutional investor participation in the Chinese market. Institutional investors often require more sophisticated risk management tools, and SSOs can provide this. It can then lead to a more stable and mature market, which can benefit both investors and the wider economy.

Recommendations:

We recommend:

- diversifying derivative product suite (e.g., bond futures and ETF options) accessible to QFIs to further expand the portfolio of available hedging instruments onshore;

- removing the hedging-only restriction or increasing flexibility on hedging quota calculations;

- providing offshore investors without a QFI license, including those under the Stock Connect scheme, access to PRC onshore derivative products;

- starting listing SSOs.

Reducing restrictions on international access is beneficial to China's financial market from the following perspectives:

- <u>Boosting economy growth and economic ties</u>: Product scope expansion and access relaxation will deepen China's financial markets and increase the availability of investment instruments to market participants. This will attract further investments into China by foreign investors and boost long term economy growth. This can help to enhance China's reputation as a global economic leader and foster stronger economic ties with other countries;

- Meeting market demand: Equity derivatives options are a useful tool for building a diversified portfolio and the removal of the "hedging purpose" restriction allows investors to use options more flexibly to meet their investment objectives. Reducing restrictions on international access can also help to level the playing field for foreign investors, who may currently face more barriers to investing in China than domestic investors;

- Improving market liquidity: The removal of the "hedging purpose" restriction is expected to increase market liquidity by attracting more investors to the options market. Greater liquidity in turn makes it easier for investors to enter and exit positions, and can reduce the cost for portfolio management and help to reduce volatility in the underlying assets.

5. Block Trades

A block trade is a transaction between two or more parties for the sale/purchase of a significantly large number of shares in a specific stock (from a value and/or average daily volume perspective). Without an efficient block trade reporting mechanism, these respective orders would likely result in significant market impact and volatility to the market order book. Block trading is frequently utilised by institutional investors (regardless of domicile) in order to transact more efficiently, thereby reducing impact costs (typically the largest component of total transactions costs) and helping to achieve their strict best execution obligations to ultimate clients (who are often retail in nature).

This block trading mechanism is currently not available to participants of Stock Connect who can only trade in auction market. This limits liquidity for both domestic and foreign participants as many Stock Connect participants who can offer liquidity do not have a QFI license and hence they are unable to access the block trading mechanism in mainland exchanges in general. Instead, these participants have to sever the block into a number of orders in smaller quantities for execution, which is inefficient, easily leading to price slippage, signalling risk, and information leakage.

The ability to transact large block trades with minimal slippage and interference is a key feature of equity markets around the globe. Block trades enable institutional investors to adjust their portfolios more efficiently therefore increasing the attractiveness of markets where such trades are allowed. Block trading is equally important for foreign investors investing through northbound trading so it would be helpful if this is made available to them as well. Stock Connect participants are a large universe and can provide more liquidity in the block trading facility; additionally, they may leverage block trading to facilitate trading strategies, client facilitation and minimize closing auction strain on index rebalancing days. Enabling block trading will encourage more institutional investors to participate A-share markets through Stock Connect.

A phased approach could be adopted to provide Stock Connect participants access to the block trading mechanism. For phase 1, the industry suggests building a separate, reciprocal block trading mechanism to allow block trading between Stock Connect participants, which can be a framework similar to that of the onshore block trading mechanism (such as adopting the same volume/value threshold, price band, etc.). Block trading between foreign participants may also offer a better framework for them to manage limitation on foreign ownership. There would not be a material issue for reporting related obligations under the block trading mechanism as participants' shareholding positions are already accessible to the regulators per current Stock Connect agreements, and foreign investors should be comfortable with sharing trading data on a daily basis post block trade if required. For phase 2, it would be good if Stock Connect participants can access the onshore block trading mechanism just as QFI investors can.

On the QFI side, ASIFMA would like to see alignment and extension of the block trade order confirmation period for both SSE and SZSE. Currently, for SSE and SZSE, basically the execution orders of block trades can only be confirmed during a defined window (i.e., 15:00-15:30) after the close except for STAR Board where block trades can be confirmed intraday (i.e., 9:30-11:30 and 13:00-15:30) [26]. We ask that the order confirmation period for block trades on SSE Main Board and SZSE be extended to be in line with STAR Board.

Recommendation:

Provide Stock Connect participants with a mechanism to conduct block trading. For QFI investors, extend the execution order confirmation period of block trading on SSE main board and SZSE for matching throughout the entire trading day.

6. Program Trading

Program trading is a kind of trading method widely used in foreign securities and futures markets. It accounts for a relatively high proportion of transactions and has played an active role in improving market liquidity, risk management, and the efficiency of price discovery.

In China, program trading rules which are practical for the market participants are critical for the long-term sustainable development of the markets. Under the amended *Securities Law* issued in December 2019, it requires that program trading shall be reported to the stock exchange, may not affect the system security or the normal trading order of the stock exchange, and shall be subject to the regulations of the regulator. After the implementation of the 2019 *Securities Law*, the regulators have not introduced further supporting regulations on program trading, and the progress of establishing program trading registration and reporting mechanism for the securities market has been slow; meanwhile, the program trading registration and reporting mechanism in ETF options trading and convertible bonds trading with stock exchange have been established and well implemented. The lack

[26] Articles 3.6.3 and 6.1.13 of *Trading Rules of Shanghai Stock Exchange (2023 Revision)* (《上海证券交易所交易规则(2023 年修订)》), and Article 3.5.7 of *Trading Rules of Shenzhen Stock Exchange (2023 Revision)* (《深圳证券交易所交易规则(2023 年修订)》).

of program trading registration and reporting mechanism in stock trading becomes one of the major concerns of professional and institutional investors at the current stage.

In the futures market, the *Futures and Derivatives Law* promulgated on April 20, 2022 also provides that program trading shall be reported to the exchange and shall not affect the system security or the normal trading order of the exchange. Under the *Administrative Measures on Futures Exchanges* issued on March 29, 2023, it requires that the exchanges shall establish program trading reporting mechanism. At the level of futures exchanges, before the issuance of the *Futures and Derivatives Law*, the futures exchanges had already established and implemented program trading registration and reporting mechanism with a focus on the filing and registration of program trading. The following table summarizes the main rules issued by the exchanges in respect of program trading:

Table 4: Rules Issued by Exchanges Related to Establishment of Program Trading Registration and Reporting Mechanism

Exchange	Name of Rules	Date Issued
SZSE	Circular on Program Trading of Stock Options	December 2019
	Circular on Matters Relating to the Reporting for the Program Trading of Convertible Bonds	February 2021
SSE	Circular on Matters Relating to the Reporting for the Program Trading of Convertible Bonds	February 2021
	The Trading Rules for the Stock Options Pilot Program of the Shanghai Stock Exchange	January 2015
DCE	Trading Rules of Dalian Commodity Exchange	January 2021
	Circular of the Dalian Commodity Exchange on the Declaration of Program Trading Application	2010
SHFE	Trading Rules of Shanghai Futures Exchange	June 2021
	Circular of Shanghai Futures Exchange Office on Improving the Requirements for Information Filing of Part of Clients of Some Program Trading	June 2021
	Circular on Effectively Carrying out the Record-filing of Program Trading	2010
ZCE	Trading Rules of Zhengzhou Commodity Exchange	2021
	Circular of Zhengzhou Commodity Exchange on the Filing of Program Trading	2010
CFFEX	Detailed Trading Rules of China Financial Futures Exchange	March 2020
INE	Detailed Trading Rules of Shanghai International Energy Exchange	December 2021
	Circular on Effectively Carrying out the Record-filing of Program Trading	2018

Recommendations:

We strongly recommend establishing and implementing program trading registration and report mechanism for stock trading soon. Apart from the above rules for program trading formulated by the exchanges, we recommend establishing a unified and dedicated legislation on program trading applicable to both securities and futures markets. We note that the formulation of rules on program trading has been included in the legislative plan of the CSRC for several consecutive years, and we look forward to the release of the legislation to provide clear guidance for the industry.

We suggest that the regulators and exchanges pay particular attention to timely registration and reporting, systems security, and security of normal trading order of the exchange.

Recommendations for Equities – Secondary Market
In respect of **QFI:** 1. **(DVP and Pre-funding)** Remove the pre-funding requirement. 2. **(Post-trade and Regulatory Reporting)** Adopt ISO standards for clearing and settlement. 3. **(Custodian)** Allow foreign bank branches to look through their parent company's capability in order to fulfill applicable net asset requirements when considering becoming a QFI custodian. 4. **(Multi-broker Model)** Reform the trading rules of SSE and SZSE to allow the multi-broker model. 5. **(SBL)** Clarify how the uptick rule applies to QFIs, and allow segregation of client accounts and proprietary positions and segregation of different trading desks. In respect of **Stock Connect:** 6. **(Trading Universe)** Expand scope of eligible investment (in terms of both stocks and ETFs). 7. **(Holiday Trading)** Expand trading calendar to all market trading days on the host market. 8. **(SBL)** Include affiliates of Exchange Participants and Qualified Institutions as eligible SBL participants, and expand the category of Qualified Institutions to encompass accredited and regulated institutions such as Agent Lenders and Custodians. 9. **(Onshore Trading Desk to Manage Northbound Orders)** Allow brokers' onshore trading desks to manage Stock Connect orders on behalf of offshore affiliates. 10. **(Bilingual Stock Connect Rules of SSE/SZSE)** Issue both Chinese and English Stock Connect rules and ideally the English version to be binding or at least available on the official websites of SSE and SZSE. 11. **(Aggregation of Positions Across Custodians)** Allow Stock Connect investors to aggregate positions across accounts opened at different custodians at the same beneficial owner level. In respect of **Short Swing Profit Rule:** 12. treat all investment managers (including offshore ones) the same way as domestic public funds and exempt them from the short swing profit rule and look at the shareholdings of funds and/or clients that are managed under separate agreements by the same asset manager separately.

In respect of **Access to Onshore Derivatives:**

13. Diversify derivative product suite (e.g., bond futures and ETF options) accessible to QFIs.
14. Remove the hedging-only restrictions or increase flexibility on hedging quota calculations.
15. Provide offshore investors without a QFI license, including those under the Stock Connect scheme, access to PRC onshore derivative products.
16. Start listing SSOs.

In respect of **Block Trades:**

17. Provide Stock Connect participants a mechanism to conduct block trading.
18. For QFI investors, extend the execution order confirmation period of block trading on SSE Main Board and SZSE.

In respect of **Program Trading:**

19. Establish and implement program trading registration and report mechanism for stock trading; establish a unified and dedicated legislation on program trading applicable to both securities and futures markets.
20. Pay particular attention to timely registration and reporting, systems security, and security of normal trading order of the exchange.

D. Fixed Income

1. Introduction

At USD 21.6 trillion, China's bond market is now the second largest in the world behind the United States (USD 51.9 trillion) with an almost 80% increase over the past five years. With over 65% of the market instruments issued by government related entities, the corporate bond market has not grown as much as in major competing economies mainly due to corporates' high reliance on loans – proportionally 50% more than in the US.[27] Moreover, while the bond market is large, the liquidity in the secondary market is rather limited compared to its size. Currently, the foreign investors' participation is mainly centered on government bonds and relatively small compared to other large bond markets. There is nevertheless a growing interest following FTSE Russell bond index inclusion announcement in March 2021.

With Chinese government bonds (CGB) included in the Bloomberg Barclays, JP Morgan and FTSE Russell bond indices in 2019, 2020 and 2021, foreign investors' holdings in CGBs grew to about 9% by the end of 2022[28]. Even though there were outflows from the China bond market due mainly to increases in US interest rates, the number of new foreign investors accessing the China bond market through the Bond Connect and CIBM Direct still grew by 7% and 11%, respectively, in 2022.[29] To better allocate capital to dynamic and healthy companies that will contribute to the economic growth, China needs to continue to move away from the loan market and incentivize corporate issuances where investors can properly assess the credit risk of issuers.

Internationally aligned, differentiating and transparent credit ratings, a developed and accessible listed and OTC derivatives market and a well-functioning repo and SBL market improve the market's liquidity and transparency which are important factors for investors looking to confidently and easily accessing the debt market.

With respect to corporate bond market, the most important is establishing or allowing an independent credit rating system with appropriate scale of differentiation between high- and lower-quality corporates. This can hardly be possible today when 95% of the Chinese credit bonds are rated AA or above (compared with less than 6% of the US market).[30] To improve credit risk analysis, foreign rating

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[27] Data from AsianBondsOnline, https://asianbondsonline.adb.org/economy/?economy=CN.
[28] Data from AsianBondsOnline, https://asianbondsonline.adb.org/economy/?economy=CN.
[29] CFETS, Market Overview of Overseas Investment in July 2022, https://www.shibor.org/english/svcnrl/20220826/2447028.html.
ICMA, Investing in China's Interbank Bond Market: A Handbook, https://www.icmagroup.org/assets/documents/About-ICMA/APAC/NAFMII-and-ICMA-Investing-in-Chinas-Interbank-Bond-Market-Handbook-September-2021-230921.pdf.
[30] The Future of China's Bond Market, https://www.elibrary.imf.org/downloadpdf/book/9781513582788/9781513582788.xml.
Introduction to China's onshore credit bond market, https://www.invesco.com/content/dam/invesco/apac-master/en/pdf/invest_china/2021/june/introduction-to-china-onshore-credit-bond-market.pdf.

agencies need to be recognized and allowed to rate all bonds and ensure level playing field with their local competitors. The regulators should encourage further alignment of domestic rating, together with information disclosure and due diligence processes to international standards and best practices.

The derivatives market needs to be further developed to allow market makers and investors to appropriately hedge their risks against interest rate, market and credit risks, which ultimately benefits price discovery and lowers funding costs while optimizing resources allocation.

Bond futures are the most important listed derivative products but lack liquidity. The big five domestic banks hold the bulk of the underlying government bonds but, to date, have not been active in the futures market even though legally permitted since early 2020.

To further develop liquidity and provide hedging instruments to a larger participant base on a level playing field with their peers, it is recommended to continue broadening the direct access to more domestic institutions and international investors through QFI and CIBM Direct channels. The market was encouraged to hear CSRC's Vice Chairman Fang Xinghai in a speech at the China International Finance Annual Forum last year mentioning the regulator's support for Hong Kong launching CGB futures and accelerate the process to allow foreign access to the domestic CGB futures market[31] (this commitment was reiterated during his speech at the 20th Shanghai Derivatives Market Forum on 25 May 2023). This was translated by the recent announcement of an additional batch of approved participants which included one foreign-invested bank and HKEX drive to (re)launch of MOF Govt Bond Futures.[32]

Interest rate swaps are relatively liquid, but floating reference rates might not be completely aligned with corporate financing reference rates. There is limited adoption of ISDA documentation (versus NAFMII documentation) which is the standard for international investors. This could reduce their appetite to be more active in the domestic derivatives market and thereby undermining its liquidity. From an offshore access perspective, the launch on 15 May 2023 of Swap Connect was warmly welcomed by the market.

The other cornerstone in the fixed income markets is a well-functioning repo market where sellers can lend securities to buyers who in turn can then trade them in the market providing liquidity to investors. Contrary to global standards, the securities are pledged and do not have their ownership transferred which prevents rehypothecation – hence reducing liquidity. There is also no triparty repo, an important feature needed to encourage bond holders like insurance companies, pension funds, etc. to finance those instruments - although we know CCDC is working on a solution. With respect to foreigners who are more familiar with repo, it would make sense to allow them to access this market

[31] Fang Xinghai's speech at China International Finance Annual Forum 2022, http://www.csrc.gov.cn/csrc/c100028/c5603389/content.shtml.
[32] Standard Chartered participates in trading of treasury bond futures in China, https://global.chinadaily.com.cn/a/202301/05/WS63b6868aa31057c47eba7e42.html.

via any channel (including leveraging the Connect channels) and not just Public Sector investors and Offshore Participating Banks (OPBs) via CIBM Direct and QFI as it stands now and to use the globally recognized Global Master Repo Agreement (GMRA) rather than the local NAFMII documentation, in addition to recognizing and allowing international triparty agents to support this activity.

The recognition of close-out netting for derivatives instruments under the *Futures and Derivatives Law* (《期货和衍生品法》) enacted in August 2022[33], is a major advancement in China's regulatory framework. International investors are now looking forward for a similar framework to recognize GMRA as a valid close-out netting master agreement.

In Hong Kong, we were very encouraged by the *Report of the Steering Committee on Bond Development in Hong Kong* (the "Report") in August 2022. Spearheaded by Hong Kong Financial Secretary Mr. Paul Chan Mo-Po (陳茂波), the Report puts forward a number of strategic directions in areas covered in this section.[34] Hong Kong being the gateway to and from China, ASIFMA and its members welcomed the Report's recommendations to attract the Mainland entities for RMB bond issuances, to develop bond-related markets components such as derivatives and repo, and to enhance the Central Moneymarkets Unit (CMU) functionalities and infrastructure – amongst others. They will contribute not only to the development of the RMB bond market but also to the internationalisation of RMB.

Finally, as global fixed income markets are dominated by institutional investors, the size of their participation - both domestic and foreign ones - needs to increase dramatically, by attracting insurers, pension funds or asset managers and by broadening the range of fixed income products available to retail investors through bond ETFs and mutual funds which could partially unlock the large retail bank deposits (USD 32 trillion) as a potential source for future development.

2. Bond Market

2a. CIBM

- **Expedite CIBM market-makers application process, and begin approval of foreign firms**

The PBOC introduced the filing mechanism for the bond market-makers in CIBM in December 2020 to replace the previous approval mechanism.[35] The CFETS published the relevant implementation rule

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[33] Article 37 of the *Futures and Derivatives Law* (《期货和衍生品法》).
[34] Report of the Steering Committee on Bond Market Development in Hong Kong, https://www.fstb.gov.hk/fsb/en/publication/report/docs/Report%20of%20the%20Steering%20Committee%20on%20Bond%20Market%20Development%20in%20Hong%20Kong_EN_2022_08.pdf.
[35] *PBOC Announcement [2020] No. 21 - Notice on Matters Relating to Improvements to Administration of Cash Bond Market Makers in the Interbank Bond Market* (《关于完善银行间债券市场现券做市商管理有关事宜的公告》).

thereafter. This was an important step to further allow the qualified financial institutions to apply for the CIBM bond market-makers, and thus promote the overall trading liquidity in CIBM.

According to the *Guidelines for Operation of the Bond Market Maker Business in the Inter-bank Bond Market* (《全国银行间同业拆借中心银行间债券市场现券做市商业务操作指引》) issued by CFETS on 25 December 2020 (the "CFETS Guidelines"), the CFETS shall inform the financial institution that meets the requirements stipulated by the PBOC Announcement [2020] No. 21 to sign a market making business agreement with the CFETS within 10 working days after the CFETS receives all the required application documents submitted by the financial institution. The financial institution shall sign the agreement within 10 working days thereafter. After the execution of the agreement, the CFETS shall report the same to the PBOC, and the financial institution will be required to conduct market-making business in cash bonds for 6 months on a trial basis. If the financial institution does not have any circumstances of an unqualified market maker during the six-month trial period, then the CFETS will publicly announce to the market that the financial institution is officially qualified to carry out the market-making business in cash bonds, and the CFETS will report the same to the PBOC.[36]

We have noted that in 2022, there was no new CIBM bond market-maker registered. The filing process was also prolonged than the market expectation, so the newly added market makers were very limited. In particular, no foreign financial institution was introduced in under the new mechanism.

Recommendation:

We expect the CFETS to expedite the review process and promote the eligible foreign financial institutions to become the CIBM bond market makers, which will reflect the nature of filing mechanism.

- **Simplify administrative procedures on non-trade transfer of bonds between CIBM Direct and QFI of the same registered investor**

The *Circular Relating to Further Facilitating Foreign Institutional Investors' Investment in the Interbank Bond Market* (《关于进一步便利境外机构投资者投资银行间债券市场有关事项的通知》) issued by the PBOC and SAFE on 30 September 2019 (the "PBOC and SAFE Circular")[37] allows a two-way non-trade transfer of bonds under QFI and CIBM Direct for the same investor. The same investor may, according to its own investment management needs, make a two-way non-trade transfer of the CIBM bonds held by it between its bond accounts under the QFI scheme and its bond account under the CIBM Direct scheme.

[36] Articles 3 and 4 of the *Guidelines for Operation of the Bond Market Maker Business in the Inter-bank Bond Market* (《全国银行间同业拆借中心银行间债券市场现券做市商业务操作指引》).
[37] *Circular Relating to Further Facilitating Foreign Institutional Investors' Investment in the Interbank Bond Market*, http://www.safe.gov.cn/en/2019/1030/1584.html.

According to the *Operational Rules for Non-Trade Transfer Application of Same Foreign Investors via QFI and Direct Access Scheme* (《关于境外机构投资者申请不同渠道下债券非交易过户的实施细则》) issued by CCDC on 18 November 2019 (the "CCDC Operational Rules")[38], in order to make a two-way non-trade transfer, a QFI shall entrust its settlement agent to file an application with the CCDC by submitting application materials. Then the CCDC shall review the application materials in a prudent manner and notify the settlement agent of the results within 2 working days upon receipt of the application. After the application is approved, the CCDC shall handle bond transfer within 2 working days.[39]

While investors welcome the PBOC and SAFE Circular and the related CCDC Operating Rules announced in 2019 to standardize the operating procedures of a foreign institutional investor to apply for two-way non-trade transfer of the CIBM bonds held by it between its bond accounts under the QFI scheme and its bond account under the CIBM Direct scheme, the current procedure generally takes investors 5-7 days to complete such transfer. Similar re-alignment procedure allowed by other International central securities depository (ICSD) typically happens on T+0/T+1 basis depending on time zone (e.g., Australian Commonwealth Government Bonds (ACGB) re-aligned between Austraclear and Euroclear; Japanese Government Bonds (JGB) re-aligned between Bank of Japan (BOJ) and Euroclear).

Recommendation:

We recommend CCDC to simplify procedures by: 1) allowing investors to submit application materials in soft copy other than hard copy that needs to be couriered; 2) waiving the requirement on submitting application materials again on the same securities when investors want to move the securities back to the original account; and 3) allowing the application materials submitted by investors to cover any transfer request with a notional value less than RMB 2 billion (i.e., making the submissions one-off for smaller transfer tickets).

- **Dual currency ratio**

Following the PBOC and SAFE *Provisions on the Management of Funds Invested by Foreign Institutional Investors in China's Bond Market (Circular 258 [2022])* (《境外机构投资者投资中国债券市场资金管理规定》), SAFE issued in March 2023 Q&A clarifying and broadening the process of inward remittance of RMB and foreign currencies while relaxing the ratio of outward remittance of foreign currencies[40], which was welcomed by the international investors.

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[38] *Operational Rules for Non-Trade Transfer Application of Same Foreign Investors via QFI and Direct Access Scheme*, https://www.chinabond.com.cn/cb/eng/zqsc/jwtzzzl/scgz/20191119/153118063.shtml.

[39] Articles 2 and 3 of the *Operational Rules for Non-Trade Transfer Application of Same Foreign Investors via QFI and Direct Access Scheme* (《关于境外机构投资者申请不同渠道下债券非交易过户的实施细则》).

[40] *SAFE's Q&A on Provisions on the Management of Funds Invested by Foreign Institutional Investors in China's Bond Market* (《境外机构投资者投资中国债券市场资金管理规定》政策问答), https://www.safe.gov.cn/safe/2023/0321/22487.html.

Recommendation:

We recommend the PBOC and SAFE to further raise and eventually remove the dual currency ratio which would provide them the flexibility to fund their accounts in either currency.

- **Omnibus account structure with recognition of foreign nominee concept**

Foreign investors have a strong preference to access a market via the omnibus account structure, which offers highest efficiency and convenience. The omnibus account concept has been introduced for Bond Connect, where the CMU is allowed to open an omnibus account at CCDC and SHCH to settle and safekeep securities on behalf of foreign investors.[41] We believe this concept could be applied to CIBM Direct as well, whereby ICSDs /custodian banks could open an omnibus account at CCDC/SHCH, similar to the CMU for Bond Connect. The foreign nominee concept would enable the omnibus account to be legally held in the name of the ICSDs/custodian banks, whilst the beneficial ownership of the securities held in the account would be fully recognized as belonging to the underlying investors.

Recommendation:

We recommend regulators to allow ICSDs and custodian banks to open an omnibus account at the level of CCDC/SHCH to hold assets on behalf of underlying foreign investors. Transparency on beneficial ownership could be met, e.g., via holding and transaction reports to PBOC and/or market infrastructures.

2b. Bond Connect

- **Northbound Bond Connect**

Many global asset managers are happy with Northbound Bond Connect, with many of their teething problems having been addressed. For example, at ASIFMA's urging, CFETS came up with an international payment service in April 2021 that enabled onshore bond dealers to quote prices inclusive of the trading fees payable to Bond Connect Company Limited (BCCL) and some of the trading platforms. As of February 2023, 80-90% of the onshore dealers are able to support this service.

(1) Rolling settlement

Settlement of bond trades was also extended from T to T+3 to as long as T+4 and beyond. In addition, at ASIFMA's suggestion, rolling settlement was introduced in March 2020 to allow foreign investors to apply to CCDC or SHCH for rolling settlement within three business days

[41] Trading Mechanism of Bond Connect, https://www.chinabondconnect.com/sc/Northbound/Trading-And-Settlement/Trading-Mechanism.html.

following the original settlement date should a trade fail to settle on the original settlement date.[42] However, in reality, foreign investors seldom use rolling settlement because of the following reasons.

Unlike many bond markets around the world where rolling settlement does not involve changes in the settlement amount (transaction price), Bond Connect investors have to re-negotiate the settlement amount with the counterparty[43], which is like entering into a new transaction and defeats the purpose of rolling settlement. In addition, compared to regular trades that can be done through Straight-Through Processing (STP), rolling settlement requires foreign investors to manually send instructions to their global custodians or the Hong Kong Monetary Authority (HKMA) CMU.[44] Moreover, foreign investors opting for rolling settlement still need to make a failed trade settlement report. Hence, a lot of foreign investors would rather have the trade fail and follow the failed trade settlement reporting process than to opt for rolling settlement.

Recommendation:

We recommend that other than the change in settlement date, no other terms of the original failed trade be changed if foreign investors opt for rolling settlement. And, that the change in settlement date can be sent through STP so that foreign investors do not have to resend instructions manually to their custodians. More important, a change in the settlement date should not be viewed as a failed trade so that there would be no need for the filing of a failed trade settlement report.

(2) Failed trade settlement reporting

Under the current Bond Connect trading rules, if a trade fails to settle, both parties involved in the northbound transaction have to report the failed trade to CFETS and another report to the clearing corporation (i.e., SHCH or CCDC) in a timely manner. [45]The counterparties will need to physically

[42] Article 2 of the *Tentative Implementation Rules for the Provision of Rolling Settlement Services for Overseas Institutional Investors by CCDC* (《中央国债登记结算有限责任公司关于为境外机构投资者提供循环结算服务的实施细则（暂行）》) and Article 2 of the *Notice of Providing Rolling Settlement Services and Flexible Settlement Cycles for Foreign Institutional Investors by SHCH* (《银行间市场清算所股份有限公司关于向境外机构投资者提供循环结算服务和灵活结算周期安排的通知》).

[43] Article 6 of the *Tentative Implementation Rules for the Provision of Rolling Settlement Services for Overseas Institutional Investors by CCDC* (《中央国债登记结算有限责任公司关于为境外机构投资者提供循环结算服务的实施细则（暂行）》).

[44] Article 5 of the *Tentative Implementation Rules for the Provision of Rolling Settlement Services for Overseas Institutional Investors by CCDC* (《中央国债登记结算有限责任公司关于为境外机构投资者提供循环结算服务的实施细则（暂行）》).

[45] Article 5.3 of the *CFETS Trading Rules for Bond Connect (for Trial Implementation)* (《全国银行间同业拆借中心“债券通”交易规则（试行）》), Paragraph 4(3) of the *Notice of CCDC on Implementation of PBC's Interim Procedures of Bond Connect Settlement* (《关于落实中国人民银行<“债券通”结算操作暂行规程>相关事宜的通知》) and Article 4.3 of the *Business Guidelines of SHCH for Northbound Trading of Bond Connect (for Trial Implementation)* (《银行间市场清算所股份有限公司“债券通”北向通业务指南（试行）》).

sign on the same reporting form which will then have to be submitted by the foreign investor. This is cumbersome and time-consuming for foreign investors since their counterparties are based in different parts of the Chinese mainland.

Recommendation:

We recommend that the reporting for failed trade settlement can be done electronically by each counterparty independent of each other. We understand that CFETS is updating their system so that this can be done and are much appreciative of all their efforts in making it easier for foreign investors to use the Bond Connect.

(3) Non-trade transfers

In response to ASIFMA's request to enable foreign investors to consolidate their securities holdings under various access channels, the PBOC and SAFE announced that starting from 15 November 2019, foreign investors are allowed to make non-trade transfers of their bond holdings and cash between their CIBM Direct account and QFI account.[46] However, such non-trade transfer is not available between Bond Connect accounts and CIBM Direct or QFI accounts because of the closed loop framework for the offshore and onshore access schemes. Nevertheless, we would like to suggest that the PBOC and SAFE consider allowing a one-time non-trade transfer between these accounts to accommodate those foreign investors who would like to consolidate their bond holdings in one channel.

For transfers within Bond Connect itself, we understand that non-trade transfers are allowed for bond holdings under the same account holder. If a CFETS account is opened in the name of the original asset manager (even though a sub-account is opened in the name of the client under the original asset manager in the CMU) and the client wants to change to a new asset manager, the holdings of the client cannot be transferred to the new asset manager under the non-trade transfer route. This means that the client can only sell its holdings under the original asset manager's account and transfer the proceeds to the new asset manager to repurchase its holdings resulting in not only transaction costs but also possible gains or losses as well as taxes in the process.

Notwithstanding the above, we have learned from BCCL via HKMA that, if the original asset manager is willing to submit a Bond Connect Registration Update Form to CFETS via BCCL to change ownership of the account in question to the new asset manager, the investor can change asset manager without changing CFETS account, and asset liquidation will not be necessary. BCCL and CFETS have facilitated this type of change in the past, and there are procedures in place for

[46] *Operational Rules for Non-Trade Transfer Application of Same Foreign Investors via QFI and Direct Access Scheme* (《关于境外机构投资者申请不同渠道下债券非交易过户的实施细则》) issued by CCDC.

CMU to support the necessary FOP transfer. But not all asset managers are willing to take this route.

Recommendation:

To enable a change in asset manager by an investor without triggering costs, expenses and taxes to the investor, we recommend that CFETS accounts can be registered in both the name of the asset manager and the client (like the QFI account structure) and that non-trade transfers be allowed when there is a change in the asset manager but not the client. After all, the beneficial owner of the bond holdings or assets is the same and the beneficial owner should not have to sell its holdings when it changes asset managers.

- **Southbound Bond Connect: increase of quota and number of market makers**

According to the *Notice on the Launch of Southbound Bond Connect of Mutual Bond Market Access between Chinese Mainland and Hong Kong SAR* (《中国人民银行关于开展内地与香港债券市场互联互通南向合作的通知》) issued by the PBOC on 14 September 2021 (the "PBOC Southbound Notice"), the net outflow of funds under Southbound Bond Connect scheme shall be subject to an annual aggregate quota and a daily quota. Presently, the annual aggregate quota is RMB 500 billion (or equivalent) and the daily quota is RMB 20 billion (or equivalent)[47].

The recent surge of interest rate differential between RMB and other foreign currencies (USD in particular) has increased the domestic investors' appetite for foreign currency denominated assets which has translated in a strong usage of the quota (up to 80%). The access to the eligible securities through Southbound Connect has been impeded at the pre-trading level with the pre-filing with the PBOC which is a managed approval process to adapt to market conditions leading to slower or rejected approvals.

In this context, new quotas are welcome but a broadened scope as well as new eligible securities – like what Stock Connect has gone through – would be necessary to support the potential strong market demand.

With respect to market makers, there are 13 financial institutions designated by the HKMA as market makers for Southbound Trading under Bond Connect.[48] We have noted that there was no new Southbound market-maker designated by the HKMA since September 2021.

[47] Article 9 of the *Notice on the Launch of Southbound Bond Connect of Mutual Bond Market Access between Chinese Mainland and Hong Kong SAR* (《中国人民银行关于开展内地与香港债券市场互联互通南向合作的通知》).

[48] HKMA publicized a list of designated market makers for Southbound Trading under Bond Connect on its web site on September 17, 2021, https://www.hkma.gov.hk/eng/news-and-media/press-releases/2021/09/20210917-6/ and https://www.chinabondconnect.com/en/Southbound/Market-Makers.html.

Recommendation:

We recommend broadening the scope of eligible assets and clarify what is in scope (e.g., structured notes linked to credit, commodities or equities) and enlarging the eligible investors base that is today limited to QDII Investors and 41 Open Market Operations (OMO) banks[49]. It would also be welcome to allow additional custodians and market makers to join the program.

- **Decouple CIBM market-maker status from Bond Connect market maker status**

On 23 December 2020, the PBOC issued the *Notice on Matters Relating to Improvements to Administration of Cash Bond Market Makers in the Interbank Bond Market* (《关于完善银行间债券市场现券做市商管理有关事宜的公告》) (the "PBOC Announcement [2020] No. 21"), which has taken into effect as of 1 April 2021. Since then, domestic financial institutions may carry out market making business by signing a market making business agreement with the CFETS without the need to obtain an approval from the PBOC.[50] Under the new filing mechanism for the bond market-makers in CIBM, a qualified CIBM market maker shall be a domestic financial institution, such as a commercial bank or a securities company, and shall have strong pricing capacity, capital strength and risk management capacity appropriate to the market making business to be carried out, as well as relevant business system and professional team to support the market making business.[51]

With respect to the entry of Bond Connect market-makers, according to the *CFETS Trading Rules for Bond Connect (for Trial Implementation)* (《全国银行间同业拆借中心"债券通"交易规则（试行）》), a Bond Connect market-maker shall have strong quoting and pricing capabilities, good international reputation, having personnel, systems and facilities to support the continuous and stable operation of Bond Connect business and other capabilities necessary to provide liquidity to the bond market.[52]

According to CFETS's practice, CIBM market-maker status is usually a pre-requisite to be a Bond Connect market-maker. Onshore entities of some foreign institutions have the intention and willingness to apply for Bond Connect market-makers, as well as the capabilities to introduce and serve new overseas clients to trade China bonds via Bond Connect mechanism, but they are not CIBM market-makers. Emblematic of this situation, the PBOC and CFETS have not granted any new Bond Connect market-makers since April 2020. We would thus like to call for the decoupling between CIBM market-maker and Bond Connect market-maker requirements, so that eligible foreign banks and

[49] *PBOC Q&A with Media on the Southbound under Mutual Bond Market Access between Mainland China and Hong Kong.*

[50] Article 3 of the *Notice on Matters Relating to Improvements to Administration of Cash Bond Market Makers in the Interbank Bond Market* (《关于完善银行间债券市场现券做市商管理有关事宜的公告》).

[51] Article 1 of the *Notice on Matters Relating to Improvements to Administration of Cash Bond Market Makers in the Interbank Bond Market* (《关于完善银行间债券市场现券做市商管理有关事宜的公告》).

[52] Articles 2.4 and 2.5 of the *CFETS Trading Rules for Bond Connect (for Trial Implementation)* (《全国银行间同业拆借中心"债券通"交易规则（试行）》).

foreign securities firms operating in China can apply for the Bond Connect market-maker directly. It will bring in high quality foreign investors and enhance China's connection to the global financial market. Allowing for more foreign market-makers in Bond Connect is also in line with China's goals of RMB internationalization and capital markets opening.

- **Assessment of various operational and trading processes (north- and south-bound)**

Bond Connect scheme is distinguished from CIBM Direct scheme in various operational and trading processes as well as relevant regulatory requirements. Please refer to Annex 3 to this Paper, where we have summarized a comparison between CIBM Direct scheme and Bond Connect scheme (and also QFI, with respect to bond trading) for reference. We believe any simplification of operational and trading processes would help attract more foreign participation in the Bond Connect scheme. Therefore, we expect regulators to continue to improve the operational and trading processes of Bond Connect scheme. One of our key **recommendations** is related to the documentation process for onshore currency hedging.

- **Documentation process for onshore currency hedging**

Under Northbound Bond Connect scheme, the *Interim Measures for the Administration of Mutual Bond Market Access between Chinese Mainland and Hong Kong SAR* (《内地与香港债券市场互联互通合作管理暂行办法》) issued by the PBOC on 21 June 2017 provide that Bond Connect investors may conduct currency conversion or foreign exchange hedging with the designated settlement banks in Hong Kong ("Hong Kong settlement banks"), and the Hong Kong settlement banks are subject to certain verification, information collection and reporting obligations.

Further, the CFETS issued the *Notice on the Implementation of the Enhanced Arrangements of the Currency Conversion and FX Risk Management under the Bond Connect Scheme* (《关于落实完善债券通渠道资金汇兑和外汇风险管理有关安排的公告》) on 24 September 2020[53], providing that each Bond Connect investor may select no more than three Hong Kong settlement banks to conduct currency conversion and foreign exchange hedging, and Bond Connect investors shall promptly inform the principal Hong Kong settlement banks of their investment needs behind currency conversion and risk hedging transactions. Hong Kong settlement banks shall verify the authenticity of these transactions and monitor these transactions based on the trading information collected from the Bond Connect investors, and perform reporting obligations via the CFETS Post-trade Processing Platform. The information to be reported shall include the execution date, the name of foreign investor, the name of bondholder(s), country/region of the foreign investor, trading product, trading direction, amount, exchange rate, purpose/source and transaction type.

[53] English version of the *Notice on the Implementation of the Enhanced Arrangements of the Currency Conversion and FX Risk Management under the Bond Connect Scheme*, https://www.chinamoney.com.cn/english/rarfmrrudrgl/20200924/1785566.html.

Under Southbound Bond Connect scheme, the PBOC Southbound Notice stipulates that domestic investors investing in foreign currency bonds with RMB may conduct currency conversion and foreign exchange hedging via the CIFXM. Where a domestic investor does not continue its investment when the bonds mature or are sold, the relevant funds shall be remitted back to the territory of China and converted into RMB. The PBOC, working with the SAFE, supervises and administers the currency conversion, outward and inward remittances of funds and information reporting relating to Southbound Bond Connect business carried out by domestic investors so as to prevent domestic investors from committing illegal or irregular activities via Southbound Bond Connect scheme. [54]

Recommendation:

Considering that the registration and reporting process remain heavy and time consuming, simplification and streamlining of documentation process for onshore currency hedging under Bond Connect would then be welcome.

2c. Alignment of Access Channels

The multitude of investment access channels and their different requirements and investment scopes can be confusing to FIIs and make it difficult for them to easily invest in China's equities and debt markets.

After almost 20 years in operation, China finally simplified its first investment access scheme for FIIs, the QFI scheme, by merging it and the subsequent RQFII scheme into one QFI scheme in September 2020. In the meantime, China also launched CIBM in 2010, Stock Connect in 2014, and Bond Connect in 2017.

Due to the different investment scopes (with the onshore ones having a broader investment scope and permitting more activities) and operating requirements (such as capital controls when investing from onshore) of these schemes, FIIs often have to choose between one access channel over another or incur the time and costs of investing through multiple access channels which often require different infrastructure or system support. Like the issue of financial institutions having to operate in China through many different entities, it is highly inefficient for FII investments in China to go through multiple access channels. Alignment of the access channels to the same markets, such as CIBM Direct and Bond Connect to the CIBM, would greatly reduce the complications involved, make investing in China easier for FIIs who would like to be able to consolidate their positions in one scheme for ease of management and to reduce duplication, minimize operational risks, achieve cost efficiencies and optimize returns for their end investors.

[54] Articles 8 and 12 of the *Notice on the Launch of Southbound Bond Connect of Mutual Bond Market Access between Chinese Mainland and Hong Kong SAR* (《中国人民银行关于开展内地与香港债券市场互联互通南向合作的通知》).

We appreciate the *Notice No. 4 on Matter Related to Further Facilitating FIIs' Investment in the China Bond Market* (《关于进一步便利境外机构投资者投资中国债券市场有关事宜的公告》) ("Notice No.4") jointly issued by PBOC, CSRC and SAFE in May 2022 which was promulgated the principle of "one set of rules under on bond market". Even though the Notice No.4 sets out the regulatory ground for aligning and further expanding the investment scope under Bond Connect and CIBM Direct to include cash bonds (both traded on the CIBM and the exchanges), bond borrowing and lending, derivatives for risk management purposes, open-ended bond index securities investment funds and other instruments permitted by PBOC and CSRC[55], we understand that this will be the direction for future developments and has not been officially implemented at the moment.

***Recommendation**:*

Alignment of the access channels to the same markets, such as CIBM Direct and Bond Connect to the CIBM, would greatly reduce the complications involved, make investing in China easier for FIIs who would like to be able to consolidate their positions in one scheme for ease of management and to reduce duplication, minimize operational risks, achieve cost efficiencies and optimize returns for their end investors.

2d. Inter-connection between CIBM and Exchange Bond Market

In July 2020, PBOC and CSRC jointly announced the decision to allow the investors that already have access to either the CIBM or exchange bond market to invest in the other through the connection between the trading platforms (i.e., SSE, SZSE and CFETS), without the need for additional investor filing or account opening.[56] The bond market clearing corporations under the two markets will open nominee accounts with each other for holding bonds traded through the inter-connection.[57]

It was made clear under the Notice No. 4 that the inter-connection will be available to the Bond Connect and CIBM Direct investors.[58] While we understand the system upgrade has been completed in early 2023 for the inter-connection, it has not been launched yet.

In addition to the inter-connection, the Notice No. 4 also provided another approach for such FIIs to access the exchange bond market, which is through directly opening a securities account in the latter. We understand from PBOC that the principle is for no additional filing or approval will be needed for going through either the inter-connection channel or the "direct access" channel.[59]

[55] Article 5 of the *Notice No. 4 on Matter Related to Further Facilitating FIIs' Investment in the China Bond Market* (《关于进一步便利境外机构投资者投资中国债券市场有关事宜的公告》).
[56] Announcement [2020] No. 7 of the PBOC and the CSRC.
[57] Article 3 of the Announcement [2020] No. 7 of the PBOC and the CSRC.
[58] Article 4 of the *Notice No. 4 on Matter Related to Further Facilitating FIIs' Investment in the China Bond Market* (《关于进一步便利境外机构投资者投资中国债券市场有关事宜的公告》).
[59] the *PBOC Q&A with Media on* the *Notice No. 4 on Matter Related to Further Facilitating FIIs' Investment in the China Bond Market*.

Recommendations:

We understand that the scheme is ready from a technical perspective. We would then welcome the regulators to approve its launch as soon as possible to respond to the strong foreign investors' appetite.

2e. Trading Platforms and Electronification

We would like to encourage and see further development of the trading protocols onshore. Specifically, the ability to request and quote two-way prices (Request for Markets – RFM) and the ability for market participants to counter levels dynamically. These features that are relatively commonplace in other markets would offer the Chinese markets a level of sophistication and serve to better protect clients by reducing bid-ask spreads.

2f. DCM

- **Regulatory update on panda bond market, particularly for international issuers, on both interbank and stock exchange market**

In December 2022, the PBOC and SAFE jointly issued the *Provisions on the Management of Funds Invested by Foreign Institutional Investors in China's Bond Market (Circular 258 [2022])* (《境外机构投资者投资中国债券市场资金管理规定》), which unified registration, remittances and account openings for renminbi-denominated bonds issued by overseas issuers in China across the interbank and exchange-traded bond markets. It also further relaxes how proceeds of panda bond issuances can be used onshore or remitted overseas.

Recommendation:

This enhanced flexibility was welcomed by panda bond issuers allowing them to deploy proceeds overseas as the previous restrictions capped the number of international issuers to those that use the proceeds onshore. Going forward, it would be important to lay out how the proceeds can be remitted offshore, especially given SAFE approval would typically be required. Ideally issuers should be able to remit the proceeds directly on the day of settlement or to reduce to a minimum the time it needs to be held in an onshore account before it can be remitted offshore. The recommendation can be extended to the interest payment and redemption mechanism.

There is therefore a need for a very clear process to be established reducing to a minimum any friction to the movements of funds cross-border. We then recommend PBOC and SAFE to continue the panda bond market reforms to attract more international issuers and investors.

3. Funding (Repo and Securities Lending) and Collateral

3a. Leverage the Connect Scheme to Access Onshore Repo Market

Currently, foreign investors can trade in the CIBM via three channels, i.e., CIBM Direct scheme, Bond Connect scheme, and QFI scheme. Bond repo can be traded only by "sovereign-type institutions" including foreign central banks or monetary authorities, international financial organizations, sovereign wealth funds, offshore CIBM participating banks and RMB settlement banks through the CIBM Direct[60], while it is not available to "commercial-type institutions" such as foreign commercial banks, insurance companies, securities companies, fund management companies. In addition, under CIBM Direct and QFI schemes, commercial-type institutions are currently only allowed to trade bond lending, bond forwards, interest rate forwards and interest rate swaps for hedging purposes.[61] Bond Connect investors are only permitted to trade in cash bonds.[62] It is currently not practical for "commercial-type institutions" to access the bond repo market through any of the three channels, for which demand from the foreign investors is growing.

With the success of Bond Connect, its investors are looking at optimizing the financing of their holding and accessing the onshore repo liquidity, the same way they will soon be able to hedge their market risk by accessing the onshore IRS market via SWAP Connect.

***Recommendation**:*

To allow international investors to access the bond repo market from offshore through a Northbound Connect channel.

3b. Facilitate Access to Onshore Repo Market for Foreign Investors

As mentioned above, onshore repo market access is currently limited to sovereigns, supra-nationals, offshore RMB settlement banks and offshore CIBM participating banks. Qualified foreign participants experience difficulties to obtain liquidity from onshore Chinese counterparts. Under the only

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[60] *Notice of the PBOC on Issues concerning Investment in the Inter-bank Market with RMB Funds by Foreign Central Banks, International Financial Organizations, and Sovereign Wealth Funds* (《中国人民银行关于境外央行、国际金融组织、主权财富基金运用人民币投资银行间市场有关事宜的通知》) and *Notice by the PBOC of Conducting Bond Repurchase Transactions by Offshore RMB Settlement Banks and Offshore Participating Banks on the Inter-Bank Bond Market* (《中国人民银行关于境外人民币业务清算行、境外参加银行开展银行间债券市场债券回购交易的通知》).

[61] *PBOC Circular on Further Improving the Matters Related to Foreign Institutional Investors' Investment in the Inter-bank Bond Market (PBOC Circular [2016] No.3)* (《中国人民银行公告(2016)第 3 号—关于进一步做好境外机构投资者投资银行间债券市场有关事宜的公告》) and its Press Conference Q&A.

[62] *Interim Measures for the Administration of Mutual Bond Market Access between Mainland China and Hong Kong SAR (PBOC Decree [2017] No.1)* (《内地与香港债券市场互联互通合作管理暂行办法》(中国人民银行令〔2017〕第 1 号)) and its Press Conference Q&A, http://www.scio.gov.cn/xwfbh/gbwxwfbh/xwfbh/rmyh/Document/1556566/1556566.htm.

recognized NAFMII repo master agreement, the liquidity is also limited due to the pledged nature of collateral that prevents any re-use of the pledged securities. It is hoped that, at some point, the PRC authorities may allow foreign investors to participate in onshore bond repo trading activities, which may encourage the growth of foreign investor participation in China's bond markets.

Recommendation:

Broadening the access for foreign investors to participate in the on-shore repo market - will improve liquidity, market volatility and support mid-long term price stability. This would be further enhanced – as described in the section 3.e. below – by allowing triparty agents to post bonds held in CIBM as collateral to receive RMB onshore.

3c. Enforceability of Close-out Netting for Repos and SBL

- **Recognition of the Global Master Repurchase Agreement (GMRA) as the standard repo master agreement in China**

GMRA is recognized as the market standard master agreement for repos, underpinning a notional market of almost USD 1 trillion. Financial institutions rely on the enforceability of GMRA's provisions to apply netting and reduce their capital requirement in compliance with BIS Basel III provisions.

Unlike the pledged repo documented under the NAFMII repo master agreement (2013) which is widely used in the onshore market, market participants exchange the subject bonds on a title transfer basis under the GMRA. This means that the GMRA provisions are similar to the other Master Agreements that are expressly recognised under the *Notice on Issues Concerning the Measurement Rules for the Default Risk Assets of Derivatives Counterparties (No. 124 [2021] of the CBIRC General Office)* (《关于衍生工具交易对手违约风险资产计量规则有关问题的通知》) (the "CBIRC Notice") together with an explanatory press note ("中国银保监会有关部门负责人就《关于衍生工具交易对手违约风险资产计量规则有关问题的通知》答记者问")(the "Explanatory Note") in November 2021 in use in China in respect of issues such as close-out netting and title transfer collateral (which relies on enforceability of close-out netting to be effective).

Recommendation:

ASIFMA welcomed the CBIRC Notice's clarifications and the provisions under Appendix 9 paragraph 2(5) of the *Administrative Measures for the Capital of Commercial Banks (Draft for Comment)* (《商业银行资本管理办法（征求意见稿）》) of the PBOC/CBIRC (the "Draft Capital Rules", issued on 18 February 2023 for public comments) that support the enforceability of close-out netting for Repos in China and applicability of netting for Risk Weight calculation. Taking into account the ubiquitous role of ICMA's GMRA in the global repo market and its similarity to other Master Agreements already recognized by PBOC and CBIRC, we recommend that the PBOC and CBIRC to explicitly recognize the

GMRA as a legally valid master netting agreement as contemplated by the "Draft Capital Rules", CBIRC Notice and more broader PRC law.

- **Including the enforceability of close-out netting in statute**

With respect to close-out netting, there are regulatory changes progressively aligned China's regulatory framework with other major financial market jurisdictions over the past two years. The most noteworthy legislative development is that the *Futures and Derivatives Law* (《期货和衍生品法》) (FDL), took effective on 1 August 2022, explicitly recognized the legal effect of close-out netting in China for OTC derivatives trading, making close-out netting to be recognized and protected at the statute level in China.[63]

Whilst it is clear that the FDL does not cover bond repos, market participants are actively considering the enforceability of close-out netting with respect to repos under other master agreements generally, including the GMRA.

The CBIRC Notice together with the Explanatory Note provide financial institutions with some comfort on the enforceability of close-out netting for repos in China. It clarified that "qualifying master agreements for the purposes of the CBIRC Notice include the NAFMII Master Agreement and China Securities and Futures Markets Financial Derivatives Master Agreement commonly used in the onshore market as well as the 2002 ISDA Master Agreement commonly used in the international market", while the catch-all expression "other legal and effective master netting agreements approved by the CBIRC" is used to allow space for future policy development. However, unlike OTC derivatives under the FDL - this does not provide an equally strong legal basis since the CBIRC Notice and the Explanatory Note are not derived from a specific piece of legislation.

Recommendation:

It is recommended that regulators support the inclusion of specific provisions at a legislative level to protect close-out netting in respect of bond repo transactions such as under the draft *Financial Stability Law* (《金融稳定法(草案)》) or amendments to the *Enterprise Bankruptcy Law* (《企业破产法》).

It is also recommended for CSDCC to add clarity on the handling of pledged bonds in the event of a reverse repo party's bankruptcy in a repo transaction. For example, it is unclear under the relevant settlement rules and procedures whether pledged bonds will be automatically released by CSDCC (and if not, the release procedures), where a repo party pays back its borrowed money but the reverse repo party has bankrupted. That will give rise to uncertainty regarding the measurement of counter-party risks in a repo transaction.

[63] Article 35 of the *Futures and Derivatives Law* (《期货和衍生品法》).

- **Provide similar framework for SBL transactions under both local and international master agreements (e.g., GMSLA)**

The CBIRC Notice issued in November 2021 gave clarity for applicability for repo transactions (except those documented under GMRA), but not for SBL. Market participants are actively considering the enforceability of close-out netting with respect to SBL under other master agreements generally, including the Global Master Securities Lending Agreement (GMSLA). CIBM Direct and QFI investors can already engage in bond lending in CIBM for quite some time, but foreign participation has not been very active – reasons being the need to use NAFMII master agreement, uncertainty over close-out netting and tight lending fees.

Recommendation:

To allow similar framework for SBL, i.e., encouraging the recognition of the GMSLA as the master agreement in use in China and the inclusion of enforceability of close-out netting for SBL in law-making, would encourage the foreign participation in China bond markets and be welcomed by international institutions.

3d. Daily Margining on Repo/Bond Lending

The pledged repo in China does not permit the lender to rehypothecate or re-use the bond collateral, for example, to cover short positions, which reduces liquidity and collateral optimization and stifles the development of a more liquid repo market. On the default of the borrower, since the lender does not have the immediate and explicit right to liquidate collateral provided by the defaulting borrower, the lender is prevented from reducing their counterparty credit and liquidity risk exposures, at least not in a timely manner. In addition, there is no current margin payment mechanism or collateral mark-to-market process, which necessitates higher haircuts to compensate, resulting in limited liquidity for longer tenors.

Recommendation:

In light that the credit quality of the borrower should matter more under a pledged repo system (all else being equal), to the extent that it is more difficult for the lender to acquire the collateral that has been pledged in the event of a default, daily margin as well as a mark-to-market regime is valuable to be introduced in China repo market – it would facilitate longer dated repo and improve market liquidity by enhancing the attractiveness of the underlying assets for long-term investors and facilitate market makers and other participants who wish to lock in longer-term borrowings on their short positions. Therefore, such a move would benefit greatly not only foreign but also domestic investors and dealers.

3e. Collateral, Triparty and Global Custodian Connectivity

- **Using Bond Connect assets as collateral for Unclear Margin Rules (UMR) purposes**

Bond Connect is one of the most popular investment channels among foreign investors and there are increasing demand from market participants on using Bond Connect assets for collateral purposes, especially in relation to the BCBS-IOSCO framework for margin requirements for non-centrally cleared derivatives, also known as UMR.

There remain certain practical difficulties for a foreign institution to use onshore Bond Connect assets as eligible collateral and credit enhancement for UMR purposes. Firstly, one of the key requirements for Bond Connect assets to be eligible as initial margin under UMR is that, in the event of a default by the investor (which includes the investor becoming insolvent or entering into insolvency proceedings), the secured party will need the ability to liquidate the pledged Bond Connect assets through the investor's access to the Northbound Bond Connect to enforce its security interest "without any regulatory or legal constraints or third party claims (other than custodial liens or liens routinely imposed on all securities in a clearing system)". However, BCCL may exercise its suspension or termination powers of an investor's right to access the Northbound Bond Connect, which could act as a legal impediment to the liquidation of Bond Connect assets by the secured party, and thus prevent the above requirements for initial margin eligibility and legal certainty in respect of collateral enforcement from being satisfied[64]. Secondly, the limitation of having only one custodian can be a challenge for market participants to utilize the Bond Connect assets as collateral for UMR purpose, as the custodian of initial margin appointed by the collateral provider is restrained to the single Bond Connect custodian and it needs to be unaffiliated with both the collateral provider and the collateral receiver. In addition, as clients can only have one CMU account, it results in custodians having to ensure instructions are not released before positions are moved into the collateral provider's main account. This adds operational constraints for participants.

***Recommendation**:*

There is substantial demand from our members' wishing to use Bond Connect assets for UMR purposes. Therefore, addressing the above practical difficulties would be helpful to investors, and would enable a significant number of parties to be in a position to use Bond Connect assets.

- **Making the case for Bond Connect assets to be used for SWAP Connect margining requirements**

Generally, there are growing requirements for collateralisation in the global markets and, consequently financial institutions are looking to make available and optimizing their various pools of assets. With respect to Bond Connect, investors are looking to use their Bond Connect holdings as collateral for liquidity management and margining.

[64] Article 6.2.1 of the *BOND CONNECT COMPANY LIMITED ACCESS RULE BOOK (As of 9 June 2021)*(《债券通有限公司准入规则》2021 年 6 月 9 日更新).

Recommendation:

It is hoped that – as a first step – these Bond Connect holdings could be used for margining under Swap Connect first (and extended to other derivative transactions and purposes – see above paragraph on "Using Bond Connect assets as collateral for Unclear Margin Rules (UMR) purposes"). This could in turn increase the liquidity in the underlying securities market.

- **Encourage CCDC and SHCH to accelerate the development of their triparty services and their connectivity to international bilateral and triparty collateral managers.**

CCDC has developed over the years a comprehensive collateral management services such as collateral selection, valuation, pledge, release of pledge, marking to market and collateral adjustment. In 2018, the PBOC announced that a General Collateral (GC) triparty repo service will be launched in CIBM through CCDC, SHCH and CFETS.[65] Although some progresses have been made and some initiative led by the international triparty agents have allowed some usage of Chinese bonds as collateral, there is still work that needs to be done. As mentioned in the previous sections, a well-functioning repo market (bilateral and triparty) is critical to ensure liquidity and transparency of the bond market.

Recommendations:

ASIFMA therefore recommends that CCDC and SHCH continue the development of their triparty services and work on connecting their platform to international triparty (and bilateral) collateral managers, allowing a broader use of Chinese fixed income assets as collateral, both on- and off-shore.

- **Usage of Chinese bonds in offshore collateral management transactions**

Due to the current segregated account structure in CIBM Direct, it is not possible to mobilize Chinese bonds in offshore collateral management transactions. The bonds are 'locked' in the segregated accounts at CCDC/SHCH, meaning that any movement of securities (even for collateral management purposes) must take place onshore, rendering their usage as a collateralized instrument inefficient. The possibility to use (especially high-quality) bonds, such as CGBs, as collateral in bilateral/triparty repo transactions for refinancing purposes is tremendously important for international investors. A pre-requisite for it is to allow omnibus accounts and offshore settlement within the ICSD's /custodian bank's books offshore, without the needs for foreign investors to enter each trade through an onshore platform, as it is done today.

Recommendation:

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[65] *Circular on Matters Related to Third-Party Repos in the Inter-bank Bond Market* (PBOC Circular No. 18 [2018]) (《中国人民银行公告(2018)第 18 号—开展银行间债券市场三方回购交易有关事宜公告》) and the *Circular of SHCH and CFETS on Conducting the Clearing Business for General Collateral Triparty Repo Service* (《关于开展通用质押式回购交易清算业务的通知》).

To allow ICSDs and custodian banks to open an omnibus account at the level of CCDC / SHCH and offshore settlement within the ICSD's /custodian bank's books. Transparency on beneficial ownership could be met, e.g., via holding and sending transaction reports to PBOC and/or via market infrastructures.

- **Trading, Settlement and Custodian model**

Trading and Settlement Segregation under Bond Settlement Agent (BSA) model: Regarding the existing BSA model, BSAs in Chinese mainland are currently responsible for both trading and settlement in the CIBM.[66] By contrast, in global financial markets, trading and settlement functions are typically separated across different financial institutions. This means that within the Chinese mainland market, global custodians must instruct their local sub-custodians that their trading departments must not settle CIBM transaction. Failure to properly separate trading and settlement actions means that global custodians do not consider CIBM assets to be under their custody, with the consequence that foreign investor assets are not properly protected.

Recommendation:

We recommend that the PBOC adopts international best practices with respect to BSAs and requires that trading and settlement functions be separated.

Multi-layer Custodian Model: We would encourage the PBOC to nail down the detailed guideline for multi-layer custodian bank model under CIBM Direct. Foreign bank branches should be allowed to become the qualified local custodian under multi-layer custodian model under the CIBM Direct.

Recommendation:

We encourage the PBOC to consider the same practice that adopted by the CSRC, which allow foreign bank branches to conduct custody business to look through the parent company's capital capability in order to fulfil applicable net asset requirement.

4. Derivatives

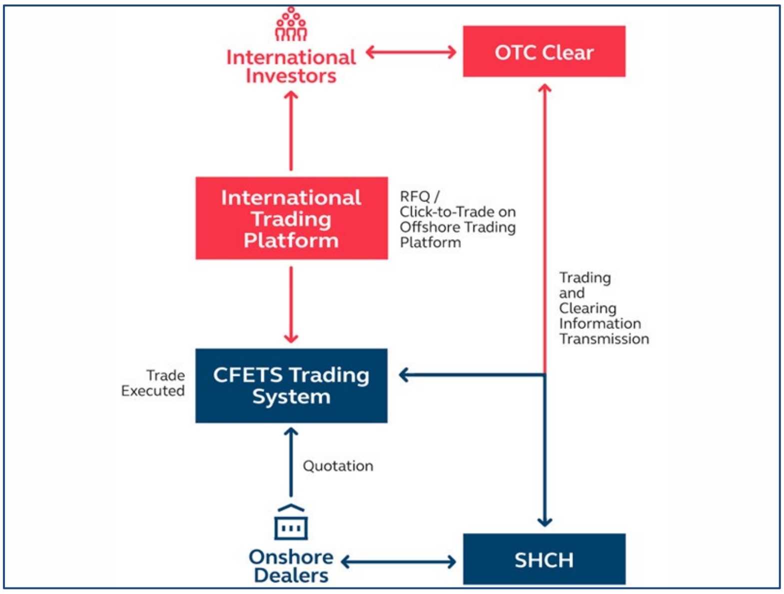
4a. OTC Derivatives

- **Taking stock on SWAP Connect launch**

[66] Paragraph 5 of the *Circular of the PBOC on the Relevant Issues concerning Launching the Bond Settlement Agency Business* (《中国人民银行关于开办债券结算代理业务有关问题的通知》).

The PBOC, the SFC and the HKMA jointly announced on 4 July 2022 the mutual access between interest rate swap markets in Hong Kong and the Mainland ("Swap Connect").[67] This was welcomed by the market as it would broaden the tools available for managing the interest risk on their bond portfolio. After one year of careful planning from a regulatory, trading and operational point of view, Swap Connect went live on 15 May 2023.

Figure 4: Trading and Clearing on the Swap Connect



Source: BCCL (Bond Connect Company Limited)

- **Tax issue related to Swap Connect**

There is an absence of clear guidance on the PRC tax treatments in relation to Interest Rate Swap (IRS) by Hong Kong market investors via Swap Connect. We hope that SFC can coordinate with Mainland China authorities (including PBOC, MOF and STA) to jointly look into clarifying the PRC tax treatments. We would like to propose that income to be derived by Hong Kong market investors from IRS transactions conducted via Swap Connect are not taxable from both PRC Corporate Income Tax (CIT) and PRC Value Added Tax (VAT) perspectives. This recommendation is aligned with various tax exemption under Stock Connect and Bond Connect, and the trend of steadily promoting the opening up of the financial sector and deepening the connectivity between domestic and foreign capital markets proposed in the Outline of the Fourteenth Five-Year Plan of the People's Republic of China (《中华人民共和国国民经济和社会发展第十四个五年规划》).

From PRC VAT perspective, under the proposed IRS via Swap Connect, (i) there is only net settlement of fixed and floating interest rate difference with no associated loan principal and no lender-borrower

[67] Joint Announcement of the PBOC, the SFC and the HKMA, http://www.pbc.gov.cn/en/3688110/3688172/4437084/4593471/index.html.

or creditor-debtor relationship inter-se between the parties, therefore the net settlement of IRS derived by HK investor via Swap Connect should not be treated as interest income; (ii) while IRS is a derivative, there is no transfer of ownership of a derivative, therefore the net settlement of IRS should not be treated as income derived from transfer of derivatives as defined in the Circular No. 36 [2016] of the MOF ("Circular 36") [68] and thus should not be subject to PRC VAT.

From PRC CIT perspective, under the proposed IRS via Swap Connect, there is only net settlement of fixed and floating interest rate difference with no associated loan principal and no lender-borrower or creditor-debtor relationship inter-se between the parties, therefore the net settlement of IRS derived by HK investor via Swap Connect should not be treated as interest income. In addition, according to Circular Guoshuihan [2004] No.753 ("Circular 753") which is issued under the old Foreign Enterprise Income Tax regime and no longer effective, only if a PRC entity has a financing transaction with an offshore creditor or the effective offshore creditor due to shareholding relationship (Note 1) and then enters into an IRS with the same offshore creditor with respect to the underlying financing transaction, the net IRS settlement amount paid by the PRC entity to the offshore creditor shall be treated as interest income and subject to PRC Withholding Income Tax (WHT).[69] Circular 753 can serve as a good reference to reach that under Swap Connect, given that there is no underlying corresponding financing transaction and no lender-borrower or creditor-debtor relationship inter-se between the parties, the net IRS settlement derived by HK investor via Swap Connect should not subject to WHT.

Recommendation:

The income to be derived by Hong Kong market investors from IRS transactions conducted via Swap Connect are not taxable from both PRC Corporate Income Tax and PRC Value Added Tax perspectives, so as to align with various tax exemption under Stock Connect and Bond Connect.

- **Level playing field amongst foreign investors accessing IRD**

In recent years, foreign institutions have shifted more asset allocation to RMB bond assets. With the rapid increase in their investment size in China's bond market, their needs for managing the interest rate risk increases accordingly, bringing a growing demand for trading onshore interest rate derivatives.

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[68] "Annex: Explanatory Notes on the Sales of Services, Intangible Assets and Immovable Properties" of the *Circular on Implementing the Pilot Program of Replacing Business Tax with Value-Added Tax in an All-round Manner (No. 36 [2016] of the MOF)* (《关于全面推开营业税改征增值税试点的通知（财税〔2016〕36 号）》).

[69] Article 3 and 4 of the *Circular on the Relevant Issues concerning the Withholding of Income Tax on Swap Transaction of Financing Business Carried out by the Enterprises in China with Foreign Enterprises (Circular Guoshuihan [2004] No.753)* (《关于中国境内企业与外国企业进行融资业务掉期交易扣缴所得税有关问题的通知（国税函[2004]753 号）》).

CIBM Direct and QFI investors are currently allowed to trade onshore interest rate derivatives for hedging purpose. For Bond Connect, since its establishment in 2017, it has been a crucial infrastructure to foreign investors who have strong appetite for China's fixed income market and investors wish to access onshore risk management tools to facilitate hedging of interest rate risk arising from their onshore Bond Connect investments as well. Demands from investors rise quickly to streamline the CIBM Direct, Bond Connect and QFI channels in terms of permissible investment instruments, so that all investors could have access to hedging tools and funding products such as bond futures, interest rate swaps, and bond repo.

Recommendation:

Being able to access the aforementioned products are essential to support bond market dealers, asset managers, pension funds, and insurance companies and it would sustain and further enhance the liquidity of the onshore bond market as a whole.

- **Broader adoption of ISDA/CSA (vs NAFMII) for OTC derivatives following the enactment of the FDL in August 2022.**

The FDL requires the master agreement adopted in OTC derivatives trading to be filed for record with PRC regulators.[70] Though signals given in the FDL for respecting derivatives market practices are welcomed, it is still unclear what are the implications of the filing requirement on the application of widely used master agreements released by international industry associations, such as ISDA/CSA.

For foreign investors, when using China access channels, the ability to continue their transaction practices, is of key importance. Giving investors options to use, where agreed by relevant parties, legal documentation used in other markets such as ISDA/CSA, and the GMRA will greatly increase confidence and desire to invest, which would likely lead to increasing in offshore institutions participating in onshore OTC derivatives markets.

- **Exchange of margin under UMR post the Futures and Derivatives Law**

Under BCBS IOSCO's UMR, counterparties must exchange margin on OTC derivatives contracts that aren't cleared through a central counterparty (CCP). It provides two types of margin that counterparties must exchange, i.e., the variation margin (VM), which covers current exposure and is calculated using a mark-to-market position, and the initial margin (IM), which covers potential future exposure for the expected time between the last VM exchange and the liquidation of positions on the default of a counterparty. Initial margin protects the transacting parties from the potential future exposure that could arise from future changes in the mark-to-market value of the contract during the time it takes to close out and replace the position in the event that one or more counterparties default. In most cases IM will be exchanged on a T+1 basis. IM must be held and segregated through a third-party custodian and rehypothecation of IM is not permitted.

[70] Article 33 of the *Futures and Derivatives Law* (《期货和衍生品法》).

It is currently not common practice for onshore financial counterparties to exchange margin to cover domestic OTC derivative exposures. International markets believe that clear netting rules, a legal framework supporting collateral enforceability, and technical and market infrastructure to support the exchange of margin that contribute individually and jointly to supporting the smooth and efficient functioning of all financial markets would help reduce the cost of hedging and increase the efficiency of derivatives as risk mitigation tools.

Recommendation:

Although most OTC Interest Rate Derivatives are mandated to be centrally cleared in China, market participants recommend that exchange of margin under UMR to be implemented in China at some point to align with practices with other markets and allow foreign investors to comply with their home jurisdictions requirements when transacting cross-border with their China based counterparts.

- **Outcome of the consultation on Promoting the Proper Development of Derivatives Business**

On 3 December 2021, the PBOC, jointly with the CBIRC, the CSRC, and the SAFE, drafted the *Guiding Opinions on Promoting the Regulation of Derivatives Business (Consultation Paper)* (《关于促进衍生品业务规范发展的指导意见（征求意见稿）》) (the "Guiding Opinions"). The Guiding Opinions can be regarded as a "super guidance" for OTC derivatives businesses. PBOC aims to formulate a set of general regulatory standards and principles in a macro-prudential approach to uniformly address different types of derivatives service providers (particularly banking and insurance institutions regulated by the CBIRC, and securities and futures servicing institutions regulated by the CSRC).During the consultation period, we would wish that the PBOC could clarify, among other issues, 2 provisions in the proposed guidance that the industry found problematic, – 1) impact on wealth management products, i.e. whether the guidance will cover wealth management product; and 2) impact on cross-border hedging through derivatives i.e., definition of hedging, in light of the stipulations that "Unless provided otherwise, banking and insurance institutions in principle shall not conduct cross-border non-hedging OTC derivatives trading"[71] and that "cross-border derivatives business mainly refers to OTC derivatives trading carried out between a domestic financial institution and an overseas counterparty, or other circumstances prescribed by the relevant financial regulatory authorities"[72]. The consultation period ended on 18 December 2021. To date, it remains to be seen when the Guiding Opinions will be finalized and officially published.

4b. CGB Futures

- **HKEX's MOF T-Bond Futures launch**

[71] Article 17 of the *Guiding Opinions on Promoting the Regulation of Derivatives Business (Consultation Paper)* (《关于促进衍生品业务规范发展的指导意见（征求意见稿）》).

[72] The Explanatory Note to the *Guiding Opinions on Promoting the Regulation of Derivatives Business (Consultation Paper)* (《关于促进衍生品业务规范发展的指导意见（征求意见稿）》).

In the past few years, China has made several strides to facilitate foreign investors to access China's interbank bond market and has passed on a message to the market that China is on the way to further open its domestic capital market. Meanwhile, the formal inclusion of RMB into the SDR basket in 2016 also increased the demand for RMB bond assets. Global investors, including global fund managers, started to consider reallocating funds into RMB debt securities, especially the PRC sovereign bonds. Considering that bond futures with better liquidity can help foreign investors improve their ability to hedge against interest rate risks via risk transfer and channelling, the access to bond futures may increase foreign investors' willingness to hold a larger portion of Chinese bond assets.

In this context, in March 2017, Hong Kong Futures Exchange Limited (HKFE) announced that the SFC approved the introduction of the MOF T-Bond Futures contracts.[73] The trading of the MOF T-Bond Futures contracts was introduced under a pilot scheme as the offshore markets' first futures on domestic Chinese government bonds.

In light of the official launch of Bond Connect on 3 July 2017, and given that clearer regulatory requirements and cooperation between Hong Kong and the Mainland are needed to support the further development of offshore derivatives on the Mainland underlying in Hong Kong, HKEX decided to suspend the pilot MOF T-Bond scheme after the expiry of the December 2017 contract.

Recently in September 2022, the Vice Chairman of the CSRC Fang Xinghai has publicly spoken at the China International Fair for Trade in Services and 2022 China International Finance Annual Forum that CSRC will work together with relevant domestic regulators and Hong Kong regulators to launch several new policy moves to expand the cooperation between Mainland capital market and Hong Kong capital market, including supporting Hong Kong launching CGB futures and accelerate the process to allow foreign access to the domestic CGB futures market.[74] Since then the HKEX has sought regulatory approvals and worked with the industry and ASIFMA for the relaunch of HKEX's MOF T-Bond Futures in the near future.

- **Accelerate foreign investors direct access to onshore CGB futures**

An active, liquid, and well-supervised government bond futures market would allow participants to hedge large positions quickly and reduce risk more effectively, while deepening the underlying bond and derivatives markets. Availability of hedging instruments is key to attracting international investors, our 2020 survey confirmed. Looking at the deepest and most liquid bond markets in the world, bond futures clearly enhance the liquidity of the underlying cash markets as market participants are able to manage risks of their bond inventories more effectively. Additionally, bond futures markets are

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[73] HKEX to Introduce 5-Year China Ministry of Finance Treasury Bond Futures, https://www.hkex.com.hk/News/News-Release/2017/1703242news?sc_lang=en.

[74] Fang Xinghai's Speech at China International Finance Annual Forum 2022, http://www.csrc.gov.cn/csrc/c100028/c5603389/content.shtml.

especially beneficial to market-makers because futures enable them to hedge their positions, thus reducing efficiently their market risk and allowing them to provide more robust liquidity to investors.

China launched 10-year government bond futures on the CFFEX in March 2015, two years after officially listing five-year government bond futures for trading. A two-year CGB futures contract was launched in 2018, but with modest trading to date. In April this year, CSRC gave CFFEX the green light to launch 30-year CGB futures with the first of three contracts listed for trading shortly after.[75] Banks have a real need to hedge their bond positions, especially for one to three-year CGBs, and would like to be allowed to trade CGB futures. However, to date, a limited number of domestic banks and only one foreign bank are allowed to participate directly in the futures market, which they need to be as the major holders of bonds. As the big five domestic banks own the vast majority of the issued government bonds, their limited activity in the market is hampering liquidity and therefore undermines the use of CGB futures as a cheap and effective way to hedge.

Recommendation:
In order to allow greater liquidity, transparency and increase foreign investors' participation, we encourage the regulator to broaden and accelerate the scope of eligible institutions to directly access the Government Bond Futures market.

- **QFI further opening-up of listed derivatives trading beyond "hedging" purpose**

With regard to bond-type and interest-rate-type derivative products, the PBOC has clarified in the *PBOC Circular [2016] No. 3* and its follow-up Q&A session that QFI may conduct bond lending, bond forwards, forward interest rate agreements, and interest rate swaps based on hedging purposes.[76] As for forex-type derivative products, the *Administrative Provisions on Funds for Securities and Futures Investments in China by Foreign Institutional Investors* (《境外机构投资者境内证券期货投资资金管理规定》) and the Q&A's jointly issued by the PBOC and the SAFE on 7 May 2020 specify that QFI may trade forex derivative products based on its genuine needs to hedge against forex risk exposures arising from their domestic securities investments.[77] Further, the *Provisions on 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和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》)

[75] Circular of CFFEX on the Listing and Trading of 30-year CGB futures, http://www.cffex.com.cn/jystz/20230414/32098.html.
[76] Q&A session of PBOC of *PBOC Circular [2016] No. 3,* http://www.pbc.gov.cn/goutongjiaoliu/113456/113472/3070371/index.html.
[77] Articles 16, 17 and 18 of the *Administrative Provisions on Funds for Securities and Futures Investments in China by Foreign Institutional Investors* (《境外机构投资者境内证券期货投资资金管理规定》).

also emphasize that the SAFE only allows QFI to trade forex derivative products based on hedging purposes.[78]

Under the current QFI rule regime, QFIs can invest in financial futures contracts listed and traded on the CFFEX, while the specific varieties and trading methods of financial futures that QFIs can participate in are subject to the approval of the CSRC. Presently, QFIs can only invest in stock index futures listed and traded on the CFFEX but cannot participate in CGB futures trading yet.

Recommendation:

At the current stage, PRC regulators still insist that QFIs must trade financial futures for hedging purposes. However, the existing laws and regulations do not explicitly require QFIs to trade commodity futures for hedging purposes. We expect PRC regulators consider QFIs' further opening-up of listed derivatives trading beyond "hedging" purpose in the future.

- **Other recommendations related to onshore futures and listed markets**

In addition to the above, we also expect the regulators to consider the following ***recommendations****:*

(1) Overseas Intermediaries or Overseas Brokers (OIs / OBs) are offshore entities that do not trade directly on onshore exchanges but are authorized to set up accounts with domestic futures firms on behalf of international clients. As of May 2023, there are over 80 approved OIs / OBs on Shanghai International Energy Exchange, over 80 approved OIs / OBs on Dalian Commodity Exchange and over 50 approved OIs / OBs on Zhengzhou Commodity Exchange, including firms from Hong Kong, Singapore, France, Germany, Switzerland, Netherlands, Japan and the UK.[79] However, no US entity has been approved as an OI or OB on onshore futures exchanges to date, while US regulations require that US investors invest via a US futures broker. As a result, US investors are unable to participate in China's onshore futures markets despite China's ongoing commodity futures internationalization. Additionally, non-US investors are also affected because many choose to clear their global futures flows via US CFTC-regulated intermediaries, given the significant time and resources involved in establishing clearing relationships with additional intermediaries. To date, Chinese regulators and futures exchanges still have not proceeded with approving US firms' OI/OB applications.

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[78] Item 8, Paragraph 1, Article 6 of the *Provisions on 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和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》).

[79] The list of QIs / QBs of INE, https://www.ine.cn/eng/services/members/overseaagency/;
the list of DCE, http://www.dce.com.cn/dalianshangpin/gywm7/jyshy/jwjjgmd/index.html;
the list of ZCE, http://english.czce.com.cn/en/Services/MemberServices/OverseasBrokers/H81050204index_1.htm.

We recommend Chinese regulators to broaden and accelerate foreign investors direct access to the onshore futures markets and the approval of US futures brokers to become Overseas Intermediaries (OIs) / Overseas Brokers (OBs) to onshore futures exchanges.

(2) Harmonization of rules and contracts between Overseas Intermediary (OI) and QFI eligible contracts. Currently, some contracts are exclusive to OI or QFI.

(3) Simplification of the registration process and streamlining of documentation requirements for foreign investors of OI.

(4) Approve US entities, regardless of US persons percentage of ownership of entity, to be eligible to apply as a foreign investor via an OI.

(5) Introduce the concept of market makers in the futures/ listed space as such a concept does not currently exist. This will increase the liquidity and vibrancy of the market.

5. Others

5a. Synchronization of Onshore Clearing Infrastructure with Offshore Bond Market (Free Trade Zone Bond, Yulan Bond, etc.)

FMIs have enhanced their capabilities to offer international investors new products and channels. In 2020, the SHCH cooperated with Euroclear on the offering of "Yulan Bond"[80] which are Chinese corporate bonds denominated in foreign currencies, issued through the SHCH. CCDC developed a program aiming to support the Shanghai free-trade-zone bond issuances that saw its maiden issuance in 2019 but that really picked up in the first quarter of 2023.

It requires additional steps for offshore investors to leverage such infrastructure (e.g., opening account with CCDC directly or via trustee), which may limit their participation in such programs or instruments. Further synchronization and connectivity between onshore and offshore clearing infrastructures would therefore be welcome by offshore investors.

5b. Onshore Licensing of International Rating Agencies

To continue the opening of its financial market to international practitioners, China has allowed international rating agencies (IRA's) to establish wholly owned onshore entities and provide domestic rating services. S&P and Fitch now both have active licenses in the interbank bond market. As IRA's may provide onshore investors with different perspectives and offshore with comparable assessments,

[80] Announcement of SHCH of the offering of "Yulan Bond", https://www.shclearing.com.cn/gywm/xwdt/202102/t20210204_810719.html.

we recommend the regulators to further grant access to these international firms and guarantee the level playing field with their domestic peers.

5c. Circular 108: Scope of "Bonds" Eligible for Exemption Under the Interbank-Exchange Bond Market Connect Mechanism

The Chinese tax authority provided relevant tax preferential policies to the foreign investors who invest in the Chinese bond market, i.e., Circular Caishui [2018] No. 108 ("Circular 108") and Notice [2021] No. 34 of Ministry of Finance (MOF) and State Taxation Administration (STA) ("Notice 34") provide CIT and VAT exemption policies on bonds interest income generated from Chinese bond market.[81] Circular 108 and Notice 34 should be a significant step in opening the bond market in China and attracting more foreign capital by providing tax exemption for bond investment in China.

However, there is still some market uncertainty with regard to scope of debt instruments eligible for such exemption. Besides traditional bonds such as government bonds, financial bonds, corporate bonds, there are many new types of debt instruments with the same characteristics as bonds, including Asset backed notes (ABN), Asset-backed securities (ABS), Private Publication Notes (PPN) and Interbank Certificates of Deposit (CDs). We recommend promoting consensus among MOF, STA and other related authorities to provide a further clarification on the scope of "bonds" that are eligible for the exemption treatment. In other words, the exemption from CIT and VAT for interest income derived by foreign investors should be applied to all "debt instruments" including deposit instruments such as CDs regulated by the CSRC, PBOC or other relevant authorities, and issued and traded in the China market legally.

If the other debt instruments traded in China market cannot fall in the scope of "bonds" that are eligible for the exemption, we recommend the tax authorities to provide an effective withholding mechanism on the interest income derived by foreign investors. In addition, when designing the withholding mechanism, we recommend considering the collection details caused by the complexity of the trading. For example, when an investor purchases the debt instruments/negotiable certificates of deposit (NCDs), the interest income may have already included in the purchase price. The withholding policy shall clarify the taxable base under this situation (interest income on cash basis or accrual basis); otherwise, it may cause tax fairness problems for different investors. Therefore, if the other debt instruments do not fall in the scope of exempted "bonds", a clear and effective withholding mechanism will be significant for the development of China's bond market.

Recommendations for Fixed Income
In respect of **CIBM:**
1. Expedite CIBM market-maker application process and begin approval of foreign firms.

[81] The Circular 108 provides that from November 7, 2018 to November 6, 2021, overseas institutions will be exempt from CIT and VAT on their interest income generated from investments in Chinese bond market. The Notice 34 extends the aforesaid period to December 31, 2025.

2. Simplify administrative procedures on non-trade transfer of CGBs between CIBM Direct and QFII of the same registered investor.
3. Raise or remove dual currency ratio.
4. Allow omnibus account structure with recognition of foreign nominee concept.

In respect of **Northbound Bond Connect:**

5. Allow only change in settlement date for rolling settlement.
6. Not treat a change in settlement date as a failed trade thereby obviating the need to file a failed trade settlement report.
7. Allow failed trade settlement to be reported electronically.
8. Allow CFETS accounts to be registered in both the name of the asset manager and the client (as with the QFI account structure).
9. Allow non-trade transfers when there is a change in asset manager but not client.

In respect of **Southbound Bond Connect:**

10. Increase quota and number of market makers.
11. Broaden scope of eligible assets and clarify what is in scope.
12. Enlarge eligible investors base.
13. Allow additional custodians and market makers to join the programme.

In respect of **Bond Connect generally:**

14. Simplify operational and trading processes.
15. Simplify and streamline documentation process for onshore currency hedging under Bond Connect.
16. Decouple CIBM market-maker status from Bond Connect market-maker status so that eligible foreign banks and foreign securities firms operating in China can apply for the Bond Connect market-maker directly.
17. Align access channels to the same markets (such as CIBM Direct and Bond Connect to the CIBM).
18. Approve the launch of Inter-connection between CIBM and Exchange Bond Market as soon as possible.
19. Develop trading protocols onshore, specifically the ability to request and quote two-way prices and the ability for market participants to counter levels dynamically.
20. Continue the panda bond market reforms to attract more international issuers and investors.

In respect of **Bond repo and bonds lending and borrowing:**

21. Allow international investors to access the bond repo market from offshore through a Northbound Connect channel.
22. Allow triparty agents to post bonds held in CIBM as collateral to receive RMB onshore.
23. Recognise the Global Master Repurchase Agreement (GMRA) as a legally valid standard repo master agreement in broader PRC law.
24. Include the enforceability of close-out netting in respect of bond repo transactions in statute.
25. Clarify the handling of pledged bonds with CCDC in the event of a reverse repo party's bankruptcy in a repo transaction.
26. Provide similar framework for SBL transactions under both local and international master agreements (GMSLA), i.e., encouraging the recognition of the GMSLA as the master agreement in use in China and the inclusion of enforceability of close-out netting for SBL in law-making.

27. Introduce daily margin as well as mark-to-market regime in China repo market.

In respect of **Use, custody, and settlement of onshore bonds:**

28. Allow use of Bond Connect assets as collateral for UMR (Unclear Margin Rules) purposes and SWAP Connect margining requirements (and extended to other derivative transactions and purposes).
29. Develop triparty services and connect CCDC and SHCH platform to international triparty (and bilateral) collateral managers, allowing a broader use of Chinese fixed income assets as collateral both on- and off-shore.
30. Allow ICSDs and custodian banks to open an omnibus account at the level of CCDC / SHCH and offshore settlement within the ICSD's /custodian bank's books under CIBM Direct.
31. Adopt international best practices with respect to BSAs (Bond Settlement Agent) and require that trading and settlement functions be separated under CIBM Direct.
32. Nail down detailed guideline for multi-layer custodian bank model under CIBM Direct.
33. Allow foreign bank branches to become qualified local custodian under multi-layer custodian model under CIBM Direct.
34. Allow foreign bank branches to conduct custody business to look through the parent company's capital capability in order to fulfil applicable net asset requirement.

In respect of **OTC Derivatives:**

35. Income to be derived by Hong Kong market investors from Interest Rate Swap transactions conducted via the Swap Connect be non-taxable from both PRC Corporate Income Tax and PRC Value Added Tax perspectives.
36. Streamline the CIBM Direct, Bond Connect and QFI channels in terms of permissible investment instruments, so that all investors can have access to hedging tools and funding products such as futures, interest rate swaps and bond repo.
37. Broader adoption of ISDA/CSA (vs NAFMII) for OTC derivations following the enactment of the FDL.
38. Implement exchange of initial margin under UMR to align with practices of other markets and allow foreign investors to comply with their home jurisdiction requirements when transacting cross-border with their China based counterparts.
39. Finalize and publicize the Guiding Opinions on Promoting the Regulation of Derivatives Business (Consultation Paper).

In respect of **CGB Futures:**

40. Launch HKEx's Chinese bond futures product as soon as possible.
41. Accelerate foreign investors direct access to onshore CGB futures.
42. Remove restriction for QFIs to trade financial futures for hedging purpose only.
43. Allow US futures brokers to become Overseas Intermediaries / Overseas Brokers to onshore futures exchanges.
44. Harmonise rules and contracts between Overseas Intermediaries (OI) and QFI.
45. Simplify registration process and streamline documentation requirements for foreign investors of OI.
46. Approve US entities to be eligible to apply as a foreign investor via an OI.
47. Introduce concept of market makers in the futures / listed space.

In respect of **Other Fixed Income Matters:**

48. Market alignment with international best practices – synchronisation of onshore clearing infrastructure with offshore bond market.
49. Further grant access to international rating agencies and guarantee the level playing field with their domestic peers.
50. Expand the scope of bonds eligible for exemption from CIT and VAT under Circular 108 for interest income derived by foreign investor to include all debt instruments with the same characteristics as bonds, including Asset backed notes ("ABN"), Asset-backed securities ("ABS"), Private Publication Notes ("PPN") and Interbank Certificates of Deposit ("CD") and provide withholding mechanism for debt instruments traded in China market that are not in scope.

E. Foreign Exchange

1. Introduction

The use and influence of RMB has continued to grow over the last three years with a significant increase in global RMB FX volumes recorded between April 2019 and April 2022. CNY is now the 5th[82] (2019: 8th) most widely traded currency globally driven by an 81% increase in the volume of spot and a 69% increase in FX swap transactions since 2019.

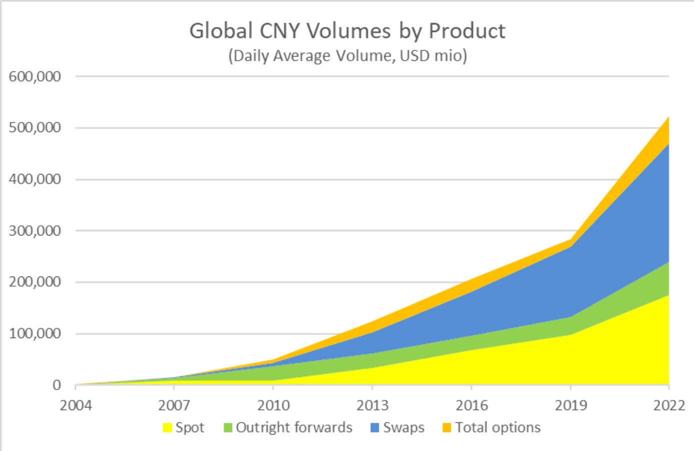
The majority of this growth has been driven by trading in Hong Kong, London, New York and Singapore where volume has increased by 78%, 163%, 181% and 138% respectively since 2019. The two largest trading centres are now Hong Kong and London which, combined, account for 50% of global volume.

In 2019, the Chinese mainland was the second largest CNY trading centre, behind Hong Kong, with 28.1% of global volume traded onshore (see the below *Figure 6: CNY Traded by Location*). However, in 2022 volume in China had fallen to 17.4% of global volume.[83]

The onshore CNY market, in April 2022, with a daily average volume of USD 89 billion[84], is nearly 70% smaller than the size of the offshore CNH market at the same time. In fact, the CNY market continues to be small in relation to China's GDP and its economic links with the rest of the world. In April 2022, China's FX derivative market turnover was only 3% of GDP compared with 30% of GDP for USD and 6% for the median EME currency[85].

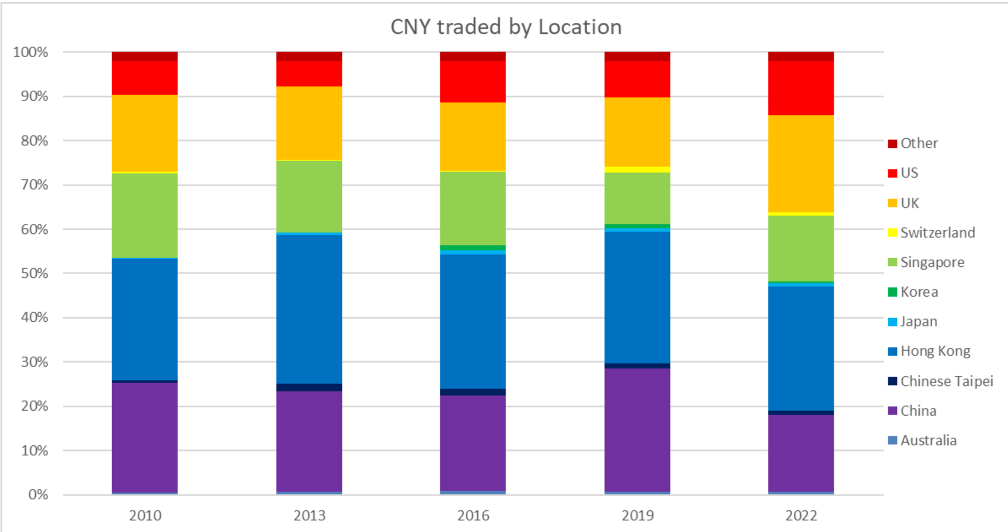
[82] OTC foreign exchange turnover in April 2022, https://www.bis.org/statistics/rpfx22_fx.htm.
[83] Offshore CNH market paces into new era, http://www.china-cer.com.cn/guwen/2023010322812.html.
[84] Overview data of China's foreign exchange market transactions, https://www.safe.gov.cn/safe/zgwhscjygk/index.html.
[85] BIS Quarterly Review - International banking and financial market developments (December 2022), https://www.bis.org/publ/qtrpdf/r_qt2212.pdf.

Figure 5: Global CNY Volumes by Product (2004-2022)



Source: BIS

Figure 6: CNY Traded by Location



Source: BIS

2. Offshore Market

2a. RMB Internationalisation

While there is no standard path to internationalisation, the process typically combines sequential and incremental steps involving, firstly, the exchange rate regime by allowing the rate to be determined increasingly by the market, and then convertibility of the capital and current account prior to the full liberalisation of the capital account to ensure the liquidity of, and confidence, in the currency. In the case of China, the internalisation has taken a different trajectory with the increased international usage of the currency taking place without its full transferability and convertibility in a regime where rates are typically managed.

The benefits of internationalisation are clear:

a. Reduce FX risk facing Chinese firms,

b. Improve the funding efficiency of Chinese financial institutions, enable them to increase their international competitiveness,

c. Increase the effectiveness of domestic monetary policy by making the market more liquid and thereby making market interest rates more sensitive to changes in the official rate,

d. Use of RMB as an invoicing currency for the settlement of cross-border transactions,

e. Increase the volume of cross-border transactions, and

f. Assist in preserving the value of foreign exchange reserves.

i. Use of RMB as an invoicing currency/payment currency

A key component of China's policy for internationalisation of the RMB has been the promotion of the external use of RMB to settle current account transactions. Cross-border trade settlement was launched on a trial basis in July 2009. It was initially restricted to selected firms in five regions in the Mainland for trading with Hong Kong, Macao SAR and ASEAN countries. The trial scheme ended in 2012 when all Mainland firms and current account transactions became eligible for invoicing and settlement in RMB.

However, the use of RMB as a global payment currency has actually decreased over the last two years despite its promotion – while RMB is the fifth most used currency its share as a global payment currency has little changed from 2.2% in February 2021 to 2.19% in February 2023. In February 2019, the RMB share of global payments was 1.85%[86].

Despite the recent plateauing in the use of RMB for cross-border settlement, there is particular demand in countries participating in the Belt and Road Initiative (BRI) and the Regional Comprehensive Economic Partnership (RCEP)[87].

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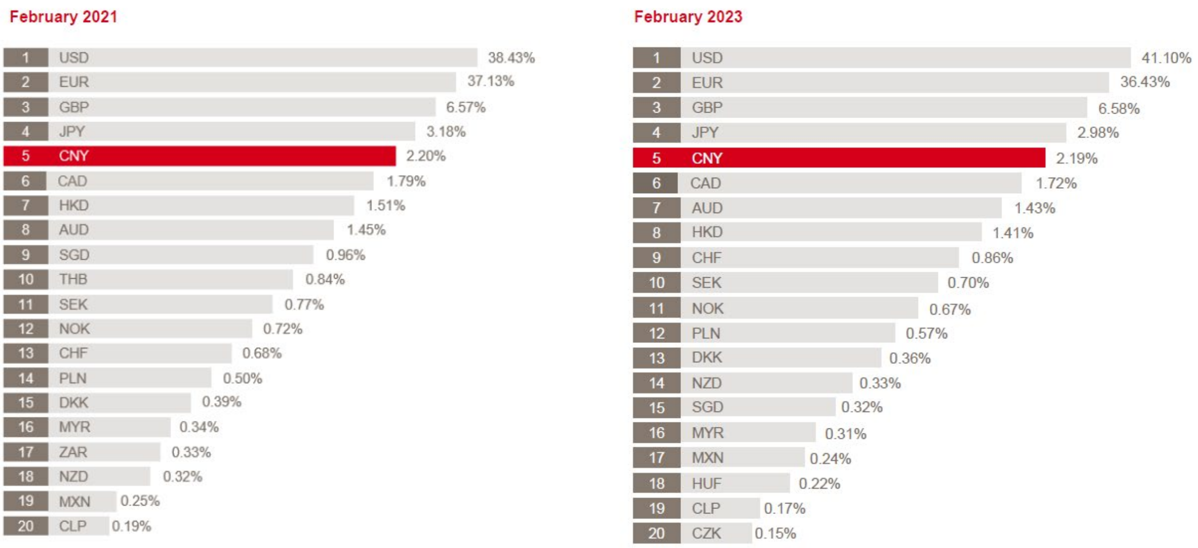
[86] RMB Tracker, https://www.swift.com/our-solutions/compliance-and-shared-services/business-intelligence/renminbi/rmb-tracker/rmb-tracker-document-centre?page=5.

[87] The Regional Comprehensive Economic Partnership (RCEP) is a free trade agreement between the ten member states of the Association of Southeast Asian Nations (ASEAN) (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, Vietnam) and its five FTA partners (Australia, China, Japan, New Zealand and Republic of Korea). The RCEP is the world's largest free-trade zone, accounting for about 30% of the world's population, trade volume and GDP.

- In BRI countries, use of RMB for trade and investment has grown as Chinese corporates use RMB more frequently for invoicing in construction, trade with the Mainland as well as local investment. As a result, a growing number of local entities are prepared to hold RMB.

- For the last two years, ASEAN has been China's largest trading partner; based on data from the General Administration of Customs bilateral trade reached CNY 6.52 trillion in 2022, accounting for 15.5 percent of China's total foreign trade[88]. Consequently, there has been a growing acceptance of RMB for cross-border payment across the RCEP. Furthermore, as evidence of regional monetary cooperation, China and Indonesia implemented the Local Currency Settlement (LCS) framework[89] that allows the use of both the rupiah and CNY in bilateral transactions processed via approved currency dealers without the need for a USD intermediary stage. In addition, the framework facilitates the use of direct exchange rate quotations and the loosening of certain regulations related to FX transactions between the two currencies.

Figure 7: RMB Share as a Global Payments Currency



Source: SWIFT RMB tracker for Mar 2023

In its 2022 RMB Internationalisation Report[90], the PBOC states that, in the next stage of internationalisation, China will continue to open up its financial market in a full-scale-regime way (全面制度型开放) and improve the liquidity of RMB assets. China will also provide a more convenient way for foreign investors to invest in China markets by diversifying investable assets and encouraging

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[88] Press conference transcripts by the Spokesperson for the General Administration of Customs, https://www.gov.cn/xinwen/2023-01/13/content_5736993.htm.

[89] 2021 RMB Internationalization Report, https://www.gov.cn/xinwen/2021-09/19/5638362/files/652d7b67eb94463f925be3985fcdb860.pdf.

[90] 2022 RMB Internationalization Report, http://www.gov.cn/xinwen/2022-09/24/content_5711660.htm.

foreign investors, especially central banks, to allocate more RMB assets. This will involve the promotion of the two-way opening up of the financial market and the interconnection of the onshore and offshore RMB markets. As a result, it is anticipated that more foreign investors will be willing to hold RMB assets.

As part of its 2023 internationalisation program, the Chinese authorities will look to promote Hong Kong as an offshore RMB centre through the establishment and launch of a series of comprehensive RMB-denominated financial products including “Dim Sum” bonds.

ii. Bilateral Swap Agreements

Over the last 14 years, China has signed 40 bilateral swap agreements with a value of CNY 4 trillion with other central banks which have become an important source of funding.[91] Central banks typically use these swap agreements to provide the foreign currency to domestic financial institutions when liquidity is tight.

iii. RMB inclusion in the Special Drawing Right (SDR)

On 1 October 2016, the RMB was included in the International Monetary Fund’s (IMF’s) Special Drawing Rights (SDR) basket of currencies with a weighting of 10.92%, the third largest weighting. This represented recognition on the world stage of China’s efforts to internationalise its currency and broaden onshore and offshore access to its capital markets. Despite the expectation that the RMB’s inclusion in the SDR would increase investor appetite for RMB-denominated assets and encourage a wider use of RMB in cross-border transactions, the share of the RMB in international payments has remained stagnant along with its position as a reserve currency. Further currency liberalisation in the short to medium term is unlikely given restrictions on capital outflows continues to be high.

On 11 May 2022, the IMF completed the quinquennial review of the method of valuation of the basket of currencies that make up the SDR. The RMB’s weighting was increased from 10.92% to 12.28%.[92]

According to the IMF, the share of RMB in global currency reserves was 2.69% as of Q4 2022, down from 2.87% in Q1 2022 but up from 2.5% in Q1 2021[93].

2b. Liquidity and Hedging

[91] Focus, why RMB is popular, https://www.ccdi.gov.cn/toutiaon/202304/t20230417_258946.html.

[92] SDR weight increased from 10.92% to 12.28% - new achievements in RMB internationalization, https://www.gov.cn/xinwen/2022-05/16/content_5690597.htm.

[93] Currency Composition of Official Foreign Exchange Reserve(COFER), IMF.

In a significant step to open up the domestic capital markets, in 2017, foreign institutional investors in the CIBM were allowed to have access to onshore FX risk hedging arrangements[94]. This was further relaxed on 1 February 2020, when access was extended to three FX banks rather than just an investor's onshore agent bank[95]. The lack of onshore hedging capabilities was previously an impediment for foreign investors who had to resort to more expensive offshore FX hedging solutions. Since then, the PBOC and SAFE issued the *Provisions on Administration of Funds Invested in China's Bond Markets by Foreign Institutional Investors* (《境外机构投资者投资中国债券市场资金管理规定》) in November 2022. Under these new rules, which came into effect on 1 January 2023, foreign investors are permitted to enter into FX spot transactions with their settlement agent banks, custodian banks, any other financial institution or indirectly trade in the interbank FX market via a prime broker; the intention being to offer foreign investors more options and help them to obtain better FX rates.

The onshore FX market was further opened in June 2018 when investors via the QFII and RQFII channels were allowed to directly hedge FX exposures without using their custodians[96]. Since then, in 2022, SAFE further lifted the restrictions by removing the cap on the number of third-party banks that can be used by investors[97].

While there have clearly been positive developments in the FX market since the deliverable CNH currency was introduced in 2010, there continue to be restrictions that limit the size of the onshore market:

- Access to the market is limited reducing the number of possible market participants and limiting the natural hedges for liquidity providers which increases the costs for end users.
- There is no CNH PVP risk mitigation infrastructure for the protection from loss of principal. This risk mitigation is important to investors and is available in developed currencies including the most liquid currencies traded with CNH.

[94] *Notice of the State Administration of Foreign Exchange on the Foreign Exchange Risk Management of Foreign Institutional Investors in the Interbank Bond Market* (《国家外汇管理局关于银行间债券市场境外机构投资者外汇风险管理有关问题的通知》) (expired).
[95] *Notice of the State Administration of Foreign Exchange on Improving the Foreign Exchange Risk Management of Foreign Institutional Investors in the Interbank Bond Market* (《国家外汇管理局关于完善银行间债券市场境外机构投资者外汇风险管理有关问题的通知》) (expired).
[96] QFII and RQFII welcome the benefits of reform again, and the finance further opens up to the world, https://www.gov.cn/xinwen/2018-06/12/content_5298189.htm.
[97] *Administrative Provisions on Funds for Securities and Futures Investments in China by Foreign Institutional Investors* (《境外机构投资者境内证券期货投资资金管理规定》).

3. Onshore Market

Figure 8: Onshore FX volumes

Source: BIS

3a. CFETS RMB Index

In December 2015, CFETS unveiled the CFETS RMB Index to be used to determine the exchange rate. This moved the focus from the USD/CNY exchange rate to the RMB's performance against a basket of currencies used by its trading partners. The original Index consisted of 13 currencies with weightings based mainly on a trade-weighted average to take into account re-exports, and included all of the world's major reserve currencies, which combined account for more than 80 percent of the basket. The USD had the largest weighting with 26.4 percent, while the weightings of the Euro and the Yen components were 21.4 percent and 14.7 percent respectively.

In December 2016, the CFETS Index was refined with 11 more currencies added to the basket, resulting in reduced weightings for the USD, the Euro and the Yen. Since then, further refinements have been made to the composition of the RMB Index; the most recent announcement by CFETS was that, with effect from 1 January 2023, the USD weighting in the RMB Index will be reduced to 19.83% from 19.88% and the EUR weighting reduced to 18.21% from 18.45%.[98]

3b. Trading Band

As part of the effort to enhance its currency regime, the PBOC has relaxed the interbank FX spot rate of USD/CNY trading band (银行间即期外汇市场人民币兑美元交易价浮动区间). In 2007 it was increased from 0.3% to 0.5%, and then again to 1% in April 2012 with the most recent increase to 2% in March 2014[99].

Widening the trading band should makes it more attractive for investors and promote its broader use for cross-border trade settlement. However, this has not always been the case given the PBOC's objective of keeping the exchange rate within a tightly controlled band; hence, the market's influence may not be fully captured.

3c. Access to the Onshore Interbank FX Market

There are currently 60 foreign central banks, 62 foreign participating banks and 22 foreign RMB clearing banks that are overseas members of the interbank FX market and as of February 2023 they accounted for only 1.66% of onshore total FX market volume.[100]

i. Market Hours

CFETS announced that with effect from 3rd January 2023 trading hours for the interbank FX market would be extended from 09:30-23:30 to 03:00 the next day for FX spot, forwards, swaps, options and cross currency swaps. For trades executed between 24:00-03:00, the trading date would be the preceding date with the value date and maturity date are all calculated based on the trading date. For spot transactions executed between 09:30 and 03:00 the following day, the CNY parity rate and trading band published at 09:15 will apply.[101]

ii. Circular 159

[98] *Announcement on Adjusting the Weights of CFETS RMB Exchange Rate Index and SDR Currency Basket RMB Exchange Rate Index Currency Basket* (《关于调整 CFETS 人民币汇率指数、SDR 货币篮子人民币汇率指数货币篮子权重的公告》).

[99] PBOC's announcement No. 5 (2014), http://www.pbc.gov.cn/zhengcehuobisi/125207/125217/125922/125945/2805761/index.html.

[100] Newsletter issued by the CFETS, February 2023, https://iftp.chinamoney.com.cn/dqs/fileDownLoad.do?mode=open&contentId=2587442&priority=0.

[101] Notice of the CFETS on Extending the Trading Time of the Interbank Foreign Exchange Market (《外汇交易中心关于延长银行间外汇市场交易时间有关事项的通知》), https://www.chinamoney.com.cn/chinese/rdgz/20221230/2526857.html#cp=rdgz.

The *Notice of the People's Bank of China on Matters Concerning Improvements to the Administration of 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》) (the "Circular 159"), issued in June 2018, represented a significant shift in policy and was a response to requests from the market to facilitate access for offshore financial institutions to the onshore USD/CNY FX market. Under the Circular 159, overseas participating banks can carry out these cross border RMB transactions on behalf of for corporate and institutional clients either via domestic correspondence banks, overseas clearing banks or directly in the onshore interbank CFETS market.

Under the Circular 159:

a. Overseas participating banks can trade in China's inter-bank FX market either indirectly via RMB clearing banks in their respective jurisdictions or their correspondent banks, or directly by applying to become members of CFETS. It is not possible to be both an indirect and a direct participant.
b. Domestic correspondent banks, overseas clearing banks and overseas participating banks can enter into FX spot, forward, swap, and option as well as cross currency swap contracts for cross border RMB settlement either for current account, direct investment, approved securities investment and other transactions for capital and finance.
c. An overseas participating bank group has to register with the PBOC Shanghai headquarters through domestic correspondent banks, overseas clearing banks or CFETS. Only one branch of an overseas participating bank group can be assigned to carry out this cross border RMB activity.
d. Overseas clearing banks and overseas participating banks which enter into transactions direct in the onshore interbank FX market are required to report them to CFETS.

Entities that are neither an overseas central bank, an overseas clearing banks nor an overseas participating banks can only trade in Chinese inter-bank foreign exchange market indirectly via an overseas participating bank.

3d. Trading

i. China FX Code (China Code)

The Global FX Code[102] (Global Code) is a set of 55 principles, universally recognised as good practice in the FX market, that have been developed to provide a common set of guidelines to promote the integrity and effective functioning of the wholesale foreign exchange market. It was developed by a partnership between central banks and Market Participants and first published in 2017.

The Global FX Committee (GFXC) was established in May 2017 as a forum bringing together central banks and private sector participants to promote collaboration and communication on trends and developments in FX markets and has responsibility to maintain and update the Global Code. The GFXC

[102] Global FX Code, https://www.globalfxc.org/docs/fx_global.pdf.

regularly assesses whether FX market developments warrant specific revisions to the Global Code and, when judged appropriate, undertakes a comprehensive review. The China FX Committee (CFXC), chaired by the PBOC, is a member of the GFXC.

The Global Code does not impose legal or regulatory obligations on market participants, nor does it substitute for regulation, but rather it is intended to serve as a supplement to any and all local laws, rules and regulations by identifying global good practices and processes.

As China's FX market is a part of the global FX market, the PBOC has developed a domestic version of the Global Code, the China Code[103], which is more detailed and complementary based on the development stage and prevailing practices in the domestic FX market. From the outset, the China Code is designed to be highly consistent with the Global Code[104].

A comparison of the two codes shows that the China Code is "not contradictory" compared with the Global Code with the global principles incorporated in the China Code. Therefore, the Global Code and the China Code are two parts that form a whole, and the code of conduct to be promoted in China's FX market is a system that consists of the two.

The CFXC is sponsored by the PBOC and SAFE. Its mandate is to provide guidance on reform and development thereby promoting a healthy and orderly FX market[105]. Membership is drawn from the PBOC and SAFE, primary market participants and infrastructure providers[106].

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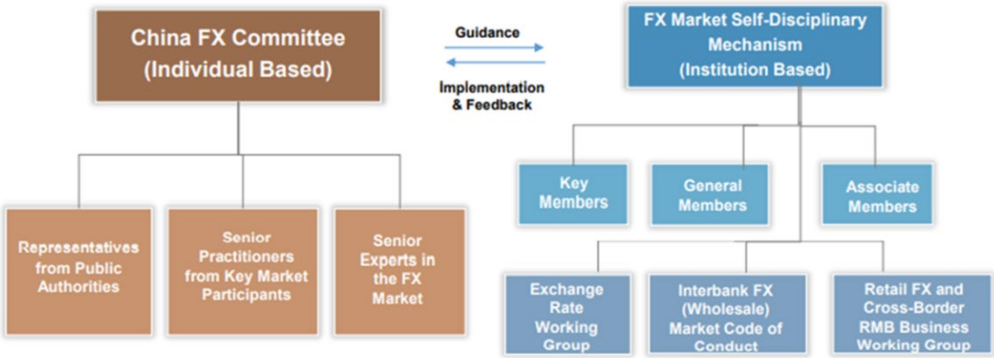
[103] Guidelines on Code of Conduct for the Foreign Exchange Market, https://www.safe.gov.cn/en/file/file/20211231/240c3891ff7744cd9cba0749541afe27.pdf?n=Guidelines%20on%20Code%20of%20Conduct%20for%20the%20Foreign%20Exchange%20Market.

[104] China's FX Code released, promoting the standardized development of the FX market, https://www.chinamoney.com.cn/chinese/jzdt/20170509/1004519.html#cp=jzdt.

[105] Basic information of the self-regulatory system of FX market, https://www.chinamoney.com.cn/chinese/jzdt/20160801/1003990.html#cp=jzdt.

[106] Member list of the self-regulatory system of FX market, https://www.chinamoney.com.cn/chinese/jzdt/20210607/1978810.html#cp=jzdt.

Figure 9: China FX Market/Regime



Source: CFETS

As a member of the GFXC, the CFXC has committed to "promoting adherence of institutions in its jurisdiction to the principles in the Global Code when conducting FX activities, and promoting implementation of the principles across the FX industry". There are 57 market participants on the domestic Register of the Statement of Commitment[107].

The China FX Market Self-Regulatory Framework was created in June 2016 by members of China's FX and relevant markets[108]. It serves as a self-regulatory and coordinating mechanism to safeguard fair competition and support the sound development of the FX market. It is responsible for the self-regulatory management of the USD/CNY central parity rate quoting, wholesale interbank FX trading and retail FX and cross-border RMB businesses, so as to safeguard fair competition and support the sound development of the FX market.

ii. Cost of Trading

At present, the onshore markets, with the exception of the spot and FX swaps which are highly liquid, are inefficient and costly, making them less attractive to those market participants permitted to trade in them.

The opening up of the option market in 2015 did not result in the expected increase in activity hence the FX derivative market remains disproportionately small relative to the size of the economy and compared to other emerging and developed market economies.

A contributing factor to the slow growth is the restriction of access to the FX market. In the offshore market, there are numerous non-bank participants that trade both sides of the market, thereby

[107] List of Market Participants, https://www.chinamoney.com.cn/english/cfxcpr/.
[108] Overview of the China FX Market Self-Regulatory Framework, https://www.chinamoney.com.cn/english/cfxovv/.

enabling banks to avoid the costs associated with risk warehousing. In the onshore market, where hedging tends to be directional, non-bank participants do not have access to the market. The resulting build-up of risk by the banks incurs costs that need to be recovered through wider spreads which dampens the demand from end users.

The PBOC reinstated the risk reserve ratio for forward foreign exchange sales (远期售汇业务的外汇风险准备金率) from zero to 20%, effective from 28 September 2022.[109] This requires banks to place a USD-denominated deposit at the Central Bank at 0% interest for one year. The size of the deposit is calculated as 20% of the notional value of all new FX forward and swap contracts where their client is long USD/short RMB. This deposit has to be funded by the banks resulting in the costs being passed through to end-users via wider spreads. This additional cost potentially disincentivises end-users from hedging the FX exposures which is a significant risk when USD/RMB volatility is high.

Under the *Circular of the State Administration of FX on Printing and Distributing the Rules for the Implementation of the Measures for the Administration of FX Settlement and Sale by Banks* (《国家外汇管理局关于印发<银行办理结售汇业务管理办法实施细则>的通知》), the foreign currency profits can only be sold off based on a quota and only at the end of each quarter. This quota is based on the banks' financial accounting results at the end of each quarter. In addition, at yearend, this sell-off needs to be consistent with the banks' annual audit report. These foreign currency profits can only be sold off after offsetting the loss, if any, in previous years. The quota requirement acts as a constraint and prevents banks from freely off-loading their FX risk at any time and as needed.

Recommendations:

Consideration should be given to removing the quota requirement on FX profit sell-off as this currently prevents banks from actively managing their foreign exchange risk.

Given RMB-FX rate has become more stable and moving along with broad USD movement, we would suggest the removal of the 20% risk reserve ratio for forward foreign exchange sales. The additional costs incurred by liquidity providers in maintaining the deposits is reflected in the prices quoted to clients and can potentially disincentivise end-users from hedging their currency exposure which is a significant risk during periods of high USD/CNY volatility.

iii. Electronic Execution

Banks and customers prefer electronic execution due to the greater price transparency, improved execution efficiencies and cost savings that it brings through higher straight-through processing and much reduced error rates. It now accounts for in excess of 55% of global volume across all products, and over 65% of spot trades which has significantly improved the efficiency of the market, driven down

[109] The PBOC has decided to adjust the risk reserve ratio for forward foreign exchange sales to 20%, http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/4666334/index.html.

bid-ask spreads and increased market turnover. In addition, it facilitates Transaction Cost Analysis which, in turn, incentivises greater efficiency and a reduction in execution costs.

These enhanced services have become available as a result of technology providing liquidity providers with real-time access to bank liquidity and pricing data via application programming interfaces (APIs). This has also enabled banks to automate risk management and eliminate manual hedging, while strengthening their control environments through improved monitoring and surveillance capabilities.

CFETS was set up in 1994 to develop infrastructure and providing innovative channels for the FX interbank market. Its strategic goal is to become “a major global trading platform and pricing centre for RMB and related products.”[110]

Following the launch of the CFETS FX2017 platform in February 2018, which leverages the underlying technology behind NEX Markets’ electronic broking service (EBS) platforms, CFETS members have the ability to either electronically execute spot via the central limit order book, known as C-trade, on an anonymous basis by accessing a central pool of liquidity, or to execute spot, forwards and swaps through a disclosed, bilateral trading model where price takers can choose from a full range of bank and non-bank liquidity providers. Currently, options are only traded on a bilateral inquiry basis.

For FX products tradable via CFETS, the trading patterns include the quote driven model (QDM), order driven model (ODM) and negotiate driven model (协商驱动), and the trading modes include anonymous trading, bilateral trading and matching trading (C-Trade).[111] As part of the CFETS FX2017 implementation, bilateral Executive Streaming Price (BIL ESP, 询价点击成交) trading with one-click function was launched for the quote-driven market trading mode. This enables liquidity providers to provide executable/laddered quotes while liquidity consumers can execute transactions by one-click function or submitting orders.

CFETS adjusts its offering in response to market demand and recently introduced an ODM which has grown in prominence and is now roughly similar in size to the QDM. However, unlike the QDM there is no API access offered under the ODM.

CFETS also offers services covering issuance, trading, information and post-trade activities for the RMB-denominated interest rate, the RMB exchange rate and related products in the cash and derivatives markets. It publishes daily market benchmarks including the RMB central parity rate, the Shanghai interbank offered rate (Shibor), the loan prime rate (LPR), the CFETS RMB index series, the fixing repo rate, bond indices, yield curves, etc.

Recommendation:

[110] Introduction to the CFETS, https://www.chinamoney.com.cn/chinese/acfact/.
[111] *CFETS’ Product Guidelines* (《中国外汇交易中心产品指引》).

Extend API connectivity to all CFETS trading modes and protocols. We understand that there is a CFETS API available for ODM but this has not yet been made available. API access:

a. Provides greater transparency and the ability to continually monitor market prices prior to execution,

b. Provides improved straight-through-processing rates available from a single automated point of entry through to settlement,

c. Enables end-users, through order management systems, to access multiple pools of liquidity and to execute orders cost effectively and efficiently regardless of ticket size, and

d. Increases the understanding of the costs of execution provided by transaction cost analysis which, in turn, incentivises greater efficiency and a reduction in execution costs.

3e. New Product Development

In June 2022, CFETS offered new FX options products including vanilla American options and Asian options in the interbank RMB/FX market, as well as vanilla American options, Asian options, European barrier options and European digital options in the interbank G10 currency pairs market.[112]

We fully support the growth in the availability of new products to enable market participants to hedge their foreign currency exposures.

Despite the recent product development, there are further opportunities to bring new products to the market that offer market participants with a cost-effective means to hedge their currency exposure; USD/CNY barrier options is one such opportunity.

3f. Others

i. Validation of Underlying Real-Economy Trade

For onshore FX trading to occur it is necessary for a bank facilitating the trade to be able to evidence that there is a "purpose of payment" for the FX trade, i.e., that there is some underlying economic reason for the FX trade such as obtaining the requisite currency for the import/export of goods or the purchase of a stock or bond. A bank will need to establish a sufficient audit trail in this regard for each FX trade implicated by these requirements.

[112] Notice on Adding New Option Varieties in the Interbank Foreign Exchange Market (《关于银行间外汇市场新增期权品种的通知》), https://www.chinamoney.com.cn/chinese/rdgz/20220526/2380657.html#cp=rdgz.

The implementation of the appropriate validation controls is often manual, required at the point of execution and create inefficiencies in the filling client orders.

Recommendation:

For client-facing trades, consideration should be given to reducing the documentation checking ratio. As an example, only if a certain proportion of client trades and certain percentage of client transaction notional did not fulfill the documentation checking requirement would they be considered in violation of the requirements. This could improve efficiency by moving the document checking to become a post trade activity and increase the usage of electronic execution by clients thereby increasing the efficiency of their transaction execution.

ii. Third-party FX Execution for QFIs and QDLPs

We are encouraged to see that PBOC and SAFE jointly promulgated the *Administrative Provisions on Funds for Securities and Futures Investments in China by Foreign Institutional Investors* (《境外机构投资者境内证券期货投资资金管理规定》) which lifted quota requirements and simplified the administrative requirements for the remittance and repatriation of funds as well as currency exchange by QFI investors. Currently QFIs who remit foreign currency to fund their investment are required to execute their FX requirements with the QFI custodian only. With more flexibility, foreign investors would be able to execute with any onshore counterparties with the capability to trade FX. Increasing the number of FX counterparties enables best execution which is a requirement for foreign investors. Remittance and repatriation continue to go through the onshore accounts maintained by the QFI custodian so the QFI custodian can continue the monitoring.

Currently QDLPs who repatriate foreign currency to fund their investment are also not allowed to execute FX with a third-party. From a market perspective, QDLP clients has increasing demand for FX execution via a third-party for the purpose of remittance and repatriation as well as hedging. In order to facilitate improved price discovery and open market competition, we would request that foreign investors are able to execute transactions with any onshore counterparty with the capability to trade FX. This similar restriction was relaxed for CIBM investors and as a result they can execute FX (for settlement) with any onshore counterparty.

iii. Loosening CBIRC Ratio Requirements

We recommend that CBIRC loosen certain ratio requirement which constrained banks' capacity to serve offshore investors. For example, under the *Administrative Measures on Liquidity Risk of Commercial Banks* (《商业银行流动性风险管理办法》), where the RMB and foreign currency assets in China of a wholly foreign-funded bank or a joint venture bank are less than its RMB and foreign currency liabilities in China, or the ratio of net outflow of cross-border funds within the group exceeds 25%, or the ratio of net outflow of cross-border funds of a branch of a foreign bank exceeds 50%, a report shall be submitted to the CBIRC within two working days. Such ratio requirement limits bank's capacity to take deposit from clients for settlement.

Recommendations for Foreign Exchange
1. Consideration should be given to removing the quota requirement on FX profit sell-off as this currently prevents banks from actively managing their foreign exchange risk. 2. Given RMB-FX rate has become more stable and moving along with broad USD movement, we would suggest the removal of the 20% risk reserve ratio for forward foreign exchange sales. The additional costs incurred by liquidity providers in maintaining the deposits is reflect in the prices quoted to clients and can potentially disincentivise end-users from hedging their currency exposure which is a significant risk during periods of high USD/CNY volatility. 3. Extend API connectivity to all CFETS trading modes and protocols to the industry. We understand that there is a CFETS API available for ODM but this has not yet been made available to the industry. Extending API access will: a. Provides greater transparency and the ability to continually monitor market prices prior to execution, b. Provides improved straight-through-processing rates available from a single automated point of entry through to settlement, c. Enables end-users, through order management systems, to access multiple pools of liquidity and to execute orders cost effectively and efficiently regardless of ticket size, and d. Increases the understanding of the costs of execution provided by Transaction Cost Analysis which, in turn, incentivises greater efficiency and a reduction in execution costs. 4. Further simplify the document checking requirement for client-facing trades. By introducing a tolerance to a proportion of client trades and a certain percentage of client transaction notional that do not fulfill the documentation checking requirement, it is likely that it would result in an increase the usage of electronic execution by clients thereby increasing the efficiency of their transaction execution. 5. Continue to bring new products to the market that offer end-users with a cost-effective means to hedge their currency exposure, e.g., barrier CNYFCY options. 6. Increase coordination among regulators and loosen certain ratio requirements which constrain the capacity of banks to serve offshore investors, e.g., the "Inter Company Net Funding Outflow Ratio" which limits a bank's capacity to take deposits from clients for settlement.

F. Onshore Operations

1. Onshore Operations of Foreign Firms

The *Measures for Further Opening Up the Financial Sector* （《关于进一步扩大金融业对外开放的有关举措》） issued by the Office of Financial Stability and Development Committee under the State Council in July 2019 laid the foundation to further promote inbound investments in the onshore financial sector. Since then, with various foreign ownership limits being lifted, many foreign financial institutions have established wholly foreign-owned or assumed majority or 100% ownership of their joint ventures in China. The table below sets out these relaxations over around the past three years.

Table 5: Relaxations of Foreign Investments in Onshore Financial Sector

Securities Companies	***As of 1 April 2020*** Removed foreign ownership cap
Fund Management Companies	***As of 1 April 2020*** Removed foreign ownership cap
Futures Companies	***As of 1 January 2020*** Removed foreign ownership cap
QFII/RQFII	***As of 11 November 2020*** Expanded investment scope to include, commodities and options
Private Fund Managers	***As of 22 September 2020*** 30 foreign PFM WFOEs
Insurance Companies	***As of 1 January 2020*** Removed foreign ownership cap on life insurance companies/expanded business scope of insurance brokers
AMCs	***As of 23 March 2020*** Clarified the conditions and thresholds for foreign capital to set up AMCs
Bank Wealth Management	***As of 20 July 2019*** Majority foreign ownership permitted
QDLP/QDIE/QFLP	***As of 2020*** New quota available

We witnessed increased willingness and efforts among regulators, industry and investors to participate in asset management through outbound and inbound capital flows. The industry is keen to meet the growing demand for diversified product offerings, and bring in global expertise and best in class solutions that are aligned with the country's strategic thinking of promoting high-quality development. In particular, we have seen the establishment of a number of public fund management companies (FMCs), in which the limit on foreign ownership was completely removed on 1 April 2020. As of early June 2023, there existed around eight wholly foreign-owned public fund management companies (FMC WFOEs), thirty-one wholly foreign-owned private securities investment fund managers (PFM WFOEs), and five majority foreign-owned bank wealth management subsidiaries (of subsidiaries) (BWMSs).[113]

1a. FMC – Information and Research Sharing with Offshore Parent

[113] Please refer to Annex 4 for the list of the FMC WFOEs, PFM WFOEs and BWMSs.

- **Information Sharing**

As the eight global asset managers start operating their FMC WFOE, they would ideally like to integrate their Mainland subsidiary into their global operating model. However, Article 19 of CSRC's *Guidelines for the Governance of Securities Investment Fund Management Companies (For Trial Implementation)* (《证券投资基金管理公司治理准则（试行）》) issued in June 2006 provides that the shareholder of a fund management company shall not, directly or indirectly, request the company to provide non-public information or materials on fund investment and research. And as recently as May 2022, Article 33 of the CSRC's *Measures for the Supervision and Administration of Publicly-Offered Securities Investment Fund Managers* (《公开募集证券投资基金管理人监督管理办法》) requires FMCs to establish policies on segregating "key information" of its business and clients from that of its shareholders.

Even though we believe the intention of these requirements is to prevent mainly the leakage of non-public information of an FMC, for fear of front running by its shareholder for example, to the detriment of retail investors, these requirements negatively affect Chinese investors as well as global firms because:

- Such information, when used by the parent or group company for group supervision, compliance, internal controls and risk management purposes, will provide an additional layer of protection to retail investors of the FMC;

- The sharing of information, such as research, within a global asset management firm is fundamental to the way global asset managers operate and there would be little distinction or additional benefit to Chinese investors if an FMC WFOE operates like any other purely domestic asset management company without being able to share and leverage off the group's global practices, information, experience and expertise.

As with most other jurisdictions, the concern over the mis-use of non-public information (whether of the FMC, or the group to which the FMC belongs) and other market abuse can be addressed with the appropriate safeguards and controls which the shareholder can help ensure by closely monitoring the activities of the FMC subsidiary.

These requirements also unreasonably restrict shareholder access to information that a shareholder is reasonably entitled to have in most jurisdictions. This is especially true for global financial institutions which are heavily regulated around the world, and for which the parent of the group is often held liable for the actions or misbehaviours of its wholly or majority owned subsidiaries. Having access to information from their FMC subsidiary is important as part of such institutions' global compliance, monitoring, surveillance and risk management processes. Without access to such information, global financial institutions or asset managers may be in breach of the laws and regulations of their home jurisdiction.

- **Research Sharing**

For global asset managers that set up an FMC in the Mainland, they not only want to be able to provide Mainland investors with a good selection of mutual fund products onshore by sharing investment views across the group, they also want to be able to leverage off the talent and resources that the onshore FMC has developed to provide investors outside the Mainland with reliable research and advice on the Chinese market, Chinese listed companies as well as onshore fund products which would bring more foreign investment into China.

In fact, many global asset managers with an FMC in the Mainland would like to have the portfolio managers at the FMC manage or advise their offshore funds that invest into the China market. This is currently not possible because FMCs are not allowed to manage or advise on the investments of foreign portfolios or funds. As mentioned above, we understand that FMCs may not share their research and other "key information" with its shareholder.

Sharing research internally within the group does not automatically mean or result in foreign intervention on FMCs' investment decision making, as FMCs are still independently operated onshore. Bringing investment management/advisory capabilities of a global asset management company onshore into China will help (1) develop China's domestic asset management talent; (2) transfer onshore to China more research activities and investment decision making, especially for offshore funds and portfolios with China exposure; (3) global investors to better understand the value of Chinese companies and the Chinese market; and (4) build China as a regional/international asset management hub.

Recommendations:

If China is to benefit from having foreign asset managers enter its market, the current CSRC restrictions on the sharing of information between an FMC and its foreign shareholder must be lifted or relaxed.

In addition to allowing the sharing of research and other information of an FMC for legitimate purposes and with appropriate safeguards, we recommend that FMCs be allowed to manage, trade for and/or advise on the investments of foreign portfolios or funds that invest in the China market, as this will not only bring onshore to China investment decision making for such foreign portfolios and funds, but will quickly develop China's domestic asset management talent and help China become a regional/international asset management hub.

Assuming FMCs will be allowed to manage, trade for and/or advise on foreign portfolios or funds, we would also need clarity from the Mainland tax authorities that such activities onshore will not create a taxable presence of such foreign portfolios or funds in China, which is currently unclear. We understand that under current Chinese tax law, having a portfolio manager based in China manage or partly manage, trade for or advise on these international strategies may expose offshore funds/portfolios to incremental China tax that would not be the case if those portfolios are managed by an offshore portfolio manager. Thus, it would be helpful for the tax authorities to clarify that offshore funds or portfolios would not, by virtue of their using such services from FMCs, be subject to more onerous China tax (including VAT on income or gain generated from the portfolio management, advice or trading provided by FMCs) or be considered as a tax resident or non-resident with an establishment or place of business in China. This would provide tax clarity for the foreign asset managers in setting up or expanding operations in China, utilizing onshore resources, and creating career opportunities for their onshore staff. We wish to stress that the foregoing would not affect foreign investment funds and institutional client accounts from continuing to pay any China tax due on their China sourced income and capital gains (generally on a withholding basis) and capital gains as non-residents without an establishment or place of business in China.

1b. PFM

When PFM WFOEs were first introduced in 2017, they were only allowed to raise monies from domestic eligible investors for their private funds which are supposed to invest in the domestic capital markets.

At ASIFMA's suggestion for a level playing field, PFM WFOEs were allowed to invest in the Southbound Stock Connect in August 2019 like the domestic PFMs[114]. Again, at the urging of ASIFMA, the New QFI Regulations issued in September 2020 allowed QFIs to appoint its affiliated PFM WFOE as its investment adviser[115] (and also invest in private investment funds whose investments falls within the QFI investment scope, i.e., essentially funds issued by PFMs), which provided a new and convenient way for PFM WFOEs to seed or kick off the fundraising for their private securities investment fund. ASIFMA's asset manager members are especially appreciative of these accommodations.

As PFM WFOEs tend to be smaller entities with a minimum staff requirement of five[116] as opposed to 30 for FMCs[117], many tend to rely on the resources of their parent or group. We hope that they will be able to continue to do so.

Recommendations:

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[114] Announcement of the AMAC, https://www.amac.org.cn/aboutassociation/gyxh_xhdt/xhdt_xhgg/201908/t20190809_2480.html.
Detailed Contents of Nine Opening-up Measures Released by the CSRC, https://www.gov.cn/xinwen/2019-06/15/content_5400452.htm.

[115] Article 6 (5) of the *Provisions on 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和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》).

[116] Article 8(4) of the *Measures for the Registration and Filing of Private Investment Funds* (《私募投资基金登记备案办法》) provides: … the full-time employees may not be less than 5.

[117] In accordance with Article 6 of the *Measures for Supervision and Administration of Public Securities Investment Fund Managers* (《公开募集证券投资基金管理人监督管理办法》), which took effect since June 20, 2022, a mutual fund management company shall, in principle, have no less than 30 employees with fund practicing qualification.

Similar to the recommendation for FMCs, we recommend that PFM WFOEs be allowed to manage, trade for and/or advise on the investments of foreign portfolios or funds investing in the China market, in addition to providing investment advice to their affiliated QFIs, and provide tax clarity that such services by them will not create a taxable presence in China for such foreign portfolios or funds.

1c. Broker Rating

The current rating system has a reward-penalty structure that seems to be asymmetrical. It favors brokers that have a large business size, which is a significant point-adding factor[118]. By contrast, certain aspects such as risk management mechanisms are only minor penalty factors in the rating[119]. This means a broker found to have issues with risk management mechanisms will only have a few points deducted, which is unlikely to affect its broker rating. Currently, if the broker has a large client base (which is mostly likely the case for a domestic broker), that broker can easily get the few deducted points back for executing orders in large quantity.

Apart from rewarding quantity than quality, in addition, the current system awards diversification for big players. More business lines can add more points. There are also 2 items, namely income of the prior year and net profit of the prior year, simply reinforcing more business line more points.[120]

Since WFOE or foreign-controlled brokers ("foreign brokers") are late entrants, their client base is not nearly as large as their domestic counterparts. Solely with strengths in risk management or other similar aspects but without a large client base, foreign brokers may encounter bottlenecks at some point when climbing up the broker rating ladder under the current reward and penalty structure.

Recommendation:

We recommend that CSRC revise the broker rating system to bring more symmetry between the reward and penalty structure as well as a more level playing field between domestic brokers and foreign brokers onshore. For example, a broker found to have issues with risk management mechanisms should be penalized more heavily than now.

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118 Article 13 of the *Provisions on the Supervision and Administration of the Classification of Securities Companies (证券公司分类监管规定)* provides that companies whose operating revenue and single business revenue rank top in the last year will be respectively awarded additional points in the range of 0.5 to 2 points when determining the classification.

119 Article 12 of the *Provisions on the Supervision and Administration of the Classification of Securities Companies (证券公司分类监管规定)* provides that the deficiencies in the comprehensive risk management will lead to a deduction of 0.5 point per specific item.

120 Article 13 of the *Provisions on the Supervision and Administration of the Classification of Securities Companies (证券公司分类监管规定)* provides that companies whose operating revenue and single business revenue rank top in the last year will be respectively awarded additional points in the range of 0.5 to 2 points when determining the classification.

We further recommend that CSRC put a cap on the number of business lines that can count towards bonus and simply put a factor for diversification of revenue or risk.

1d. Derivatives License

In accordance with the consultation paper of the *Administrative Measures for Supervision of Derivatives Trading* (《衍生品交易监督管理办法(征求意见稿)》), derivatives dealership is subject to CSRC approval. Under Article 27 thereunder, the criteria for CSRC to review applications include, among others, registered capital and net capital. We are worried if registered capital and net capital would be a determining factor for CSRC's review of applications, and believe factors such as risk management capacities shall be given due importance.

In addition, the existing Tier 1 derivatives license approval process is not transparent in terms of criteria or approval time.[121] For example, it is unclear whether the notional scale will be a major factor. Clarifying the approval process can attract foreign brokers which help to enhance the development of the market and liquidity within the market.

***Recommendation**:*

We recommend not attaching excessive importance to registered capital and net capital when reviewing derivatives license applications. We further recommend clarifying the existing Tier 1 approval process.

1e. Investor Suitability Assessment

We understand that the Chinese context is unique in terms of joint liability requirements for asset managers and distributors to ensure investor suitability, even when, in most cases in a third-party distribution context, asset managers do not have visibility into the end clients and have to rely on the distributors to conduct investor suitability assessments. This is a notable deviation from most (if not all) other jurisdictions, where liability resides with distributors (being the party who onboard the end clients and "own" that relationship). Whilst asset managers may seek to mitigate the risk of liability by requiring distributors to provide investor information upon request, such requests are commonly rejected by distributors who view such information to be proprietary and to be maintained as a trade secret. Given that investor protection is not enhanced by imposing joint liability (indeed, distributors would typically be regulated entities subject to local regulatory oversight) and impracticality of asset managers verifying such information, we recommend regulators to further consider re-aligning the liability standard to better reflect the practical and commercial reality, and better align with global practices.

[121] Article 7(1) of the *Measures for the Administration of Over-the-counter Option Business of Securities Companies* (《证券公司场外期权业务管理办法》) provides "Those with a classification rating of Grade AA in the Class A or above in the past year, upon recognition of the CSRC can become Tier 1 derivatives traders."

In addition, the client suitability framework in China is focused on a singular product risk rank approach. As the product landscape evolves in China, and clients' sophistication and demand increases, the suitability framework should evolve towards a holistic / portfolio suitability approach, rather than a product-based approach.

Recommendation:

As practically and commercially asset managers may rely on distributors to conduct investor suitability assessments, the liability shall also reside with distributors rather than asset managers.

Shift the client suitability framework from a product-based approach to a holistic, portfolio-based approach.

1f. China Pension

We are excited about the pension market opportunity ahead, especially with a focus on pillar three pensions. Building on existing partnerships and acting as outsourced overseas managers for the National Social Security Fund, ASIFMA members have accumulated China pension knowledge and experience in pillar one. Echoing the nationwide strategic initiative to promote pillar three pensions for individual investors, the asset manager members of ASIFMA are looking forward to being able to share their expertise and experience from managing overseas pension schemes and products, such as Asset Liability Match (ALM) and Liability Driven Investment (LDI) mechanisms. We recommend only that the criteria for being allowed to participate in the different pilot pillar three schemes be more transparent and that the pilots can become permanent schemes sooner than later.

1g. Custodian Settlement Qualification

We welcomed CSRC's reforms in the *Administrative Measures on Securities Investment Funds Custody Businesses* (《证券投资基金托管业务管理办法（2020）》) in July 2020 which allow foreign bank branches to conduct custody business to look through to the parent company's capital capability in order to fulfill applicable net asset requirements.

However, pursuant to the *CSDC Settlement Participants Management Work Guideline (2017)* (《中国证券登记结算有限责任公司结算参与人管理工作指引（2017 年修订版）》), to apply for the QFI custodian settlement qualification, a commercial bank shall submit documents including an undertaking letter on, among others, having a paid-in capital of at least RMB 8 billion[122]. We encourage CSDC to consider the same practice to allow foreign bank branches to conduct QFI settlement business by leveraging parent company's capital capabilities.

Recommendation:

[122] Pages 12 and 43, *CSDC Settlement Participants Management Work Guideline* (2017).

Allow foreign bank branches to conduct QFI settlement business by leveraging parent company's capital capabilities.

1h. Third-Party Connection

The so-called third-party connection or external connection was restricted in 2015 when the CSRC issued the *Notice on Strengthening the External Interface with Information System by Securities Companies* (《关于加强证券公司信息系统外部接入管理的通知》) and the *Opinions on Clearing up and Rectifying Illegal Securities Business Activities* (《关于清理整顿违法从事证券业务活动的意见》). In 2019, the CSRC issued a consultation draft of the *Interim Administrative Provisions on External Connection with Trading Information Systems of Securities Companies* (《证券公司交易信息系统外部接入管理暂行规定》) (the "API Consultation Draft"), which was intended to standardize the API provided by brokers and seems to signal CSRC's intention to permit institutional investors to get access to brokers' trading system and route orders to the Exchanges via the brokers' API.

However, the API Consultation Draft still has not been promulgated. Just as stated in the explanatory note of the API Consultation Draft, with the development of the securities market, the trading proportion of institutional investors, such as fund managers and insurance companies, is increasing year by year, and the traditional manual operation cannot meet the needs of institutional investors for separate position management and unified risk control, and the API Consultation Draft can guides securities companies to provide external interface services to institutional investors on the premise of safety and compliance. As such, the industry welcomes its promulgation soon.

Further, the industry has concerns around the broker criteria under the API Consultation Draft. Particularly, the API Consultation Draft requires that securities brokers seeking to offer third party connection must have received an A-class rating or higher for at least two years within the past three years. Such grade rating requirements may be a substantial challenge for foreign-invested securities companies seeking to provide third-party connection for their investors.

Recommendation:

We look forward to the promulgation of the API Consultation Draft, and also recommend removing the drafted prerequisite that a broker must be rated grade A or higher for the past two out of three years.

2. Dual-Licensing Regime

Overview of the Mutual Qualification Recognition Arrangement within the GBA

To enhance market integration within the GBA, in December 2003, the SFC and the CSRC signed the *Mainland and Hong Kong Closer Economic Partnership Arrangement - Arrangements relating to Qualifications of Securities and Futures Industry Practitioners* (《内地与香港关于建立更紧密经贸关系的安排--与证券及期货人员资格有关的安排》) pursuant to which they agreed on certain arrangements relating to the mutual recognition of the qualifications of securities and futures industry practitioners ("Mutual Qualification Recognition Arrangement").

Under the Mutual Qualification Recognition Arrangement:

(i) Hong Kong permanent residents holding (or having held within the past three years) relevant licences issued by the SFC ("Hong Kong Licensed Individuals") applying to obtain securities industry qualifications in the Mainland may, by passing the Mainland examination, be granted industry qualifications by the Mainland regulators. A waiver from this examination requirement will only be granted to an applicant intending to act as senior management personnel of a Mainland intermediary in special circumstances and on a case-by-case basis. Once a Hong Kong Licensed Individual has obtained such industry qualifications, if the Hong Kong Licensed Individual is licensed as a representative in Hong Kong, such licence status will be equivalent to having obtained the general industry qualifications in the Mainland.

(ii) PRC nationals possessing valid and relevant practising qualifications in the Mainland ("Mainland Licensed Individuals") are deemed to have attained the industry qualifications to act as a licensed representative in Hong Kong. Mainland Licensed Individuals who possess the senior management personnel qualification in the Mainland are deemed to satisfy the industry qualifications to act as a responsible officer in Hong Kong.

After obtaining the industry qualification, the relevant professional is required to file an application in accordance with the respective procedures in the Mainland or Hong Kong for the practising qualification or licence.

Key challenge faced by the industry

1. **Individuals**. Hong Kong Licensed Individuals and Mainland Licensed Individuals are still required to undergo onerous processes to conduct licensed activities in the other jurisdiction. For example, Hong Kong Licensed Individuals are required to pass examinations on Mainland laws and regulations and apply for practising qualification in the Mainland, and Mainland Licensed Individuals are required to pass examinations on Hong Kong regulations.

   Where a Hong Kong Licensed Individual has not obtained the relevant qualifications in the Mainland, the individual is not permitted to engage in any activity in the Mainland that constitutes a regulated activity (including, for example, promoting wealth management products under the Southbound WMC Scheme to eligible Mainland investors).

2. **Entities**. At the level of entities, as a general rule under PRC law, offshore licensed entities (and their employees) may only engage in limited activities in the Mainland without triggering the relevant licensing requirements. That is, it is generally understood by the market that the activity must:

    (i) be for educational/brand promotion purposes only; and

    (ii) not be conducted with a view to generate any revenue or profit.

    In essence, offshore licensed entities (and their employees) are not permitted to market or sell specific offshore services or products in the Mainland, or even accept offers from clients for any offshore product or service in the Mainland, without triggering the relevant licensing requirements. Such restrictions limit investors' knowledge regarding products available, for example, under the WMC Scheme, thereby hindering the attractiveness and success of the WMC Scheme significantly (see Part 2 (Wealth Management Connect) of Section G (Other Connects) of this Paper for further discussions in this respect).

Opportunities that may be brought about by a dual-licensing regime

The introduction of a dual-licensing regime, allowing individuals and entities licensed in one jurisdiction within the GBA to engage in activities within a defined scope in another jurisdiction without having to obtain a separate license in that jurisdiction, would greatly enhance the cross-border human capital flow across the GBA and facilitate the integration of the financial markets across the GBA.

As highlighted in Part 2 (Wealth Management Connect) of Section G (Other Connects) to this Paper, one of the key challenges of implementing the WMC Scheme is the prohibition on cross-border marketing activities between Hong Kong and the Mainland, which restricts banks participating in the WMC Scheme to promote their wealth management products directly to potential investors under the WMC Scheme. The introduction of a dual-licensing regime would enhance the implementation and operation of the WMC Scheme by allowing participating banks to actively promote their wealth management products distributed under the WMC Scheme.

Recommendation:

ASIFMA recommends introducing a dual-licensing regime, allowing individuals and entities licensed in one jurisdiction within the GBA to engage in activities within a defined scope in another jurisdiction without having to obtain a separate license in that jurisdiction. The mutual recognition of professional qualifications and licensing status of persons within the GBA is crucial to the integration of the financial markets across the area. While implementation of a dual-licensing regime would need to be coupled with measures to ensure that expectations on any mutually recognised licensed entities are met and that the experience and capability of any mutually recognised professionals are adequate, such development will prove to be valuable to the growing connectivity between financial markets across the GBA, particularly the implementation and operation of the WMC Scheme.

Recommendations for Onshore Operations
In respect of **Onshore Operations of Foreign Firms**: 1. **(FMC)** - lift or relax restrictions on the sharing of research and other information between an FMC and its foreign shareholder. - allow FMCs to manage, trade for and/or advise on the investments of foreign portfolios or funds that invest in the mainland market (in which case, provide clarification that such activity onshore will not subject such foreign portfolios or funds to taxes in China as this is currently unclear). 2. **(PFM)** allow PFMs to manage, trade for and/or advise on the investments of foreign portfolios or funds (besides their affiliated QFIs) investing in the China market, and provide tax clarity that they will not create a taxable presence of such foreign portfolios or funds in China. 3. **(Broker Rating)** revise the broker rating system to bring more symmetry between the reward and penalty structure. 4. **(Derivatives License)** attach less importance to registered capital and net capital, and clarify the existing Tier 1 approval process. 5. **(Investor Suitability Assessment)** re-align the liability standard to better reflect the practical and commercial reality that asset managers may rely on distributors to conduct investor suitability assessments, and shift the client suitability framework from a product-based approach to a holistic, portfolio-based approach. 6. **(Custodian Settlement Qualification)** allow foreign bank branches to conduct QFI settlement business by leveraging parent company's capital capabilities. 7. **(Third-Party Connection)** remove the prerequisite that a broker must be rated grade A or higher for the past two out of three years in the draft *Interim Administrative Provisions on External Connection with Trading Information Systems of Securities Companies*. In respect of **Dual Licensing**: 8. Introduce a dual-licensing regime, allowing individuals and entities licensed in one jurisdiction within the GBA to engage in activities within a defined scope in another jurisdiction without having to obtain a separate license in that jurisdiction, would greatly enhance the cross-border human capital flow across the GBA and facilitate the integration of the financial markets across the GBA.

G. Other Connects

1. Mutual Recognition of Funds (MRF)

The MRF scheme was launched in May 2015 to enable eligible Mainland and Hong Kong retail funds to be registered and distributed within the other market. As of the end of 2022, there are 38 northbound funds from Hong Kong that have been approved for distribution in the Chinese mainland and 47 southbound funds from the Chinese mainland that have been approved for distribution within Hong Kong. However, there have not been any new funds approved for northbound since April 2021, while the last southbound fund was approved in 2017.[123]

Table 6: MRF - Funds Approved and Net Capital Flows[124]

	Northbound		Southbound	
	HK funds approved	**Total net capital outflow (as of end of the year)**	**Mainland funds approved**	**Total net capital inflow (as of end of the year)**
2015	3	N.A.	13	N.A.
2016	3	RMB 7.77 billion	33	RMB 0.10 billion
2017	4	RMB 12.46 billion	1	RMB 0.34 billion
2018	7	RMB 9.02 billion	0	RMB 0.43 billion
2019	6	RMB 16.18 billion	0	RMB 0.27 billion
2020	6	RMB 14.42 billion	0	RMB 0.31 billion
2021	9	RMB 14.24 billion	0	RMB 1.03 billion
2022	0	RMB 11.54 billion	0	RMB 1.02 billion
Total:	38		47	

As shown in the above table, the appeal of Mainland mutual funds to Hong Kong investors has been much lower, due possibly to the wide availability of existing funds with a Mainland focus. In comparison, there has been greater appeal of Hong Kong mutual funds to the Mainland investors. However, net flows into Hong Kong mutual funds have been dropping in the past few years, possibly due to poor performance or overall downturn in the market.

[123] List of northbound funds, http://eid.csrc.gov.cn/fund; list of southbound funds, https://apps.sfc.hk/productlistWeb/searchProduct/UTMF.do.

[124] Form for Inward and Outward Remittance of Funds for sales and Issuance of Hong Kong Funds in Mainland, http://www.safe.gov.cn/safe/2018/0424/8884.html.
Form for Inward and Outward Remittance of Funds for sales and Issuance of Mainland Funds in Hong Kong, http://www.safe.gov.cn/safe/2018/0424/8885.html.

1a. 50/50 AUM Requirement

One of the reasons why the MRF scheme has not taken off as many thought it would is because of the restriction that no more than 50% of the value of a fund can be raised in the other jurisdiction[125]. This 50/50 AUM requirement limits investor monies that a Hong Kong fund can raise in the Mainland to the AUM in Hong Kong, which is a much smaller market compared to the Mainland market. There was a reported case in 2021 where a Northbound MRF had to cease selling to Mainland investors when it approached the 50% limit.[126]

While we understand the reciprocal nature of the MRF in requiring half the value of a fund to be raised in the fund's home jurisdiction, and the other half in the host jurisdiction, the undeniable fact is that the Mainland market is much larger than Hong Kong's, and it would be very difficult for Hong Kong funds to grow their Investor monies in Hong Kong to match that in the Mainland. This limits the profitability and attractiveness of the scheme for global fund managers to apply for recognition of their Hong Kong funds in the Mainland.

Recommendation:

We recommend that the requirement of no more than 50% of the fund value to be raised in the host jurisdiction be removed or increased for northbound Hong Kong funds.

1b. Fund Eligibility and Delegation

Currently, only funds domiciled in Hong Kong that are managed by asset managers registered with and licensed by the SFC are eligible for the northbound MRF[127]. In addition, the funds' asset manager cannot delegate its investment management functions to a party operating outside Hong Kong[128]. These requirements diminish Mainland investors' opportunity to diversify their investment to a broader scope of funds, such as UCITS that invest in many other markets and which are widely sold to Hong Kong retail investors, as well as to leverage the expertise of fund managers in other markets.

Recommendation:

Allowing more flexibility in the location where a fund is domiciled for the northbound MRF, particularly for globally recognised funds like UCITS, would not only offer Mainland investors more choices but

[125] Item 5, Article 4 of the *Interim Provisions on the Administration of Recognized Hong Kong Funds* (《香港互认基金管理暂行规定》).

[126] JPMorgan Pacific Technology Fund ceased selling to Mainland investors, https://mp.weixin.qq.com/s/LFNi9NNoEAIGvdCAvLwykg.

[127] Items 1 and 2, Article 4 of the *Interim Provisions on the Administration of Recognized Hong Kong Funds* (《香港互认基金管理暂行规定》).

[128] Item 2, Article 4 of the *Interim Provisions on the Administration of Recognized Hong Kong Funds* (《香港互认基金管理暂行规定》).

also enhance the attractiveness of the MRF to global fund managers who may not have set up funds in Hong Kong. In the absence of allowing overseas domiciled funds to be eligible for the MRF, allowing delegation of investment management by Hong Kong fund managers to offshore managers would help expand the fund choices to Mainland investors which can benefit from access to funds with more diversified investments.

2. Wealth Management Connect

Background and opportunities for the Greater Bay Area ("GBA")

The Cross-boundary Wealth Management Connect scheme ("WMC Scheme"), launched in September 2021, is the first mutual market access mechanism for individual investors in the Guangdong-Hong Kong-Macao Greater Bay Area ("GBA") to make cross-boundary investment in wealth management products distributed by eligible banks operating in the GBA through a closed-loop funds flow channel.

The introduction of the WMC Scheme and cross-boundary investment in the GBA is a key milestone of the opening of the financial markets in the GBA and represents an important breakthrough in the financial development of the area. With a population of more than 86 million and a combined GDP of over USD1.9 trillion, [129] the GBA accounts for over 10% of the GDP of China[130] and the WMC Scheme plays an important role in advancing the financial and economic development within the GBA.

As of the end of May 2023, there are 23 Hong Kong banks participating in the Southbound Scheme and 22 Hong Kong banks participating in the Northbound Scheme.[131] While the WMC Scheme has attracted significant interest in the market when it was announced, neither the Northbound Scheme nor the Southbound Scheme has generated as much flows as expected. The aggregate quota allocated to the WMC Scheme (for both Northbound and Southbound) is RMB 150 billion but as of 16 April 2023, the net value of cross-boundary remittances under the Northbound Scheme and the Southbound Scheme were approximately RMB 260.8 million and RMB 608.65 million respectively, representing approximately 0.17% and 0.41% of the aggregate quota respectively.[132]

One of the reasons for the lack of flows under the WMC Scheme could be due to the COVID-related travel restrictions that were in place between Hong Kong and other areas within the GBA until January 2023. This is likely a significant factor given that eligible investors who wish to invest in wealth management products distributed by banks operating in another jurisdiction within the GBA are

[129] 2021 figure; based on statistics published by the Hong Kong Trade Development Council, https://research.hktdc.com/en/article/MzYzMDE5NzQ5.
[130] 2021 figure; based on statistics published by the World Bank, https://data.worldbank.org/indicator/NY.GDP.MKTP.CD?locations=CN.
[131] Based on statistics published by the Hong Kong Monetary Authority, https://www.hkma.gov.hk/eng/key-functions/international-financial-centre/wealth-management-connect/.
[132] Based on statistics published by the Guangzhou branch of the People's Bank of China, http://guangzhou.pbc.gov.cn/guangzhou/129196/4332364/index.html.

generally required to physically travel to such jurisdiction to open an investment account to facilitate such investment under the WMC Scheme. Set out below are some of the key reasons why the WMC Scheme has not been as successful as some of the other Mainland-Hong Kong connect schemes.

1. **Account opening in other jurisdiction**. Under the Southbound Scheme, eligible Mainland investors must open a new investment account with the relevant Hong Kong bank, dedicated for investment under the southbound WMC Scheme, regardless of whether they already maintain existing bank accounts with such a Hong Kong bank. However, at ASIFMA's suggestion, the final rules provide that eligible Mainland investors may apply to open a dedicated investment account for the southbound WMC Scheme either in person in Hong Kong or by attestation (i.e., the verification of the client's identity and identification documents through certification by the partnering Mainland bank) in the GBA, avoiding the need to travel to Hong Kong.

   Under the Northbound Scheme, eligible Hong Kong investors holding bank accounts with investment functions with the relevant Mainland banks in the GBA may opt to designate such accounts as their dedicated investment accounts for the Northbound Scheme. However, investors who do not have any existing investment accounts with the Mainland bank are required to physically travel to the Mainland to open new investment accounts with the Mainland bank for the purpose of facilitating investment under the Northbound Scheme.

   Recommendation:

   To encourage more Hong Kong investors to participant in the Northbound Scheme, we suggest providing Hong Kong investors with the same or similar attestation option in Hong Kong in lieu of having to physically travel to Mainland cities within the GBA to open an investment account with Mainland banks in person. If it is not feasible to provide such option to Hong Kong investors, we recommend waiving the in-person account opening in the GBA for Hong Kong investors who are existing clients of the relevant Mainland banks in Hong Kong since such banks would already have conducted their KYC and due diligence procedures on such clients.

2. **Product limitation.** Aside from the account opening issue, one of the key reasons for the lack of investor participation in the WMC Scheme is the product limitations. Currently, only products involving low to medium risk are eligible for trading under the WMC Scheme. Given that low to medium risk products generally include bond and some balance funds and hardly any equity funds, and interest rates on fixed income products tend to be low, products available under the WMC Scheme are generally not attractive to investors who expect higher returns.

   As an alternative to the WMC Scheme, investors seeking for fund investments with higher returns may invest in local funds or cross-boundary funds through the MRF scheme, both of which are not limited to low to medium risk funds. Equity funds, which are viewed as high risk, used to account for 50-60% of total fund sales in Hong Kong but in 2022, equity fund sales represented 33% of total fund sales in Hong Kong, with mixed or balance fund sales representing 35%.[133] According to the Asset Management Association of China's *National Public Fund Market Investor Situation Survey Report 2020* (《全国公募基金市场投资者状况调查报告（2020 年度）》)[134], over 70% of Mainland retail investors chose equity funds (excluding index funds) as their preferred mutual fund investment. Unless equity funds are included in the WMC Scheme, investors' interest in the WMC Scheme will remain limited.

Recommendation:

We recommend expanding the wealth management products available under the WMC Scheme to cover a) higher risk products, including equity funds; b) products domiciled outside of Hong Kong; and c) Hong Kong-domiciled funds that feed into overseas funds. This would provide GBA investors with more investment options and opportunities for diversification, especially since a lot of Hong Kong domiciled funds invest in the Mainland.

In the 2023-24 Budget Speech given by the Hong Kong Financial Secretary on 22 February 2023, the Hong Kong government announced its plan to further widen mutual market access between the Mainland and Hong Kong and enhance the WMC Scheme.[135] The chief executive of the HKMA further announced at the Bloomberg Wealth Asia Summit on 9 May 2023 that the HKMA is in on-going discussions with the Mainland authorities regarding plans to widen the product suite available under the WMC Scheme, potentially to global equity products, and hopes to launch "Wealth Management Connect 2.0" in the near future. The market welcomes this initiative and awaits to see further implementation details of these enhancements to the WMC Scheme.

3. **Participant Limitations**. The WMC Scheme imposes eligibility requirements on the participants of the Scheme, i.e., the investors and the banks. For example, investors with less than two years of investment experience and/or household financial assets valuing less than RMB 2 million (or RMB 1 million, calculated on a net basis) are not entitled to invest under the WMC Scheme. In addition, each individual investor is subject to an investment quota of RMB 1 million in aggregate under the WMC Scheme. Considering the capital requirement for eligible investors and the aggregate quota allocated to the WMC Scheme, the individual investment quota is relatively small.

[133] Based on statistics published by the Hong Kong Investment Funds Association, https://www.hkifa.org.hk/upload/Documents/Retail-Funds/Sales-Redemptins-Data/2022-YTD.pdf.
[134] National Public Fund Market Investor Situation Survey Report 2020 (《全国公募基金市场投资者状况调查报告（2020 年度）》),https://www.amac.org.cn/researchstatistics/report/tzzbg/202201/P020220107702402352747.pdf.
[135] The 2023-24 Budget Speech, https://www.budget.gov.hk/2023/eng/speech.html.

Recommendation:

We welcome the proposal to raise individual investment quota under "Wealth Management Connect 2.0" initiative mentioned by the HKMA at the recent Bloomberg Wealth Asia Summit held in May 2023. For the WMC Scheme to achieve greater success, we recommend that the individual investment quota be increased or that investors be distinguished by two categories, i.e., retail investors and professional investors, with their individual investment quota being increased respectively.

Currently, only banks meeting certain eligibility requirements are entitled to participate and distribute mutual fund/wealth management products under the WMC Scheme. As some of these products are also sold or distributed by securities companies and fund management companies (in the Mainland) and private banks (in Hong Kong and Macao), we recommend that these entities be added to the eligible participants under the WMC Scheme to further enhance the rate of usage of the WMC Scheme.

4. **Investment advice and role of product manager**. The WMC Scheme was established on the basis of an "execution only" or a "non-solicitation" model to avoid cross-boundary marketing and regulatory issues. However, it is difficult for investors to assess the investment potential and attractiveness of specific products available under the WMC Scheme given they are not able to enquire or obtain advice from the product issuer or the bank distributing the products without travelling to the relevant jurisdiction. This is likely to have been a significant deterrent to participation in the WMC Scheme.

   Recommendation:

   To enhance investors' understanding of products available under the WMC Scheme and allow investors to make informed investment decisions, we recommend that the strict non-solicitation model be relaxed so that educational and information sessions can be conducted by product issuers across the different jurisdictions within the GBA, and if necessary, in the presence of or together with the distributing bank. While the relevant regulatory authorities across different jurisdictions within the GBA may need to reach a mutual understanding or enter into cooperation agreements in respect of this, the relaxation of the non-solicitation model will certainly boost the rate of participation in the WMC Scheme and facilitate its further development.

5. **Tax implications.** Conducive tax policy is often an important determinant of the success of cross-border investment schemes.

   Recommendation:

We recommend that the tax treatment of investors under the WMC Scheme should be simple to understand, easy to implement, and reciprocal between the Mainland, Hong Kong and Macau. We recommend broad tax exemption, including exemptions on corporate income tax, individual income tax and value added tax on any income, capital gains and distributions derived from all investments made under the WMC Scheme, as this will make them similar to the MRF, Stock Connect and Bond Connect schemes. Tax rules that are complicated and unclear will have especially adverse impacts on individual investors as they do not have the sophistication or resources to handle the complexities.

In addition, we recommend that specific tax regulations or administrative measures be introduced to provide a clarity that the WMC-related cross-border activities undertaken in the GBA by participating Hong Kong banks or Hong Kong product issuers (e.g., Hong Kong asset managers) do not create any taxable presence in China from both corporate and individual income tax perspectives.

6. **Cross-boundary payment and settlement**. In a survey conducted by the Hong Kong Institute for Monetary and Financial Research,[136] the survey participants have identified three key challenges[137] in respect of the conduct of cross-boundary payment and settlement activities as follows:

(i) the lack of fully automated processes for performing payment and settlement activities;

(ii) the reliance on legacy technology in performing payment and settlement activities; and

(iii) the inconsistency of standards, protocols and procedures applied across different jurisdictions within the GBA.

These hurdles not only increase the complexity of cross-boundary payment and settlement transactions within the GBA and limit the efficiency of carrying out such transactions, but also give rise to heightened security concerns and risk of error.

Recommendation:

[136] Hong Kong Institute for Monetary and Financial Research, "Cross-boundary Payment and Settlement Systems in the Greater Bay Area" (dated March 2023), https://www.aof.org.hk/docs/default-source/hkimr/applied-research-report/gbarep.pdf.

[137] A total of 58 institutions participated in the survey. Of these institutions, 31 were from the banking sector, 14 were from the insurance sector and 13 were from the asset management sector.

The market awaits to see further refinement on the selling process for wealth management products under "Wealth Management Connect 2.0". We recommend enhancing the cross-border payment and settlement systems within the GBA by automating processes and implementation of a set of standards, protocols and procedures to be applied consistently across different jurisdictions within the GBA.

3. QDII

As of December 2022, SAFE has released a total of around USD 159.7 billion of QDII quotas to institutional investors across segments; while we welcome the continued approval for increasing total quotas, it is observed that the year-on-year growth rate is relatively small at around 1.5%[138].

Recommendation:

Diversification of investments, which include investments in markets outside the home jurisdiction, is important for all investors. Therefore, expanding the QDII scheme for domestic institutional investors is important for them to be able to take advantage of potential higher returns in other markets as well as to learn from investing abroad.

In addition, expanding the investment scope under the QDII scheme is also recommended. Based on the *Implementing Rules for the Interim Administrative Measures on the Overseas Investment of Insurance Funds* (《保险资金境外投资管理暂行办法实施细则》), we suggest that the NAFR consider including private credit funds (e.g., senior, mezzanine and special situations debts) as one of the eligible overseas assets classes which Chinese insurers can invest in under the QDII scheme. We have seen a trend of global insurers working to increase asset allocation into private credit over the years, taking capital efficiency under the Solvency II framework into consideration. We believe that broadening the scope of eligible investments for insurers will further meet the growing needs of asset allocators in China and will encourage further development and sophistication in the market.

4. QDLP

There is currently a relatively small number of overseas alternatives managers that have looked to obtain a QDLP licence in the Mainland, which we believe is due to a lack of clarity around what is required by them to apply, and regional variations in the interpretation and implementation of the QDLP approval process.

Recommendation:

[138] Report of Securities Daily, http://www.zqrb.cn/fund/jijindongtai/2022-12-17/A1671240994822.html.

We suggest the relevant regulatory bodies continue to fine-tune the guidance, and promote standardization of the QDLP workflow. We believe such actions will further encourage and attract well-established alternatives managers to enter the Chinese market, thereby enhancing the product offerings available to onshore investors.

Recommendations for Other Connects
In respect of **MRF**: 1. Allowing more flexibility in the location where a fund is domiciled for the northbound MRF would not only offer Mainland investors more choices but also enhance the attractiveness of the MRF to global fund managers who may not have set up Hong Kong domiciled funds. In the absence of overseas domiciled funds being eligible for the MRF, allowing delegation of investment management by Hong Kong fund managers to offshore managers would help expand the fund choices to Mainland investors which can benefit from access to funds with more diversified investments. In respect of the **WMC Scheme**: 2. Remove the requirement for face-to-face account opening with Mainland banks under the Northbound Scheme or waive such requirement for investors who are existing clients of the relevant Mainland banks in Hong Kong. 3. Broaden the scope of products available under the WMC Scheme to cover higher risk products, including equity funds and products domiciled outside of Hong Kong or Hong Kong-domiciled funds that feed into overseas funds. 4. Increase individual investment quota, or distinguish investors by two categories, namely retail investors and professional investors, and increase their individual quota respectively. 5. Broaden the range of eligible distributors by allowing securities companies and fund management companies to distribute products under the WMC Scheme. 6. Relax the non-solicitation model such that educational and information sessions can be conducted by product issuers across the different jurisdictions within the GBA, if necessary, in the presence of or together with the distributing bank. 7. Implement broad tax exemption, including exemptions on corporate income tax, individual income tax and value added tax on any income, capital gains and distributions derived from all investments made under the WMC Scheme. 8. Provide clarity that cross-border activities undertaken under the WMC Scheme in the GBA by participating Hong Kong banks or asset managers do not create any taxable presence in China from both corporate and individual income tax perspectives. 9. Enhance the cross-border payment and settlement systems within the GBA by automating processes and implementing a set of standards, protocols and procedures to be applied consistently across different jurisdiction within the GBA. In respect of **QDII**:

10. Continue to promote the QDII scheme as a key cross-border channel that would provide domestic institutional investors access to offshore markets where they may be able to get a higher return and to learn from such investments.
11. Broaden the scope of overseas eligible investments for insurers to include private credit funds (e.g., senior, mezzanine and special situations debts).

In respect of **QDLP**:

12. Fine-tune the regional guidance on QDLP approval process, and promote standardization of the QDLP workflow.

H. Cross-Border Data

China has witnessed the acceleration of the digital economy in the past few years. A Nikkei survey showed that, in 2019, China accounted for 23% of global cross-border data flows, while the United States ranked second at 12%.[139] Further provided by a national data report, China is the second largest country for data in 2022, with 8.1ZB of data production within the year, which accounts for 10.5% of the total global data.[140] As the huge quantities of data resource will be invaluable to the economic competitiveness, China places increasing emphasis on the data security, especially the regulation of cross-border data transfers. Within the finance industry, sectoral rules impose more detailed requirements on the protection of financial data, including personal financial information. While the industry is supportive of data protection, we expect the cross-border data rules in China to align with international best practice, and achieve the balance between the free flow of data and security of data. Uncertainties amongst the cross-border data rules may make it difficult for the industry to fully comply with those requirements, and we await further clarification and detailed guidance from the Chinese authorities to ensure the effective implementation of the cross-border data rules, and to facilitate the orderly movement of data without inhibiting the efficient functioning of capital flows.

The *Institutional Reform Plan of the Party and the State* (《党和国家机构改革方案》) released in March 2023 is also noteworthy, which optimises and adjusts the responsibilities of institutions in key areas such as financial supervision and data management. In accordance with such plan, China will establish a National Data Bureau (NDB, 国家数据局) to be responsible for advancing the development of data-related fundamental institutions; coordinating the integration, sharing, development and application of data resources; and pushing forward the planning and building of a “digital China, the digital economy and a digital society”. Certain functions of the Cyberspace Administration of China (CAC) and the National Development and Reform Commission (NDRC), in connection with the “digital China, the digital economy and a digital society” and data infrastructure, will be re-assigned to the NDB. In addition, a National Administration of Financial Regulation (NAFR, 国家金融监督管理总局) has been set up on 18 May 2023 accordingly on the basis of the CBIRC, and its scope of regulatory jurisdiction has been expanded to incorporate PBOC’s regulatory responsibilities in connection with financial groups and financial consumer protection, as well as the investor protection responsibilities of CSRC.

1. Data Export Paths

1a. Definition of Important Data and CII

Under the framework of three keystone laws, namely the *Cybersecurity Law* (《网络安全法》， CSL), the *Data Security Law* (《数据安全法》， DSL) and the *Personal Information Protection Law* (《个人

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[139] Nikkei, 24 November 2020, China Rises as World’s Data Superpower as Internet Fractures, https://kr-asia.com/china-rises-as-worlds-data-superpower-as-internet-fractures.

[140] Cyberspace Administration of China, 23 May 2023, *Digital China Development Report (2022)* (《数字中国发展报告（2022 年）》), http://www.cac.gov.cn/2023-05/22/c_1686402318492248.htm.

信息保护法》，PIPL), the personal information and important data collected by Critical Information Infrastructure (CII) Operators must be stored within the Mainland's borders and subject to cross-border transfer security assessment.

Given that the obligations on CII operators and important data processors are significant, ASIFMA's key concern is the unclear definitions of CII and important data in the financial sector:

- **CII**. The *Regulations on the Security and Protection of Critical Information Infrastructure* (《关键信息基础设施安全保护条例》) issued in 2021 only provides a general scope of CII and allows the competent regulators in the respective industries and sectors to formulate the CII identification rules and organize the identification work. So far, the Chinese financial regulators have not published relevant CII rules or CII lists for the financial sector yet.

- **Important data**. Although, the TC260 is improving the *Information Security Technologies – Guidelines on the Identification of Important Data (draft for comments)* （《信息安全技术 重要数据识别指南（征求意见稿）》）and also drafting the *Information Security Technologies – Security Requirements for Processing Important Data* （《信息安全技术 重要数据处理安全要求》）, due to the lack of important data catalogue in the financial sector, the specific scope of "important data" can be confirmed only after regulatory review. Besides the aforesaid national standards themselves, implementation in the financial sector and CAC's attitudes on them are yet to be clarified.

Recommendation:

We welcome regulators to provide further clarifications on these key concepts, thus diminishing the uncertainty that prevents companies from efficiently using data falling into these categories.

We recommend defining CII and important data explicitly on the basis of balancing cyber/data security and the need of free data flows for efficient business operations, and adopt a risk-based management approach. Particularly, we recommend clarifying that the scope of important data only covers data which impacts the PRC's national interests and not merely the data exporter's interests.

1b. Data Export Paths

The aforesaid three keystone laws have established the basic paths of data export for firms in China, including:

- **Security assessment**: passing a security assessment organised by the CAC where required;
- **Certification**: obtaining a personal information protection certification issued by a specialised institution; and
- **Standard Contract**: concluding a contract with the overseas recipient based on the standard contract formulated by the CAC.

We are delighted to see the regulatory development of China's data export regime in recent years, with the taking effect of the *Measures for Data Export Security Assessment* (《数据出境安全评估办法》), the release of a new set of TC260 （全国信息安全标准化技术委员会） specifications for certification of cross-border transfer of personal information, and the issuance of the long-awaited *Standard Contract for Cross-border Transfer of Personal Information* (《个人信息出境标准合同》). However, some requirements under the data export paths have aroused controversy in the industry and may significantly increase the compliance costs of both foreign and domestic firms.

(1) Security Assessment

The CAC issued the *Measures for Data Export Security Assessment* (《数据出境安全评估办法》) in 2022 which was followed by relevant application guidelines to provide detailed guidance and reference on how to perform the security assessment. Pursuant to such measures, if any of following circumstances is triggered, the security assessment organized by the CAC must apply:

- The data processor transfers important data (重要数据) offshore;
- The CII operator (关键信息基础设施运营者) or the data processor that processes personal information of over one million people transfers personal information offshore;
- The data processor that has provided personal information of over 100,000 people or sensitive personal information of over 10,000 people, in each case on a cumulative basis, since 1 January of the previous year, transfers personal information offshore.

In terms of application procedures and methods for security assessment, the regulators are still working to review the thousands of self-assessment materials submitted by market, and we expect to receive clearer guidance after CAC has completed summarizing the results.

Recommendations:

- We recommend establishing online application channels to streamline the application process and promote the communication between enterprises and regulatory authorities (we are aware of the online application platform launched by Suzhou CAC, [141] and we look forward to a unified application platform at the national level).

[141] Suzhou Data Export Security Assessment Application and Filing Platform (苏州市数据出境安全评估申报备案平台): https://jy.suzhou.com.cn/dataexport/#/export-index.
Instruction for the Platform: https://www.ourjiangsu.com/a/20230303/1677810563234.shtml.

- It is also recommended for the regulators to embrace flexibilities in the security assessment report and other application materials submitted by data processors, such as the requirements on the disclosure of some hard-to-access information (e.g., IP addresses of offshore data centers).

- We expect further interpretations from the regulators regarding the carve-outs to the security assessment requirements. For example, if a company processes more than 1 million clients' personal information (without transferring any clients' personal information outside of China), it will be subject to the data export security assessment when it transfers only a few hundred employees' personal information offshore for internal HR management purposes. This will significantly increase the compliance cost of market players.

- We also welcome regulators to confirm whether data transfers to Hong Kong, in the context of the GBA development, will be deemed as cross-border transfers, and if so, whether a more streamlined and less stringent process is available for data transfers to Hong Kong.

(2) Certification

China's certification regime for cross-border transfers of personal information has recently been further developed. In November 2022, the SAMR and the CAC jointly issued the *Notice for the Implementation of Personal Information Protection Certification* (《关于实施个人信息保护认证的公告》). TC260 also released version 2.0 of the non-binding practice guide titled *Specifications for the Security Certification of Personal Information Cross-Border Processing (Certification Rules 2.0)* (《网络安全标准实践指南—个人信息跨境处理活动安全认证规范 V2.0》), and the draft national standard titled *Certification Requirements for Cross-border Transfer of Personal Information* (《信息安全技术 个人信息跨境传输认证要求（征求意见稿）》). Under the aforesaid rules, the applicable scope of the certification regime is now extended to cover all cross-border transfers of personal information rather than merely the intra-group transfers of personal information stipulated in the previous versions.

In addition, the certification path does not seem to have significant advantages over the standard contract path. The certification path requires the personal information processers to conduct the personal information protection impact assessment (个人信息保护影响评估, PIPIA), enter into binding and enforceable legal documents with overseas recipients, and comply with the same corporate rules with overseas recipients. Both the personal information processers and overseas recipients shall set up the data protection organization and designate the responsible person for personal information protection, and are further subject to the continuous supervision of the certification institutions (接受认证机构的持续监督).

(3) Standard Contract

The long-awaited *Standard Contract for Cross-border Transfers of Personal Information* (《个人信息出境标准合同办法》, the "Standard Contract") was released on 24 February 2023 and took effect on 1 June 2023.

ASIFMA submitted its consultation response to the CAC on 29 July 2022 in respect of the draft Standard Contract, and we are pleased to see that some of ASIFMA's recommendations appear to have been reflected in the final Standard Contract. It is clarified in the Standard Contract that the separate consent must be obtained when the cross-border transfer of personal information is based on individuals' consent ("基于个人同意向境外提供个人信息的，应当取得个人信息主体的单独同意"), which means that, if the cross-border transfer of personal information is based on other legal bases instead of individual's consent, the separate consent is not required for that data export activity.

According to the Standard Contract, Article 4, Paragraph 6 requires the overseas recipient shall immediately notify the personal information processor (个人信息处理者) after receiving a request to provide any personal information hereunder from a government authority or judicial body of the country or region where it is located. However, for many financial institutions, it is not feasible for them to give the notification as it may trigger a "tipping off" offence under the AML/CFT laws for which those financial institutions are required to comply in the jurisdictions they are located. In general, "tipping off" means a criminal offence for anyone to release information which is likely to prejudice an investigation once an internal or external suspicion report has been made. We would suggest adding some caveats to this paragraph, such as "to the extent permitted by the laws and regulations that the overseas recipients are subject to".

Recommendations:

By issuing the Standard Contract, CAC creates a comprehensive and flexible legal framework for cross-border transfers of personal information. Still, since the industry recognizes the Standard Contract as one of the key mechanisms facilitating cross-border transfer of personal information, we recommend further considering the following issues under the Standard Contract:

- The application scenarios of Standard Contract: Unlike the Standard Contractual Clauses under the GDPR which provides four modules (i.e., controller to controller, controller to processor, processor to controller, and processor to processor), China's Standard Contract has only one form, which can be used for transferring personal information by a personal information processor (个人信息处理者) (akin to a controller under the GDPR) to an overseas recipient. In this regard, under the PIPL and the Standard Contract, it is unclear how a China based entrusted party (受托人) legitimizes its necessary data transfer to overseas recipients. We recommend this is interpreted and clarified by the CAC.

- Modification to Standard Contract: We recommend allowing the Standard Contract's wording to be modified provided the substance of all prescribed safeguards is maintained, so that FIs may leverage existing data transfer agreements if substantially similar to the Standard Contract.

- The personal information protection impact assessment (个人信息保护影响评估，PIPIA) report: Although the Standard Contract provides the risk factors to be assessed in the PIPIA report and CAC also issued the *Filing Guidance of Standard Contract for Cross-border Transfers of Personal Information (First Edition)* (《个人信息出境标准合同备案指南（第一版）》), ASIFMA recommends further clarifications from the CAC. For instance, one of the assessment factors is whether laws and policies of the overseas recipient's jurisdiction will impact the performance of the Standard Contract. As PRC domestic entities are unfamiliar with foreign laws and policies, such an assessment is burdensome for them and increases their compliance costs. In this regard, the standardized assessments on foreign laws and policies published by the CAC are recommended to ensure market consistency. To align with international best practice, ASIFMA also recommends a "white-list" or similar mechanism that reduces the burden on domestic entities under the cross-border data transfer regime.

1c. Cross-Border Cooperation

China has been speeding up its digital development and expanding institutional opening-up in recent years, and advanced negotiations on joining the *Digital Economy Partnership Agreement* (DEPA) since 2022.[142] Against this background, we recommend forming best-in-class digital trade agreements with more like-minded countries to facilitate "trusted data flows", and suggest that a specific work track between the public and private sectors of both countries be created to classify the type of data that should be eligible for cross-border exchange, assess the sensitivity of each data type, and agree on an acceptable oversight and assurance model that brings certainty to the compliance process at the sectoral level, while harnessing the benefits of cross-border data transfers.

We also promote cross-border financial regulatory dialogues, to share best practices, resolve potential frictions, and establish regulator-to-regulator memoranda of understanding to provide more detail on implementing commitments to cross-border data flows.

In line with recommendations from international agreements such as the Regional Comprehensive Economic Partnership (RCEP)[143], FIs should be allowed to conduct cross-border data transfers where necessary in the ordinary conduct of business.

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[142] The State Council Information Office, 23 August 2022, China Advancing Negotiations on Joining DEPA: Commerce ministry, http://english.scio.gov.cn/pressroom/2022-08/23/content_78384212.htm.

[143] According to the Article 9(2) of Annex 8A of Chapter 8 (Financial Services) in RCEP, a Party shall not take measures that prevent: (a) transfers of information, including transfers of data by electronic or other means, necessary for the conduct of the ordinary business of a financial service supplier in its territory; or (b) processing of information necessary for the conduct of the ordinary business of a financial service supplier in its territory, https://rcepsec.org/wp-content/uploads/2020/11/Chapter-8-Annex-8A.pdf.

2. Cross-border Sharing of Data in Financial Sector

While CSL, DSL and PIPL provide the basic data export paths, there are still many challenges faced by industry participants for the cross-border sharing of certain data in the financial sector, such as research data, shareholding information and AML/CTF information. Restrictions on data sharing may discourage the entry and/or continued operation of international institutions, as they are restrained from sufficiently leveraging the benefits of global expertise and centralized infrastructure, and risk control functions. We fully understand the importance of data security to national security, economic stability and legitimate rights and interests of domestic entities and individuals. On the other hand, more clarified and tailor-made rules are necessary to enable cross-border sharing of data in the financial sector. Therefore, ASIFMA proposes a number of carve-outs from the general prohibitions, and a risk-based approach towards the sharing of research data, shareholding information, as well as AML/CTF information. We would like to work with PRC authorities to enable the better adoption of such risk-based approach while having adequate controls on cross-border data transfers.

2a. Research and Analysis Data

The ability to share research and exchange investment outlook and views as well as portfolio or financial analysis between international asset managers and their wholly or majority owned subsidiaries onshore is a critical part of their strategy, and a key factor in their attraction to investors on a global scale (see ASIFMA's February 2023 white paper, *Importance of Research Sharing to Global Asset Managers*). The benefits of research sharing include but are not limited to:

- Broadens the views of onshore analysts with experiences and knowledge acquired in other markets, which ultimately benefits Chinese investors;

- Deepens foreign investors' understanding of the China market from the sharing of local knowledge and experience, thereby attracting more foreign investments;

- Brings global best practices in compliance, risk control and monitoring that would better protect the interests of Chinese investors;

- Develops local asset management talent both for the domestic market and also for future outbound investments;

- Prepares China to be a regional financial asset management hub that will service both local and global investors.

Some restrictions imposed by Chinese regulations in terms of research and analysis data sharing may impact international asset managers and their domestic subsidiaries disproportionately.

The *Measures for Supervision and Administration of Publicly-offered Securities Investment Fund Managers* (《公开募集证券投资基金管理人监督管理办法》) issued by the CSRC requires that the public fund management companies (FMC) put in place the measures to ensure that the FMC's research and investment decisions are scientific, professional, independent and objective. While international asset managers adopt a global research sharing model, portfolio managers manage their portfolios independently, in accordance to their own investment thesis and investment objectives of their funds/clients while taking into account the research information available to them. FMC's portfolio managers, in compliance with Chinese law, should be making their own independent investment decisions. However, research sharing should not be equated with investment decisions. The safeguarding of the independence of investment decisions does not necessarily require the prohibition of research sharing, and the risks associated therewith can be mitigated by adopting proper corporate governance, procedures, and controls.

In addition, the *Guidelines for the Governance of Securities Investment Fund Management Companies (for Trial Implementation)* (《证券投资基金管理公司治理准则（试行）》) issued by the CSRC provide that FMC shareholders shall not, directly or indirectly, request the company's directors, management personnel or staff members to provide non-public information or materials on fund investment, research, etc. CSRC's concerns over FMCs in sharing information with its shareholders may be that FMCs manage retail public funds and the leakage of any non-public information of the FMC may hurt the interest of retail investors. However, it is a common requirement and widely accepted global practice that financial institutions have in place policies, procedures and controls on their access and use of non-public information.

Overall, the benefits of allowing research and analysis sharing between international asset managers and their onshore subsidiaries outweigh the risks, and the latter can be mitigated by adopting proper corporate governance and controls.

Recommendation:

ASIFMA recommends FMCs be allowed to exchange and share research and analysis information with their global counterparts.

2b. Shareholding Information

There is a need for Chinese firms to share their shareholding information in listed companies with its overseas affiliates, to ensure the monitoring of the shareholding positions by investors acting in concert. We understand certain PRC laws and regulations prohibit the FMC or bank wealth management subsidiaries (BWMS) from providing non-public information [144] or key sensitive

[144] Article 19 of the *Guidelines for the Governance of Securities Investment Fund Management Companies (for Trial Implementation)* (《证券投资基金管理公司治理准则（试行）》) provides that an FMC shareholder

information[145] with their shareholders. Although shareholding information may be regarded as non-public information unless it reaches 5% or more of the shares of a listed company, aggregation of group holdings at the global level in a listed company is necessary for the group to monitor their global or overall shareholding positions, and comply with the disclosure obligations under the applicable laws and regulations. Similar disclosure requirements can be found in PRC laws and regulations, such as Article 16 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和人民币合格境外机构投资者境内证券期货投资管理办法》).

Recommendation:

In this regard, ASIFMA recommends that shareholding information be treated as an exception of non-public information, and thus is allowed to be shared within the group (including being shared by an onshore entity to its offshore affiliates within the same group).

In addition, the purposes to set those information sharing restrictions under the PRC laws and regulations are based on the consideration of independence of FMC and BWMS. Proper corporate governance and internal controls adopted by FMC and BWMS can mitigate the risk of disclosing non-public information, and thus safeguard the independence of FMC and BWMS. In light of this, the sharing of shareholdings in a PRC listed company within a group for compliance with PRC disclosure obligations is unlikely to be captured by such restrictions and we request the competent Chinese authorities to further clarify such issues.

2c. AML/CTF Information

The PRC laws and regulations generally take a prudent approach to the cross-border transfer of the AML/CTF information, which is subject to strict confidentiality requirements. Pursuant to the *Anti-money Laundering Law* (《反洗钱法》), customer identity information and transaction records obtained in the course of performing AML duties or obligations must be kept confidential and not be disclosed to any entity or individual unless required by the law. The *Administrative Measures for the Freezing of Assets Involving Terrorist Activities* (《涉及恐怖活动资产冻结管理办法》) prohibit domestic institutions from providing customer identity information and transaction records to an overseas regulatory authority arbitrarily. In the banking sector, the *Administrative Measures on Anti-money Laundering and Counter-terrorist Financing by Banking Financial Institutions* (《银行业金融机构反洗钱和反恐怖融资管理办法》) specifically requires the banking financial institutions not to

shall not, directly or indirectly, request the company's directors, management personnel or staff members to provide non-public information or materials on fund investment, research, etc.

[145] Article 41 of the *Administrative Measures of the Wealth Management Subsidiaries of Commercial Banks* (《商业银行理财子公司管理办法》) provides that a BWMS should set up a key sensitive information segregation system to prevent it providing sensitive information on investment, research, client, etc. which may create potential conflict of interest to its primary shareholder as well as other entities that its shareholder hold shares in or has actual control of.

disclose the customer identity data and transaction information to any organization or individual unless required by law.

We agree that client identity information and transactional records that a domestic firm obtains from its client due diligence or KYC process should be treated confidentially, but sharing such information with its parent, whether domestic or overseas, is a critical part of internal controls and compliance, particularly when it comes to AML/CTF and prevention of insider trading and market manipulation.

Recommendation:

We observe some positive changes in the *Anti-money Laundering Law (Revised Draft)* (《反洗钱法》（修订草案公开征求意见稿）) published in 2021 to specify the application process with Chinese financial authorities for providing compliance information to an overseas regulatory authority, and we also look forward to a path for domestic firms sharing AML/CTF information with overseas parents to be prescribed by the Chinese authorities.

More broadly, we recommend that data transfers by FIs be eased for risk management or customer service purposes where customer consent has been obtained or legitimate business needs require this. This will allow for more efficient information sharing to meet the requirements of overseas regulatory authorities and will improve the effectiveness of AML / CTF measures.

Recommendations for Cross-Border Data
In respect of **Data Export Paths**: 1. Define CII and important data on the basis of balancing cyber/data security and need of free data flows for efficient business operations and adopt a risk-based management approach. 2. Establish online application channels to streamline the application process for the data export security assessment and promote the communication between enterprises and regulatory authorities. 3. Embrace flexibilities in the data export security assessment report and application materials submitted by data processors, such as requirements on disclosure of hard-to-access information. 4. Confirm whether a more streamlined and less stringent process is available for data transfers to Hong Kong. 5. Clarify how a China based entrusted party legitimises its necessary data transfer to overseas recipient if the Standard Contract would be adopted for the data export. 6. Allow the Standard Contract's wording to be modified provided the substance of all prescribed safeguards is maintained. 7. Provide further guidance on the PIPIA for personal information export, including but not limited to introducing a "white-list" or similar mechanism in connection with the assessment factor of whether laws and policies of the overseas recipient's jurisdiction will impact the performance of the Standard Contract.

In respect of **Cross Border Sharing of Data in Financial Sector:**

8. Allow research sharing and exchange of investment outlook as well as portfolio or financial analysis between international asset managers and their onshore subsidiaries.
9. Allow sharing of shareholdings in a PRC listed company within a group (including offshore subsidiaries) for compliance with PRC disclosure obligations.
10. Allow sharing of AML/CTF information within a group (including offshore subsidiaries) for internal control and compliance purposes.

I. Technology and Cybersecurity

1. Public Cloud in China

According to McKinsey[146], China is the world second largest cloud market after the United States and the size of the public cloud market in China is expected to double from 2021 to 2025 to USD90 billion. Cloud computing is an important pillar of the digital economy. According to the 14th Five Year Plan for the Development of the Digital Economy (《"十四五"数字经济发展规划》), the added value out of the digital economic core industry, which includes cloud computing, will increase to 10% of GDP by 2025. Also, the PBOC's Fintech Development Plan (2022 – 2025) (《金融科技发展规划》（2022-2025 年）) expressed support for technological innovation, including the use of cloud computing.

Despite the support from the authorities, according to a McKinsey study[147] however, public cloud adoption in China's financial sector is much lower than in other sectors which might be attributed to a lack of regulatory clarity.

Need for Regulatory Clarity

More and more global FIs are accelerating cloud adoption to leverage increased computing capabilities, boost innovation, lower costs, mitigate risk and increase operational resiliency, and many FIs have a cloud-first strategy. Many global FIs have firmwide global cloud strategies that support headquarters and affiliated entities around the world and China entities are among the beneficiary entities of such firmwide cloud arrangements. However, FIs struggle to understand the regulatory expectations from the Chinese financial regulators around the use of public cloud in China. The industry observed unclear regulatory guidance on the FIs' use of public cloud and sometimes regulatory guidance discouraging the use of public could. Global FIs need clear guidance from Chinese financial regulators around the regulatory expectations. We recommend that – in line with regulators' practices in many other jurisdictions – the Chinese financial regulators express their support for the use of public cloud by FIs in China and spell out the applicable guidelines and regulations. This would give FIs the regulatory certainty and clarity they need to develop and execute their cloud strategies in China, which in turn will benefit innovation and the resilience of the Chinese markets. The industry stands ready to share with the regulators the scenarios for different cloud adoption needs.

Group-wide Cloud Arrangements

As cloud adoption in the financial industry is accelerating, most global FIs have deployed or migrated to many cloud-compatible applications to benefit from the advantages cloud could offer. Global FIs have global systems and global public cloud strategies (e.g., global roll-out of a particular application

[146] Cloud in China: The Outlook for 2025, https://www.mckinsey.com/capabilities/mckinsey-digital/our-insights/cloud-in-china-the-outlook-for-2025.

with a global provider), benefiting the FI's group entities across the globe. Examples are management systems, reporting systems, and collaborative office systems. Such group-wide global arrangements create a consistent technology stack, support efficiencies, boost innovation and strengthen resilience. China's economy would also benefit from the adoption of global systems and applications as cross-border trade needs to be supported by global systems.

As it stands, due to the lack of regulatory certainty, it is unclear which of those global applications and setups can be extended to the FIs entities in China. This lack of clear regulatory guidance presents uncertainties to global FIs' China entities in leveraging services provided at firmwide group level and creates the risk that China entities could lag behind.

Therefore, we seek clarity from the Chinese financial regulators regarding which global cloud applications and systems can be rolled out and used by the group's entities in China and we seek confirmation that global FIs' China entities could continue to leverage internal management systems and internal collaborative office systems (such as Office 365 and Microsoft Teams) among others.

Locally Deployed Systems

For any systems that need to be locally deployed in China, we seek clear guidance from the financial regulators on regulatory expectations on regulated entities' use of public cloud in China, including any conditions on the cloud services providers that can be used.

We would appreciate if Chinese financial regulators can share their roadmap to public cloud adoption in the financial sector in China. Clear and transparent public guidelines around the use of public cloud by FIs in China would address the current uncertainty that FIs are facing when aiming to attempt cloud migration projects in China. We hope that the regulators will engage with the industry to ensure any framework, rules or guidelines can be operationalized whilst at the same time allowing FIs to fully leverage the benefits of public cloud.

Recommendations:

Industry observers have reviewed existing and draft standards and guidance relevant to cloud and would like to seek clarification on some key terms and recommendations.

1) <u>Clarity on global/local systems</u>: FIs need regulatory confirmation that FIs' entities in China can continue to use global systems and applications; and for onshore applications, clarify what are the requirements and expectations among which cloud providers can be accessed for such onshore applications.

2) <u>Clarity on PBOC's plan on cloud in the context of reported financial community cloud</u>: We note some media reports on financial community cloud. In June 2021, the regulators also drafted

the Measures for Filing of Financial Cloud (《金融云备案管理办法》) (the "Cloud Measures") and invited several FIs and Cloud Service Providers (CSPs) for comments. A Financial Community Cloud is a walled-off, highly secure hosting service, specifically designed to meet regulators' need for monitoring, investigating, and auditing the activities of financial services companies. We have concerns around the direction of travel towards Financial Community Cloud, as physical or conceptual community cloud is likely to offer inferior products and services compared to the general offerings of the hyperscale cloud, which could further limit FIs' capabilities and flexibilities to operate, scale, and innovate. Community cloud may also add to concentration risk by grouping FIs together. If the PBOC will however adopt a Financial Community Cloud, we would appreciate an update from the PBOC on the latest filing status of Financial Community CSPs and the estimated timeline to open up the use of Financial Community Clouds to FIs. As we read from the media coverage, the Cloud Measures explicitly require that FIs who use Financial Community Cloud should select those CSPs who have completed the filing requirements with the regulators. However, the Cloud Measures remain unclear whether all FIs' workloads (including core systems and non-core systems) should be on a Financial Community Cloud. We respectfully suggest that PBOC provide more clarity and the roadmap pertaining to the implementation of the Cloud Measures. FIs need this regulatory clarity as it will impact their partnership with CSPs and their cloud architecture.

2. Cybersecurity

2a. Multi-Level Protection Scheme (MLPS)

Background

The MLPS represents a more than decade-long effort to develop a comprehensive IT system security protection scheme. The scheme grades the importance of IT systems on a five-level scale according to their importance with respect to China's national security, social order, public interest, and the legitimate interests of individuals and organizations, with specific corresponding security requirements[148]. Since June 2017, the MLPS is also enshrined in the *Cybersecurity Law* (《网络安全法》) (Article 21), making compliance with the MLPS a statutory obligation.

Issues

The draft *Cybersecurity Classified Protection Regulations* (《网络安全等级保护条例(征求意见稿)》) (the "Draft MLPS Regulations") released in June 2018 outlines several significant requirements with respect to the structure and maintenance of networks operating within China. The requirement that an operator of a cyberspace graded at level three and above must establish a connection to the public

[148] Articles 6 and 7 of the *Administrative Measures for Multi-Level Protection of Information Security* (《信息安全等级保护管理办法》).

security organ at the same level are unnecessarily broad and intrusive and may introduce significant risks for industry.[149] Industry also notes the requirement to only use local technical maintenance for level three or above systems[150]. As mentioned above, global FIs in China benefit from global operation and support model, and sometimes work with global teams for technical support and maintenance. We would like to recommend that the requirement allows for such global technical support so that global FIs could fully leverage expertise available firmwide. Lastly, a cyberspace graded at level three and above is required to use certified encryption technologies, products, and services.[151] Global firms leverage consistent technology infrastructure and the consistency reduces complexity and risks. Industry would like to encourage China to allow global firms' ability to leverage international industry best practice and have consistent technology stack in China.

Recommendations:

We recommend that the MLPS:

- allows for such global technical support so that global FIs could fully leverage expertise available firmwide;
- allows global firms to leverage international industry best practice and have consistent technology stack in China.

2b. Safe and Sound Cyber Supervisory Requirements

Industry noted certain supervisory practice could inadvertently bring risks to FIs individually and the industry as a whole and would like to raise awareness of safe supervisory practice to minimize the risks to the FIs and the industry. Examples of such supervisory practice include sensitive data collection that involves detailed IT asset information and requests to conduct pen-testing (via a third party) on FIs among others.

1) Data collection and data handling

In 2022, FIs were asked to provide a large amount of information on detailed IT asset information (serial number, software version and others) to PBOC in an effort to create a sector wide IT asset management platform. The data requested are sensitive in nature and could be used to target FIs if compromised or leaked to bad actors. FIs keep sensitive data closely-held to protect itself and the sector considering the interconnectedness of financial sector. However, mandatory requirements to disclose such information to any third party outside of the firm increase digital footprints that add to cyber risks to the firm. Industry would like to highlight the risks associated with such sensitive data collection and encourage financial regulators to collect only relevant and minimum data that can meet supervisory objectives and reduce electronic footprint.

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[149] Article 30 of the *Draft MLPS Regulation* (《网络安全等级保护条例(征求意见稿)》).
[150] Article 29 of the *Draft MLPS Regulation* (《网络安全等级保护条例(征求意见稿)》).
[151] Article 47 of the *Draft MLPS Regulation* (《网络安全等级保护条例(征求意见稿)》).

Recommendations:

We commend the Chinese financial regulators for their continued measures in cybersecurity controls and capabilities, and hope they will continue to boost these controls and capabilities to provide similar level of protections financial firms have implemented based on regulatory rules and guidance in existence. Meanwhile, we suggest regulators to

- limit the collection of sensitive data to that which is directly relevant and necessary to accomplish specific purposes and explore alternative methods by adopting appropriately secure methods and practices to receive or sight the sensitive data from firms. For example, in case a regulator needs certain very sensitive data from a financial firm during the course of supervision, instead of sending that sensitive data electronically, we hope regulators can consider reviewing that data at the firms' premises, without the data leaving the firms' premises and therefore reducing the risk of a breach;

- provide timely disclosure of future material cyber events or data breaches to impacted industry members and information on what sensitive data they have gathered from the industry may have been compromised.

2) Penetration testing

Industry notes the CSRC regulatory requirements in rules [152] and the supervisory practices from the NAFR to conduct pen-testing on FIs. We understand regulators' interest in obtaining a better assessment of FIs' cyber security programs and strengths and weakness in their defences through independent testing. However, regulator-led or regulator-commissioned third party-led penetration testing could be unsafe to firms and the sector as the tests pose real risks to firms due to the potentially disruptive nature of penetration testing and the sensitivity of testing results. Testing systems and applications without operational context could create significant disruption to firm operations. Testing provides a point-in-time assessment of a specific vulnerability. It is only one of many tools a firm uses as part of a mature "defence-in-depth" approach to evaluating risk and the efficacy of controls and will not provide the comprehensive view in terms of assurance of a firm's overall security posture.

Recommendation:

[152] For example, the CSRC's *Measures for the Information Technology Management of Securities and Fund Operators* (《证券基金经营机构信息技术管理办法》) (Article 56) explicitly states that pen-testing is a way for CSRC to conduct IT management inspection over operating institutions. The CSRC *Cybersecurity Measures for the Securities and Features Industry* (《证券期货业网络和信息安全管理办法》) also states that the CSRC and its commissioned third party may conduct supervision and inspection over core institutions and operating institutions by way of vulnerability scanning and risk assessment, etc., according to which we wonder if pen-testing may be adopted as well.

We recommend that NAFR and CSRC reconsider regulatory-led or regulator-commissioned third-party-led pen-testing, recognize firm-led pen-testing and scanning, and work with FIs to identify alternative approaches that FIs could demonstrate their cybersecurity capability.

2c. Financial Sector Cybersecurity Profile

We recommend the Chinese regulators to focus on encouraging FIs to make use of a risk-and principles-based cybersecurity framework that could be appropriately applied to all financial market participants regardless of size. The global financial industry created the Financial Sector Profile[153] (or Cyber Risk Institute Profile or FSP), a cyber risk management assessment tool which allows an organization to diagnose cyber risk and apply relevant standards and best practices to appropriately manage that risk. FSP adopts a tiering mechanism that serves as a scaling device to customize the profile based on an individual institution's risk and activities. Four categories of impact are most reflective of the institution's impact: National, Subnational, Sectoral, or Localized. As an example, tier 1 institutions with national impacts are expected to assess against 277 diagnostic statements while tier 4 institutions with localized impact need only to answer to 137 diagnostic statements. FSP synthesizes the best cyber practices from industry, as well as regulators in different jurisdictions.

Recommendation:

We believe adoption of the FSP by FIs and recognition of the FSP by financial regulators would increase global regulatory harmonization and elevate the sector's cyber posture as well as make communication between firms and competent authorities in China more effective. Financial regulators could benefit from the standardized risk assessment tool to better discern the sector's systemic risk with more time for jurisdictional specialization. We hope that the Chinese regulators will join the many regulators across the globe in recognizing the FSP, such as New Zealand[154], CFTC[155], BOJ/JFSA[156], and IOSCO[157].

Recommendations for Technology and Cybersecurity
In respect of **Public Cloud in China:** 1. Clarify that FIs' entities in China can continue to use global systems and applications, and for onshore applications, clarify what are the requirements and expectations among which cloud providers can be accessed for such onshore applications. 2. Clarify PBOC's plan on cloud in the context of reported financial community cloud.

[153] Financial Sector Profile, https://cyberriskinstitute.org/the-profile/.
[154] Reserve Bank of New Zealand publishes cyber resilience guidance, https://www.rbnz.govt.nz/hub/news/2021/04/reserve-bank-publishes-cyber-resilience-guidance.
[155] CFTC Encourages Standardized Approaches to Assessing Cybersecurity Preparedness, Including the FSSCC Cy bersecurity Profile, https://www.cftc.gov/PressRoom/SpeechesTestimony/commisisonstatementtac071620?utm_source=govdelivery.
[156] Financial System Report - Annex, https://www.fsa.go.jp/news/r4/cyber/honbun.pdf.
[157] Cyber Task Force- Final Report, https://www.iosco.org/library/pubdocs/pdf/IOSCOPD633.pdf.

In respect of **Multi-Level Protection Scheme**:

3. Allow for global technical support such that global FIs could fully leverage expertise available firmwide.
4. Allow global firm to leverage international industry best practice and have consistent technology stack in China.

In respect of **Cyber Supervisory Requirements:**

5. Limit collection of sensitive data to that which is directly relevant and necessary to accomplish specific purposes and explore alternative methods by adopting appropriately secured methods and practices to receive or sight the sensitive data from firms.
6. Provide timely disclosure of future material cyber events or data breaches to impacted industry members and information on what sensitive data they have gathered from the industry may have been compromised.
7. Reconsider regulatory-led or regulator-commissioned third-party-led pen testing.
8. Work with FIs to identify alternative approaches that FIs could demonstrate their cybersecurity capability.
9. Recognize the Financial Sector Profile of Cyber Risk Institute.

J. Other Tax Matters

1. Draft VAT Law

The draft *PRC Value Added Tax Law* (《中华人民共和国增值税法（草案）》) ("the draft VAT Law") has been issued in December 2022. We are pleased that the draft VAT Law has elevated the status of the Value Added Tax ("VAT") rules in China to a legislative form, reduced uncertainties in the current rules, and implemented more of the OECD's International VAT/GST Guidelines. We have summarized key issues addressed in the draft VAT law:

1) Input tax credit for loan services

If the VAT exemption policy continues to be implemented after the VAT legislation, we would like to suggest providing the taxpayer with flexibility on adopting or waiving the exemption treatment. In addition, we would like to suggest promoting the development of fully digitalized invoice in the financial industry as soon as possible and allow financial institutions to issue VAT special invoice in electronic format. Moreover, given the need for financial institutions to upgrade their internal IT system to adapt to the increasing needs on VAT invoices, we would like to suggest the draft VAT Law would preserve adequate preparation time for the financial industry. A transition period can also be considered, i.e., allowing taking the internal vouchers as the supporting document for input VAT credit purpose.

2) Tax jurisdiction - Place of consumption rule

We recommend a clarification on the principles arising under the place of consumption rule. We would suggest that exclusion from VAT should apply if the service relates to an underlying transaction, asset, property or event arising outside of China to avoid confusion in the definition of "consumed" outside China.

3) Non-creditable items

We recommend a clarification for the un-creditable fixed assets, intangible assets, immovables involved therein, shall mean the fixed assets, intangible assets and immovables exclusively used for the aforesaid items. Otherwise, we recommend providing a simple and reasonable input tax portion method to reduce the VAT management burden and compliance cost of the taxpayer.

4) Tax jurisdiction - VAT exemption for gains derived by foreign investors from trading in financial products

We recommend providing a general exemption for offshore investors in relation to gains from trading of and payments relating to financial products and derivatives in the draft VAT Law[158]. We recommend clarifying the scope of exempted financial products and derivatives to include OTC derivatives such as FX swaps, FX options, cross currency swaps, total return swap, CNY deliverable forwards, etc. We also recommend clarifying the definition of "listing" in the VAT Law or VAT implementation rules in respect of the gains from trading of financial products by adopting the definition that is widely accepted by the financial services industry. To be specific, listing refers to being on the list (or board) of stocks, bonds, and other financial products officially traded on a public market. Furthermore, if the VAT implementation rule sets out determinative scenarios about financial products that qualify as being listed in the China market, it would help to remove the uncertainty for foreign investors investing in China's financial markets. Finally, the draft VAT law should clarify whether listing refers to the financial product being listed by a Chinese entity, or the financial product being listed in China's capital markets."

5) Scope of taxable transactions and non-taxable transactions

We suggest the VAT Law should specify general the principle that could distinguish taxable activities and non-taxable activities. Alternatively, add back the "fallback clause" of "other circumstances as prescribed by the competent fiscal and taxation authorities of the State Council" so that the detailed implementation rules could further clarify the non-taxable transactions.

6) Continuance of VAT incentives applicable to the financial industry

In addition to the list of VAT incentive policies included in Article 22 of the draft VAT Law, we suggest the VAT Law should also provide continuance of VAT incentives that is currently in force, yet not specifically included in the draft VAT Law. We have summarized below a non-exhaustive list of VAT incentives in relation to the financial services sector in China not covered by Article 22 of the draft VAT Law.

Table 7: VAT Incentives in Relation to the Financial Services Sector not Covered by Article 22 of the Draft VAT Law

VAT incentives	Relevant rules
Interbank lending exemption	Caishui [2016] No.36, Caishui [2016] No.46, Caishui [2016] No.70
Exemption for interest income derived from reverse Repo	Caishui [2016] No.46, Caishui [2016] No.70
Exemption for interest income derived from discounted bills	Caishui [2017] No.58

[158] The draft VAT Law defines taxable activities, which are potentially subject to VAT, as the sale and importation of goods, the sale of services, the sale of immoveable properties and the sale of intangible assets. Furthermore, the sale of financial product is subject to VAT only if the seller is a domestic entity or the financial products are "listed" in China. However, the scope of "financial products", how to identify the seller of financial products, and the definition of "listing" are not defined in the draft VAT Law.

VAT incentives	Relevant rules
Exemption for capital gain derived by trading of local securities by QFII and RQFII	Caishui [2016] No.36, Caishui [2016] No.70
Exemption for capital gain derived by trading of financial products in CIBM local currency market, including currency market, bond market and derivative market	Caishui [2016] No.36, Caishui [2016] No.70
Bond interest exemption for foreign financial institution	Caishui [2018] No.108
Exemption for capital gain derived by trading of A-shares through Stock Connect program	Caishui [2016] No.36 and Caishui [2016] No.127
Exemption for capital gain derived by trading of interest in funds under Mainland-Hong Kong Mutual Recognition of Funds program	Caishui [2016] No.36
Exemption for insurance premiums income derived by insurance companies from personal insurance products with insured period of more than one year.	Caishui [2016] No.36

2. Common Reporting Standard

Under the *Administrative Measures on Due Diligence Checks on Tax-related Information of Non-residents' Financial Accounts* (《非居民金融账户涉税信息尽职调查管理办法》), China introduced the legal framework for the introduction of the Common Reporting Standard (CRS). Due diligence and reporting requirements were introduced on account holders in onshore fund products. Given the lack of nominee concept in China, distributors are not seen as the account holder for CRS purposes in China and due diligence and reporting is required on the underlying investor. Practically speaking this process is undertaken by the distributor, however responsibility for compliance falls on the fund manager. This can cause issues around transfer of information where a third-party distributor is used and is inconsistent with the general process globally which places the obligation on the distributor.

Recommendation:

We recommend the responsibility with compliance would be aligned to market practice. We also note that the performance of the third-party distributors regarding CRS obligations can be revealed to the China tax authority through means such as disclosures in the annual CRS reports and self-assessment reports filed by the fund managers.

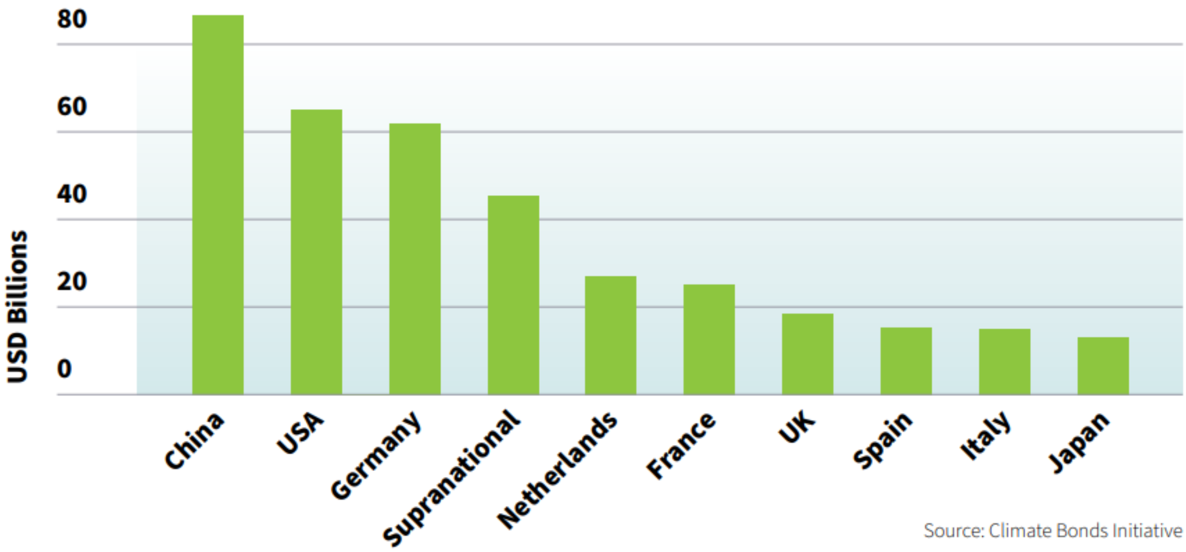
K. Sustainable Finance

1. Industry Development of Sustainable Finance in China

1a. Rapid Growth of Green Bonds Issuance

China's green bond market has experienced continuous growth since the launch of the green financial system in China in 2016 and hit a record high in 2022. Cumulative issuance of labelled green bonds in the onshore and offshore markets reached USD 489 billion (approximately RMB 3.3 trillion) at the end of 2022, of which nearly USD 286.9 billion (approximately RMB 1.9 trillion) met the definition of CBI Green, rising from the 4th in 2020 to the 2nd in 2021[159] and the 1st in 2022.[160]

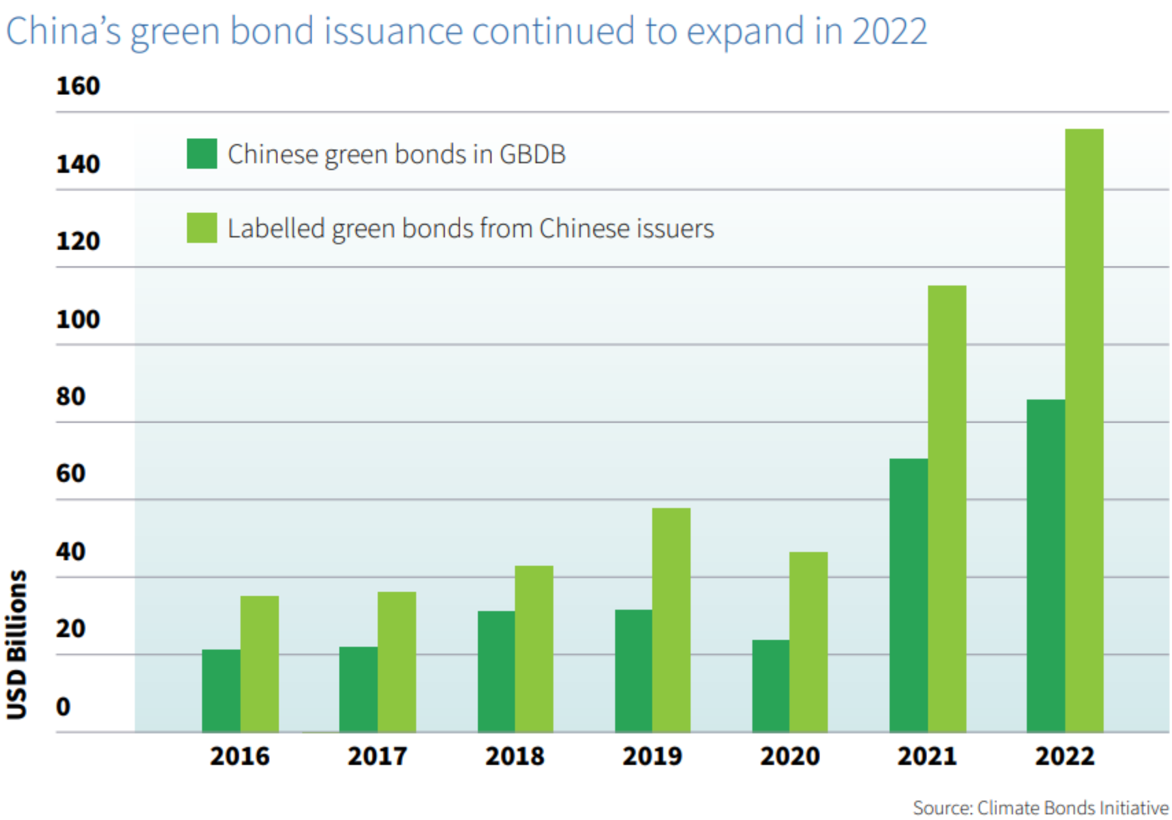
Figure 10: China is the Largest Source of Green Bonds (under the Definition of CBI Principles)



In the year of 2022, China has issued USD 155 billion (RMB 1 trillion) of labelled green bonds in the onshore and offshore markets, representing a 35% year over year increase, of which USD 85.4 billion (RMB 575.2 billion), as recorded by the Climate Bonds Green Bond Database (the "GBDB"), met the definition of CBI Green.[161] That being said, labelled green bonds account for only approximately 1.5% of the overall bond market in China, with significant room for growth.[162]

[159] China Green Bond Market Report 2021 (《中国绿色债券市场报告 2021》) co-published by the CBI and China Central Depository & Clearing Research Centre ("CCDC Research"), at 4. Please refer to CBI's website for more details: https://www.climatebonds.net/files/reports/cbi_china_sotm_2021_0.pdf.
[160] China Sustainable Debt State of the Market Report 2022 (《中国可持续债券市场报告 2022》) co-published by the CBI, the CCDC Research and CIB Economic Research and Consulting Co., Ltd., at 3 and 5. Please refer to CBI's website for more details: https://www.climatebonds.net/files/reports/cbi_china_sotm_22_en.pdf.
[161] CBI Report 2022, at 3.
[162] CBI Report 2022, at 4.

Figure 11: Chinese Green Bond Continued to Expand in 2022



1b. Green Credit

By the end of 2022, the balance of green loans in domestic and foreign currencies totalled RMB 22.03 trillion, representing a 5.5% increase from last year and higher than the growth rate of all the other loans by 28.1%. The loans lent to projects with direct and indirect carbon reduction effects are RMB 8.62 and RMB 6.08 trillion respectively, collectively accounting for 66.7% of green loans.[163]

In terms of the use of the loans, the balance of loans for the infrastructure green upgrade industry, the clean energy industry, and the energy conservation and environmental protection industry is RMB 9.82, RMB 5.68 and RMB 3.08 trillion respectively, representing a 32.8%, 34.9% and 59.1% increase year-on-year. By industry, the balance of green loans for the electricity, thermal power, gas and water production and supply industries is RMB5.62 trillion, representing a 27.4% increase year-on-year; the balance of green loans for the transport, warehousing and postal industries is RMB 4.58 trillion, representing a 10.8% increase year-on-year.[164]

[163] Statistical Report on the Loans Orientation of Financial Institutions (2022 4th Quarter) (《2022 年四季度金融机构贷款投向统计报告》) published by the PBOC on 3 February 2023, Section 4, http://www.gov.cn/xinwen/2023-02/03/content_5739947.htm.
[164] *Id.*

2. Policy State of Play

2a. National Policies and Regulations

In December 2015, the PBOC, which regulates the inter-bank market, issued the *Announcement of the People's Bank of China [2015] No.39*, which guides the issuance of green financial bonds (the "GFBs") in the interbank bond market. As a landmark policy for the green financial market, it marks the official launch of China's GFBs market. Together with the announcement, the *Green Bond Endorsed Project Catalogue (2015 Edition)* (the "Catalogue") was issued. As the first green bond standards in China, the Catalogue has served as an important reference for issuers and intermediary institutions in the green bond market in the coming five years, and has been updated in 2021.[165]

The *Guiding Opinions on Building a Green Financial System* (the "Guiding Opinions") issued in August 2016 aimed to accelerate the progress and green transformation of economy.

In May 2020, the CPC Central Committee established a group to promote and accelerate the establishment of the "1 + N" policy system for peak carbon emission and carbon neutrality.[166]

In September 2020, President Xi Jinping put forward the target that "China aims to reach the peak of carbon dioxide emissions by 2030 and to achieve carbon neutrality by 2060" at the 75th session of the United Nations General Assembly.[167]

In February 2021, the State Council issued the *Guiding Opinions on Accelerating the Establishment and Improvement of Green, Low-carbon and Cyclic Development Economic System* to guide the development of green finance.

In May 2022, the *Notice of the General Office of the State Council on the Implementation Plan for Promoting High-quality Development of New Energy in the New Era* requires enriching green financial products and services, and exploring the inclusion of new energy projects into the support scope of the pilot program of infrastructure real estate investment trusts (REITs), and supports the inclusion of certified emission reductions of greenhouse gas of eligible new energy projects into the national carbon emission trading market.

In October 2022, the NDRC issued the *Opinions on Further Improving the Policy Environment to Strengthen Support for the Development of Private Investment*, for the purpose of exploring the implementation of environmental, social and governance (ESG) assessment of investment projects and learning from international experience.

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[165] Notice on Promulgation of the Green Bond Endorsed Project Catalogue (Edition 2021) (《关于印发<绿色债券支持项目目录（2021 年版）>的通知》) promulgated by the PBOC, the NDRC and the CSRC and effected on 1 July 2021.
[166] Xinhua News, http://www.news.cn/politics/xxjxs/2021-10/29/c_1128011295.htm.
[167] Please refer to the MOFCOM's website for more details: http://www.mofcom.gov.cn/article/i/jyjl/m/202009/20200903003397.shtml.

In March 2023, the NDRC issued the *Green Industry Guiding Catalogue (2023 Version) (Draft for Comments)* (the "2023 Consulting Paper") for public feedback.

Recommendation:

It is suggested that general policy incentives be given for financial institutions to promote green finance:

- Provide tax incentives or interest subsidies and other appropriate incentives to encourage financial institutions to actively participate in the design, issuance and investment of green financial products;

- Attract blend funds to energy conservation and low-carbon sectors.

2b. Regulatory Framework for Bond Markets

China has multiple bond markets, so the regulation differs for different markets and products. At the national level, regulators mainly include the PBOC, which regulates the inter-bank market, the CSRC, which regulates the exchange market, and the NDRC, which regulates the issuance of enterprise bonds.

Inter-bank Market

In March 2017, the NAFMII promulgated the *Business Guidelines for Green Debt Financing Instruments of Non-financial Enterprises* and their supporting forms, which for the first time clarified the various requirements for non-financial enterprises in issuing green debt financing instruments, and effectively promoted the development of green bonds in China. In the context of low-carbon development, in 2021, the NAFMII has introduced two innovative green bond types, being carbon neutral bonds[168] and sustainable development-linked bonds[169], which has broaden the scope of green bonds and are expected to attract more high-quality assets to the green bond market.

Exchange Market

In July 2021, Shanghai Stock Exchange[170] and Shenzhen Stock Exchange[171] issued announcements to revise the guidelines for bond types, specifying the new sub-varieties of green corporate bonds such

[168] Please refer to NAFMII's website for more details: https://www.nafmii.org.cn/cpxl/zwrzgj/bdffdxfcp/tsyt/202112/t20211201_94660.html.

[169] Please refer to NAFMII's website for more details: https://www.nafmii.org.cn/xhdt/202104/t20210428_197371.html.

[170] Guidelines on the Application of Review Rules for the Issuance and Listing of Corporate Bonds No. 2 -- Specific Types of Corporate Bonds (Revised 2021) (《上海证券交易所公司债券发行上市审核规则适用指引第 2 号——特定品种公司债券（2021 年修订）》) promulgated by the Shanghai Stock Exchange and effected on 13 July 2021.

[171] Business Guideline on Innovative Types of Corporate Bonds No. 1 -- Green Corporate Bonds (Revised 2021) (《深圳证券交易所公司债券创新品种业务指引第 1 号——绿色公司债券（2021 年修订）》) promulgated by Shenzhen Stock Exchange and effected on 13 July 2021.

as carbon neutral bonds and blue bonds, and optimizing the requirements for the use of raised funds and for information disclosure to ensure that funds are channeled to green and low-carbon industries.

<u>Enterprise Bonds</u>

In late 2015, the NDRC issued the *Guidelines for the Issuance of Green Bonds*, which clarified the review requirements for green enterprise bonds, and encouraged the funds raised from bonds to be invested in 12 categories of projects such as technological transformation for energy conservation and emission reduction, and green urbanization.

In February 2019, the NDRC and other six departments jointly issued China's first *Green Industry Guiding Catalogue (2019 Version)*, which serves as the main basis for local governments and authorities to define development priorities of the green industry, formulate green industry policies and guide social capital investment. As described above in section 2a, the 2023 Consulting Paper as an update of the 2019 version, has been published for public feedback.

2c. Green Bond Assessment and Certification Institutions

With the growth of green bond market, the institutions engaging in green bond assessment are also developing.

The "Green Bond Assessment and Certification Institution" refers to an institution that conducts evaluation, review, or certification procedures on whether a bond meets the relevant requirements for green bonds, publishes evaluation, review, or certification conclusion, and issues a report.[172]

In October 2017, the PBOC and the CSRC jointly issued the *Guidelines for the Assessment and Certification of Green Bonds (Interim)* (the "Circular 20"), providing for the first time for the assessment and certification of green bonds by third-party institutions. Circular 20 specifies that assessment and certification institutions shall meet the relevant qualifications and shall file a record with the Green Bond Standards Committee (the "GBSC").

In September 2021, the GBSC, as the self-regulatory and coordination mechanism for green bonds, issued the *Operating Rules for Market-oriented Appraisal of Green Bond Assessment and Certification Institutions (for Trial Implementation)* and its supporting documents (Announcement [2021] No.1 of the GBSC), clarifying for the first time in the form of self-regulatory rules the qualifications, materials and submission methods of market-oriented appraisal of green bond assessment and certification institutions.

In July 2022, the GBSC issued the *China Green Bond Principles* (the "CGBP"), which apply to green bonds issued within the territory of China (not only limited to issuance in the inter-bank market) and marks a milestone in the development of China's green bond market and convergence of China's green

[172] Article 2 of the Guidelines on Green Bond Assessment and Certification (Provisional) (《绿色债券评估认证行为指引（暂行）》) promulgated by the PBOC and the CSRC and effected on 26 October 2017.

bond standards with international standards. *China Green Bond Principles*, by reference to the *Green Bond Principles* published by the International Capital Market Association (the "ICMA"), list the use of raised funds, project evaluation and selection, management of raised funds and information disclosure during the term of green bonds as four core elements, covering two periods of time before and after the issuance.

In October 2022, the *Official Publication of the List of Assessment and Certification Institutions for Green Debt Financing Instruments* was officially issued.[173]

2d. Regulatory Framework for Green Credit

In May 2016, the CSRC issued the *Regulatory Q&A on Asset Securitization (Part I)*, clarifying that projects relating to the green and environmental protection industry are encouraged to finance and develop through asset securitization.[174]

In July 2021, the PBOC issued the *Plan on Evaluating Green Finance for Banking Financial Institutions*, which conducts green finance evaluations on 24 major banking financial institutions and local banking financial institutions on a quarterly basis.

In November 2021, the PBOC launched the structural monetary policy tool known as the "supporting tools for carbon emission reduction", under which national financial institutions will be granted support tools for the time being,[175] i.e., the financial institutions will obtain low-cost funds from the PBOC to grant loans to the targeted enterprises.

Through the direct mechanism of "lending first, borrowing second", the PBOC provides financial support based on 60% of the principal of qualified carbon emission reduction loans granted by financial institutions to relevant enterprises in key areas of carbon emission reduction at the interest rate of 1.75%.[176]

In June 2022, the CBIRC issued the *Guidelines for Green Finance in Banking and Insurance Sectors*, specifying "promoting green finance from a strategic perspective", and provides guidance for banks to set green finance development goals, build green finance development paths, and carry out businesses in the green financial market.

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[173] The Official Publication of the List of Assessment and Certification Institutions for Green Debt Financing Instruments (《绿色债务融资工具评估认证机构公示名单》) promulgated by the NAFMII and effected on 31 October 2022.

[174] Regulatory Q&A on Asset Securitization (《资产证券化监管回答（一）》) published by the CSRC on 13 May 2016. Please refer to CSRC's website for more details: http://www.csrc.gov.cn/csrc/c100107/c1447212/content.shtml.

[175] The Supporting Tools for Carbon Emission Reduction launched by the PBOC (《人民银行推出碳减排支持工具》) published on 8 November 2021. Please refer to the Central People's Government's website for more details: http://www.gov.cn/xinwen/2021-11/08/content_5649848.htm.

[176] Q&A of Relevant Responsible Person in charge of the PBOC and Reporters on the Supporting Tools for Carbon Emission Reduction (《人民银行有关负责人就碳减排支持工具答记者问》) published by the PBOC on 8 November 2021, Section 2.

Recommendation:

Further expand the PBOC's carbon emission reduction supporting tools, for international financial institutions

2e. Sustainability-related Disclosures

China's framework for sustainability disclosure has been developing and is expected to further align with international practice, especially on the mandatory disclosure.

In May 2022, the CSRC issued the *Work Guidelines for the Management of Investor Relations of Listed Companies*, specifying that the companies' environmental, social and governance information should be the main content of the communications between listed companies and investors in respect of the management of investor relations.

Also in May 2022, the SASAC issued a work plan, promoting the high-quality development of state-owned enterprises directly under the central government.

As described in the above sub-section 2d, in June 2022, the CBIRC issued the *Guidelines for Green Finance in Banking and Insurance Sectors* to direct banks and insurers to incorporate ESG into their risk management systems and strengthen ESG information disclosure. The guidelines took effect on 1st June and requires the aforesaid institutions to establish internal green finance management systems and procedures within one year.

In February 2023, Shanghai Stock Exchange and Shenzhen Stock Exchange respectively issued their *Listing Rules of Listed Companies (February 2023 Revision)*, requiring listed companies to actively implement sustainable development, proactively undertake social responsibilities, maintain social public interests, and pay attention to environmental protection. Listed companies should prepare and disclose social responsibility reports and other documents as required. In the event of violations of social responsibilities or other major events, listed companies should fully evaluate the potential impact and make a timely disclosure, stating the reasons and solutions.

Recommendation:

We encourage policymakers to continue to embed sustainability across the financial system and global economy and support capital market development and the transition to a green economy. In this context, we propose the below recommendations for policymakers to consider:

- Introduce domestic disclosure frameworks economy-wide by 2025, aligning with global standards. As a minimum, these frameworks should cover climate reporting in line with the Taskforce on Climate-Related Financial Disclosures' (the "TCFD") 2021 recommendations and the International Sustainability Standards Board's (the "ISSB") climate reporting standards. This will reduce fragmentation and avoid inconsistent or conflicting requirements between jurisdictions and for international financial institutions.

- We encourage regulators to consider adopting a "phased-in" approach to disclosure reporting – this recognizes the need for initial flexibility and allows time for methodologies to mature, for greater standardization to be developed and data to become more readily available.

- We are supportive of the option to leverage parent level disclosures to meet local requirements.

- In terms of transition plans, we support alignment of transition plan under the TCFD and ISSB frameworks; this is a global standard which most jurisdictions are familiar reporting against, rather than imposing new requirements.

2f. Carbon Market

In September 2020, President Xi Jinping announced the "double-carbon" goal at the 75th United Nations General Assembly. In May 2020, the "1 + N" policy system for peak carbon emission and carbon neutrality was established.[177] In September and October 2021, the *Opinions on Completely, Accurately and Comprehensively Implementing the New Development Concepts and Effectively Carrying out the Work of Peak Carbon Emission and Carbon Neutrality* (the "Opinions")[178] and the *Action Plan for Peak Carbon Emission by 2030*[179] were promulgated. Thereafter, implementing plans for peak carbon emission in the energy, industry, transportation, urban and rural construction and other sectors were introduced one after another.

Currently, China has a total of 9 local pilot carbon emission right trading platforms in Beijing, Tianjin, Shanghai, Chongqing, Hubei, Guangzhou, Shenzhen, Sichuan and Fujian, which have jointly launched the "common carbon inclusion mechanism". The platforms mainly focus on spot trading. For the details of the platforms, please refer to Annex 6.

China's national carbon trading market has been under development since 2013, and was officially launched in July 2021 in Beijing, Shanghai and Wuhan simultaneously.[180] The trading center of the national carbon market is located in Shanghai, and the carbon emission allowances registration system is based in Wuhan. Enterprises register accounts in Wuhan and carry out trading in Shanghai. Both function as the pillar of the national carbon trading system. Beijing has proposed to undertake the

[177] Please refer to Annex 5 for the details of the "1+N" system.

[178] The Opinions on Completely, Accurately and Comprehensively Implementing the New Development Concepts and Effectively Carrying out the Work of Peak Carbon Emission and Carbon Neutrality (《中共中央 国务院关于完整准确全面贯彻新发展理念做好碳达峰碳中和工作的意见》) promulgated by the State Council and effected on 22 September 2021.

[179] The Action Plan for Peak Carbon Emission by 2030 (《2030 年前碳达峰行动方案》) promulgated by the State Council and effected on 24 October 2021.

[180] Please refer to the Central People's Government's website for more details: http://www.gov.cn/xinwen/2022-07/22/content_5702238.htm

construction of a national management and trading center for voluntary emission reduction of greenhouse gases, which is an important complement to the national carbon market.

China is gradually promoting the development of the national carbon market in phases on the basis of fully learning from the experience of the pilot local carbon markets and starting with the power industry. There are two types of carbon market products – carbon emission allowances ("CEA") and voluntary China Certified Emission Reduction ("CCER").

Since the launch of the online trading in the national carbon market in July 2021, the focus of China's carbon market work has shifted from local pilot demonstration to the development and improvement of the national unified carbon market. According to the *Administrative Measures for Carbon Emission Right Trading (for Trial Implementation)*, key emitters that have been included in the national carbon market will no longer participate in local carbon markets, to ensure the unity, integrity and fairness of the national carbon market.[181] According to the *Plan for Building the National Carbon Emission Right Trading Market (Power Industry)*, the pilot carbon markets will gradually transit to the national carbon market while the exploration of new paths for the national carbon market will continue.[182]

In 2022, the construction of the national carbon market has experienced a steady growth. Compared with 2021, the national carbon market shows a trend of declining volume and increasing price in 2022. The trading volume and value of CEA are 50.89 million tons and RMB2.8 billion respectively, and CEA's closing price and average trading price in the year are RMB55 yuan/ton and 55.3 yuan/ton respectively.[183]

In 2022, a total of 7.959 million tons of CCER were traded on the market, representing a decrease of 95.46% year-on-year. The monthly and geographical distribution of the trading volume were also relatively concentrated. Fudan Carbon Price Index shows that the price range of CCER increased from around RMB35 yuan/ton at the beginning of 2022 to around RMB60 yuan/ton by the end of the year.[184]

In March 2023, the MEE issued the *Letter regarding Open Solicitation of Methodological Proposals for Greenhouse Gas Voluntary Emission Reductions Projects*, which seems to indicate the restart of the CCER filing.[185] It is expected that the construction of a national CCER market will be advanced.

[181] Article 13 of the Administrative Measures for Carbon Emission Permits Trading (for Trial Implementation) (《碳排放权交易管理办法（试行）》) promulgated by the MEE and effected on 1 February 2021.
[182] Article 7 of the Plan for Building the National Carbon Emission Permit Trading Market (Power Generation Industry) (《全国碳排放权交易市场建设方案（发电行业）》) promulgated by the NDRC and effected on 18 December 2017.
[183] Guo Minping et al., China Carbon Market Annual Report 2022 (《2022 中国碳市场年报》), Section 1, 14 February 2023. Please refer to IIGF's website for more details: https://iigf.cufe.edu.cn/info/1012/6391.htm.
[184] China Carbon Market Annual Report 2022, Section 1.
[185] The Letter regarding Open Solicitation of Methodological Proposals for Greenhouse Gas Voluntary Emission Reductions Projects (《关于公开征集温室气体自愿减排项目方法学建议的函》) published by the MEE on 30 March 2023.

Separately, Hainan International Carbon Emissions Trading Center ("Hainan ETS") was established in July 2022, and the first cross-border carbon transaction was successfully completed on 30 December 2022, with the Verified Carbon Units (VCUs) under the Verified Carbon Standard (VCS) being the trading products. Hainan ETS is expected to become an offshore center of trade and finance to streamline the flow of commodities, capital and talents, and aims to connect China's national trading scheme with the global market.

Recommendation:

We encourage the development of the compliance carbon markets in China as the key driver for carbon pricing and support the further integration of these markets, the exploration of a futures market and participation of foreign financial institutions to assist in building liquidity, hedging and carbon pricing (as well as other price discovery mechanisms such as auctions).

We encourage the development of voluntary carbon markets in China to be aligned with international standards, such as those made by the Integrity Council on Voluntary Carbon Markets ("ICVCM"), to reduce the risk of fragmented markets and to facilitate international flow of capital. The ICVCM standards largely represent industry best practice on carbon credit quality and will help to ensure that carbon credits are properly verified, transparently reported, and accurately reflect the emissions reductions they claim to represent.

We support the development of a connect scheme between mainland exchanges and HK Core Climate - an initial step in connecting with international markets.

Separately, while we understand the MEE has been facilitating the legislation of the *Interim Administrative Regulations on the Trading of Carbon Emission Rights*, it would be beneficial to speed up the legislation for carbon market to ensure that liquidity is maintained in case of any events of default.

3. China's Role on Global Sustainable Finance Stage

3a. Expanding the International Cooperation Space for Green Finance

On 4 November 2021, during the United Nations Climate Change Conference (COP26), the International Platform on Sustainable Finance released the *Common Ground Taxonomy - Climate Change Mitigation* (the "Taxonomy"). The Taxonomy, based on *China's Greed Bond Endorsed Project Catalogue* and the *EU's Taxonomy: Complementary Climate Delegated Act*, covers six sectors, namely, agriculture, forestry, animal husbandry and fishery, manufacturing, energy, water supply and solid waste, construction and transportation energy storage, and is conducive to promoting China-EU cooperation in green investment and financing, guiding cross-border investment and financing, and reducing the cost of green certification. The Taxonomy, based on a detailed comparison of standards between China and the EU, represents the close cooperation between China and the EU in harmonizing green standards.

At the bilateral level, China and the United Kingdom have established a UK-China Green Finance Centre to organize financial institutions in the two countries to carry out a pilot project for environmental information disclosure. The Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) is the main channel for promoting cooperation on green finance between China and Germany. It has hosted several round-table meetings and provided technical support to China-EU low-carbon eco-city cooperation projects. On April 21, 2023, the Monetary Authority of Singapore and the PBOC announced the establishment of the China-Singapore Green Finance Taskforce, which will deepen bilateral cooperation in green and transition finance between Singapore and China and facilitate greater public-private sector collaboration to better meet Asia's needs as it transits to a low carbon future.[186]

3b. Bay Area

In 2019, the State Council issued the *Outline of the Plan for the Development of Guangdong-Hong Kong-Macau Greater Bay Area* to develop green finance in the Greater Bay Area (GBA).[187] Green finance has become an important part of the financial reform and innovative development of the GBA. In 2020, China's strategic goals of peak carbon emission and carbon neutrality has brought more development opportunities to the green finance industry of the Greater Bay Area. Green finance policies in terms of development planning, industry standards, incentive mechanisms, and implementation paths have been launched to guide and regulate the establishment of green finance system, but these policies are mainly concentrated in Hong Kong, Guangzhou and Shenzhen, while the policies system in other GBA areas are yet to be developed.[188]

Hong Kong is a key sustainable finance market in Asia. In April 2020, SFC issued the *Circular to Management Companies of SFC-Authorized Unit Trusts and Mutual Funds – Green or ESG Funds*, helping to enhance the information transparency for green financial products.[189] In 2021, approximately one third of green and sustainable bonds in Asia were financed and issued in Hong Kong. In addition, the Hong Kong government initiated its Pilot Green and Sustainable Finance Capacity Building Support Scheme in December 2022, which aims to support talent development in the industry by providing subsidies to market practitioners as well as prospective practitioners in taking up relevant training and acquiring relevant professional qualifications.[190] The HKMA also sent a

[186] Please refer to MAS's website for more details: https://www.mas.gov.sg/news/media-releases/2023/singapore-and-china-establish-green-finance-taskforce.

[187] The Outline of the Plan for the Development of Guangdong-Hong Kong-Macau Greater Bay Area (《粤港澳大湾区发展规划纲要》) promulgated by the State Council and effected on 18 February 2019.

[188] Cheng Lili, Ou Weixiang, Enhancing the Driving Force of Green Finance in the Greater Bay Area (《提升大湾区绿色金融驱动力》), Chinese Finance, Vol.23.

[189] Circular to Management Companies of SFC-Authorized Unit Trusts and Mutual Funds – ESG Funds (《致证监会认可单位信托及互惠基金的管理公司的通函 — 环境、社会及管治基金》) promulgated by the HKSFC and effected on 29 June 2021, https://sc.sfc.hk/TuniS/apps.sfc.hk/edistributionWeb/api/circular/openFile?lang=TC&refNo=21EC27.

[190] Please refer to HKMA's website for more details: https://www2.hkma.org.hk/general/gsf/#:~:text=The%20Pilot%20Green%20and%20Sustainable%20Finance%

Circular (and annex) on Due Diligence Processes for Green and Sustainable Products to authorized institutions in December 2022, setting out good practice guidance on due diligence and other processes relating to the management of green and sustainable products which resulted from a round of thematic examinations.[191]

Macao's green bond market is at the initial stage. In 2019, the Macao branch of Bank of China issued its first green bond of CNY7 billion[192], and Zhuhai Da Heng Qin Investment Co., Ltd. issued senior green bonds of CNY800 million, which were listed in both Hong Kong and Macao.[193]

The complete industrial system in the Pearl River Delta, the mature capital market in Hong Kong and the open institutional environment in Macao provide a broad space for cooperation on green finance among the three regions. In September 2020, the Greater Bay Area Green Finance Alliance was established with the aim of promoting cross-border coordination and cooperation in the GBA and supporting the development of green finance.[194]

3c. One Belt and One Road

Since President Xi Jinping put forward the "One Belt, One Road" initiative in 2013, China has signed over 200 cooperation documents on the "One Belt, One Road" initiative with 151 countries and 32 international organizations and established over 90 bilateral cooperation mechanisms[195].

In 2017, the Industrial and Commercial Bank of China ("ICBC") initiated and established the “Belt and Road Bankers” Roundtable ("BRBR"), calling on financial institutions from various countries to participate and discuss strategies for green development of the Belt and Road Initiative. With the promotion of the BRBR, the Belt and Road Green Finance (Investment) Index was launched in conjunction with the Oxford Economics.

Recommendation:

Encourage further development of the Taxonomy to complete the remaining sectors comparison – this could serve as a template for further comparison between regional taxonomies and helpful on the journey to interoperability/equivalence.

20Capacity%20Building,up%20relevant%20training%20and%20acquiring%20relevant%20professional%20qualifications.

191 Please refer to HKMA’s website for more details: https://www.hkma.gov.hk/media/eng/doc/key-information/guidelines-and-circular/2022/20221209e3.pdf.

192 Please refer to BOC’s website for more details: https://www.boc.cn/aboutboc/ab8/201910/t20191012_16785448.html.

193 Please refer to Xinhuanet’s website for more details: http://m.xinhuanet.com/gd/2019-11/22/c_1125263323.htm.

194 Cheng Lili, Ou Weixiang, Enhancing the Driving Force of Green Finance in the Greater Bay Area, Chinese Finance, Vol.23.

195 Please refer to the website of “Belt and Road Portal” for more details: https://www.yidaiyilu.gov.cn/xwzx/roll/77298.htm.

Similar to what happens in other international markets, we would welcome ongoing engagement and policy discussions between the Chinese financial policymakers and the industry – in both formal and informal dialogue. This will enable Chinese policymakers to receive candid feedback from the industry and an understanding of what works in international markets. This will help Chinese regulators to leverage international best practices.

We would also welcome the Chinese authorities support for capacity building, as addressing climate change is an industry wide challenge. It's a learning curve that we all need to ride together and time is of the essence.

4. Sustainability in Asset Management

The AMAC has been evaluating green and sustainable investments since 2017 through various studies on the ESG evaluation system of listed companies. In November 2018, the AMAC issued its *Interim Green Investment Guidelines* to provide suggestions and guidance for fund managers to improve environmental performance, promote development of green industries and reduce environmental risk.[196] Between 2019 and 2022, the annual green investment self-assessment survey was conducted each year. As of July 2021, over 50% of the surveyed FMCs have incorporated green investment into company strategy, 87% have carried out green research, and 72% have issued green investment products, while only 17% of the PFMs surveyed have incorporated green investment into their company strategy, 74% have conducted green research but only 3% have issued green investment products.[197]

In April 2022, the China Enterprise Reform and Development Society ("CERDS"), together with various research institutions and leading companies in China, published the *Guidance for Enterprise ESG Disclosure*, providing a non-binding framework for ESG disclosure.[198] Mandatory disclosure is expected following the issuance of international sustainability standards in June 2023 which China has been involved in developing. FMCs currently wishing to apply for establishing an ESG-themed fund should comply with the *Administrative Measures for Public Securities Investment Funds' Operations* which generally sets out criteria for public funds, such as those requiring the name and prospectus to accurately reflect the fund features and not to be misleading, and requiring 80% or more of the non-cash assets to be invested in accordance with the investment direction in its name (if available).[199]

Broader enhancements to corporate governance and shareholder engagement by listed issuers, supporting the sustainable investing and stewardship obligations of asset managers, are being

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[196] The Interim Green Investment Guidelines (《绿色投资指引（试行）》) promulgated by the AMAC and effected on 10 November 2018.

[197] AMAC's Fund Manager Green Investment Self-Evaluation Report (2022) (《基金管理人绿色投资自评估报告 (2022) 》), published in December 2022, https://www.amac.org.cn/aboutassociation/gyxh_xhdt/xhdt_xhyw/202212/P020221213341035900020.pdf.

[198] Guidance for Enterprises ESG Disclosure (《企业 ESG 披露指南》) promulgated by the CERDS and effected on 1 June 2022.

[199] Administrative Measures for Public Securities Investment Funds' Operations (《公开募集证券投资基金运作管理办法》) promulgated by the CSRC and effected on 8 August 2014.

progressively introduced by the CSRC. In April 2022, the CSRC issued the *Enhanced Investment Relations Management Guidelines* formalising the roles and responsibilities of the investment relations function.[200] In May 2023, the CSRC proposed the *Administrative Measures for Listed Companies' Independent Directors* which clarifies the responsibilities and accountability of independent directors.[201]

Recommendation:

Observe regional and international sustainability developments.

Focus on non-prescriptive disclosure rules which can protect the interests of end investors but without restricting the evolving dynamics of the nascent sustainable investment market.

Recommendations for Sustainable Finance
In respect of **National Policies and Regulations**, it is suggested that general policy incentives be given for financial institutions to promote green finance: 1. Provide tax incentives or interest subsidies and other appropriate incentives to encourage financial institutions to actively participate in the design, issuance and investment of green financial products. 2. Attract blend funds to energy conservation and low-carbon sectors. In respect of **Regulatory Framework for Green Credit:** 3. Further expand the PBOC's carbon emission reduction supporting tools, for international financial institutions. In respect of **Sustainability-related Disclosures:** 4. We encourage policymakers to continue to embed sustainability across the financial system and global economy and support capital market development and the transition to a green economy. In this context, we propose the below recommendations for policymakers to consider: 5. Introduce domestic disclosure frameworks economy-wide by 2025, aligning with global standards. As a minimum, these frameworks should cover climate reporting in line with the Taskforce on Climate-Related Financial Disclosures' (TCFD) 2021 recommendations and the ISSB climate reporting standards. This will reduce fragmentation and avoid inconsistent or conflicting requirements between jurisdictions and for international financial institutions. 6. We encourage regulators to consider adopting a "phased-in" approach to disclosure reporting – this recognizes the need for initial flexibility and allows time for methodologies to mature, for greater standardization to be developed and data to become more readily available. 7. We are supportive of the option to leverage parent level disclosures to meet local requirements.

[200] Work Guidelines for the Investor Relations Management of Listed Companies (《上市公司投资者关系管理工作指引》) promulgated by the CSRC and effected on 15 May 2022.
[201] Administrative Measures for Listed Companies' Independent Directors (Draft for Comment) (《上市公司独立董事管理办法（征求意见稿）》) promulgated by the CSRC on 14 April 2023.

8. In terms of transition plans, we support alignment of transition plan under the TCFD and ISSB frameworks, which is a global standard which most jurisdictions are familiar reporting against, rather than imposing new requirements.

In respect of **Carbon Market:**

9. We encourage the development of the compliance carbon markets in China as the key driver for carbon pricing and support the further integration of these markets, the exploration of a futures market and participation of foreign financial institutions to assist in building liquidity, hedging and carbon pricing (as well as other price discovery mechanisms such as auctions).
10. We encourage the development of voluntary carbon markets in China to be aligned with international standards, such as Integrity Council on Voluntary Carbon Markets (ICVCM) to reduce the risk of fragmented markets and to facilitate international flow of capital. The ICVCM standards largely represent industry best practice on carbon credit quality and will help to ensure that carbon credits are properly verified, transparently reported, and accurately reflect the emissions reductions they claim to represent.
11. We support the development of a connect scheme between mainland exchanges and HK Core Climate - an initial step in connecting with international markets.

In respect of **China's Role on Global Sustainable Finance Stage:**

12. Encourage further development of the Taxonomy to complete the remaining sectors comparison – this could serve as a template for further comparison between regional taxonomies and be helpful on the journey to interoperability/equivalence.
13. Similar to what happens in other international markets, we would welcome ongoing engagement and policy discussions between the Chinese financial policymakers and the industry – in both formal and informal dialogue. This will enable Chinese policymakers to receive candid feedback from the industry and an understanding of what works in international markets. This will help Chinese regulators to leverage international best practices.
14. We would also welcome the Chinese authorities support for capacity building, as addressing climate change is an industry wide challenge. It's a learning curve that we all need to ride together and time is of the essence.

In respect of **Sustainability in Asset Management**:

15. Observe regional and international sustainability developments.
16. Focus on non-prescriptive disclosure rules which can protect the interests of end investors but without restricting the evolving dynamics of the nascent sustainable investment market.

L. Market Infrastructure

1. Payments

1a. Cross-border Payments and Settlement Risk

RMB is cleared domestically through the China National Advanced Payment System (CNAPS), a central bank operated RMB clearing system which provides real-time gross and net settlement[202]. To have direct access to CNAPS a bank is required to have a settlement account at a branch of China's central bank.

One reason behind the disproportionately small use of the RMB as a settlement currency was the inadequacy of the infrastructure supporting cross-border RMB payments, which were made via a patchwork of clearing hubs and correspondent banks. Payments were hindered by complicated routing procedures, the need to maintain multiple foreign correspondent accounts, liquidity shortages in some offshore RMB clearing centres, different hours of operation between clearing centres and a lack of common standards between international and Chinese domestic payment systems.

Today, all major RMB clearing centres are serviced by a dedicated RMB clearing bank that facilitates RMB payment and settlement of transactions between market participants.

In 2015, China launched the Cross-border Interbank Payment System (CIPS)[203], a cross-border RMB payment system, to address these issues. CIPS is a real-time gross settlement system that provides one-point entry for participants and a central location for clearing RMB payments by allowing both direct access for onshore banks and indirect access for onshore and offshore banks and has enabled faster payment processing and a reduction in cross-border payment costs. As a result, CIPS will play a critical role in RMB's growth as an international payments currency.

Because payment messages are now supported in both English and Chinese and CIPS operates the ISO20022 messaging standard and SWIFT bank identifier codes, cross-border payments made through CIPS have been able to achieve higher straight-through processing rates.

As of April 2023, CIPS had 80 direct participants[204] and 1,357 indirect participants[205] and operates 5×24 hours + 4 hours.

[202] Introduction to the CNAPS made by the PBOC, http://www.pbc.gov.cn/zhifujiesuansi/128525/128527/2847564/index.html.
[203] Introduction to CIPS, http://www.cips.com.cn/cips/gywm/cipsxt/xtjj/index.html.
[204] The list of direct participants, http://www.cips.com.cn/cips/gywm/cipsxt/zjcyzmd/index.html.
[205] CIPS System Participant Announcement (No. 84), http://www.cips.com.cn/cips/ywfw/cyzgg/59491/index.html.

CIPS adopts a hybrid settlement mechanism combining Real-Time Gross Settlement (RTGS) and Deferred Net Settlement (DNS) to optimize liquidity arrangements and meet diversified needs of CIPS participants. It offers a vast range of settlement and clearing services, including RMB payment for DVP, onshore PVP in RMB and foreign currencies, settlement of centralized clearing of CCP, and RMB settlement of other cross-border transactions[206].

Besides RMB business, CIPS started to provide the HKD payment and clearing services, which made it easier for mainland investors to invest in Hong Kong's financial market.

In September 2021, Southbound Trading on Bond Connect was officially launched. CIPS acted as the dedicated settlement channel, working together with CFETS, SHCH, and other FMIs to integrate bond trading, depository and settlement services.

To further grow the use of the RMB as an international payment currency, the channel selection or rationalisation increasingly becomes important and imperative for global banks to consider. Connecting to CIPS as the direct participant will bring not only the efficiency gain to a bank's RMB payment operation, but also reinforces a bank's profile as a RMB transaction bank. However there are a number of factors to consider when considering the business case, such as the distribution of global RMB liquidity, the TCO of network access, the consistency with international market standards, the clearing process as well as the SLA.

As of 20 March 2023, along with the global correspondent payment message standards starting to migrate from MT to ISO20022 CBPR+, the RMB cross-border payment today is able to enjoy the end-to-end consistent standards which contains the rich and structured payment data needed for RMB regulatory reporting and sanction screening. The mapping report between CIPS ISO20022 message and Swift CBPR+ has been published by CIPS, and the ISO20022 CBPR+ messaging practice guideline for China market has been published jointly by Swift and its onshore banking community. It is expected that ISO20022 standards – being used as common for both RMB international inter-bank and Chinese domestic payment systems – will help further remove the potential frictions of RMB cross-border payment and propel its user experience to the next level.

1b. CNH – PVP/Settlement Risk

Although the physical settlement infrastructure for CNH FX instructions has evolved considerably, there are aspects where it does not meet international best practice standards:

- Settlement of CNH FX transactions is completed predominantly on a non-PVP basis. This exposes participants to principal risk (or Herstatt risk), the risk of a loss of the full value of the transactions. In line with the Basel Committee on Banking Supervision's Supervisory Guidance on managing FX

[206] Introduction to CIPS, http://www.cips.com.cn/cips/gywm/cipsxt/xtjj/index.html.

settlement risk[207] which states that, where practicable, banks should use FMIs that provide PVP settlement to eliminate principal risk when settling FX transactions.

- Settlement of RMB transactions is not provided in central bank funds in all jurisdictions or in the counter-currencies. The CPMI-IOSCO *Principles for financial market infrastructures*[208] provide specific guidance as to settlement in central bank money to limit credit and liquidity risks.

- CNH is eligible for settlement on CLSNet[209], an automated bilateral payment netting calculation service which provides participants with a legal confirmation of their net payment obligation[210]. However, bilateral settlement of CNH transactions continues to be performed on a gross or netted basis. While market participants benefit from reduced credit exposures and improved liquidity under CLSNet, they are unable to realise the significant liquidity benefits of multilateral netting that are available to the 18 currencies eligible[211] for settlement by CLSSettlement[212].

As demand for CNH settlement continues to grow in line with the growth of FX volumes, it will increase pressure on liquidity and counterparty limits and on assuring risk mitigation for the notional amounts to be settled. For internationally active banks, holding separate pools of liquidity in various clearing centres makes it difficult to manage and makes liquidity at times expensive to obtain and unpredictable in terms of time of receipt. CNH is the only top-10 currency, as noted by the BIS, ineligible for CLSSettlement which impacts its ability to become a truly international currency.

Recommendation:

We recommend that the PBOC allow the development of CNH PVP risk mitigation infrastructure for the protection from the loss of principal on payments for all market participants, both the Mainland and international entities. Introduction of PVP risk mitigation is a priority of central banks globally and supports adherence to both the Chinese[213] (Article 146) and Global[214] (Principles 35 and 50) FX Code.

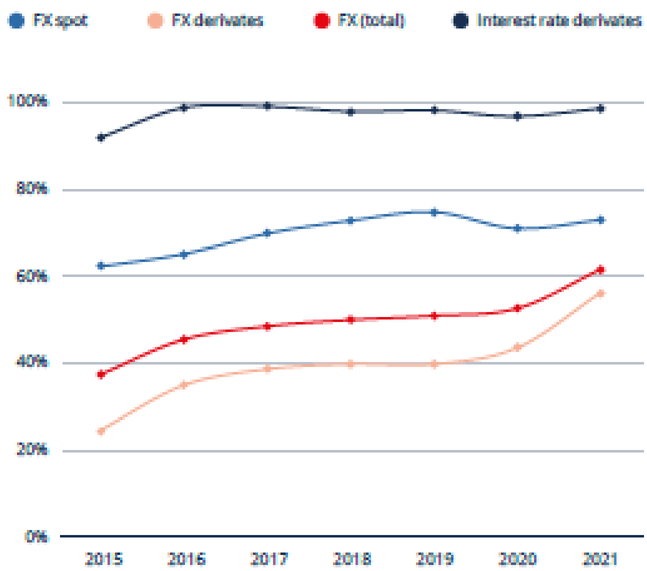
2. Clearing

[207] Supervisory guidance for managing risks associated with the settlement of foreign exchange transactions, https://www.bis.org/publ/bcbs241.pdf.
[208] Principles for financial market infrastructures, https://www.bis.org/cpmi/publ/d101a.pdf.
[209] CLS' introductory video, https://www.cls-group.com/news/publications/clsnet-how-it-works/.
[210] The introduction to the CLSNet, https://www.cls-group.com/products/processing/clsnet/.
[211] CLS's eligible currencies list, https://www.cls-group.com/products/settlement/clssettlement/currencies/.
[212] CLS's home page, https://www.cls-group.com/.
[213] Article 146 of China FX Code provides "Market Participants should reduce their Settlement Risk as much as practicable, including by settling FX transactions through services that provide PVP settlement where available."
[214] Principles 35 and 50 of Global FX Code respectively provide "Market Participants should reduce their Settlement Risk as much as practicable, including by settling FX transactions through services that provide PVP settlement where available" and "Market Participants should properly measure, monitor and control their Settlement Risk equivalently to other counterparty credit exposures of similar size and duration".

Currently, certain CNY interest rate swaps are subject to mandatory clearing while certain interbank USD/CNY FX trades are required to be cleared and settled via the SHCH. SHCH currently offers clearing services for bonds, interest rate derivatives, FX spot and derivatives, credit derivatives and commodity derivatives[215].

In 2021, the cleared volume of FX spot and derivative transactions accounted for approximately 62% of the total onshore interbank volume; for interest rate derivatives the percentage of cleared volume was 99%.

Figure 12: Proportion of Central Cleared FX Spot and Derivatives and Interest Rate Derivatives in China's OTC Financial Markets



Source: SHCH

[215] Introduction to SHCH, https://www.shclearing.com.cn/gywm/gsjs/.

Figure 13: Break-down of SHCH OTC Clearing Market

Source: SHCH

The implementation of Swap Connect which will enable offshore market participants to trade CNY interest rate swaps with onshore counterparties that clear through a bilateral arrangement between the Hong Kong Exchange's OTC Clear and the SHCH will be particularly important in the context of being able to hedge interest rate risk arising from bond holdings via CIBM and Bond Connect as well as the QFI program.

i. Close out Netting

In most jurisdictions, banks and certain regulated financial institutions (together referred to as "Covered Financial Entities") are subject to regulatory capital rules as published by the Basel Committee on Banking Supervision (the "Basel Committee"). Consequently, these Covered Financial Entities are required to hold capital against their exposures to a central clearing counterparty (CCP).

For instance, under Article 296(2)(a)[216] of the EU Capital Requirements Regulation ("EU CRR") states that "the institution has concluded a contractual netting agreement with its counterparty which creates a single legal obligation, covering all include transactions, such that, in the event of default by the counterparty it would be entitled to receive or obliged to pay only the net sum of the positive and negative mark-to-market values of included individual transactions". For a CCP, the agreement between a clearing member and the CCP constitutes a contractual netting agreement. This means the CCP's clearing rules, guidelines or some other written agreement between the CCP and the clearing member must provide for close-out netting upon occurrence of an event of default by the CCP.

[216] Art 296 of EU CRR, https://www.eba.europa.eu/regulation-and-policy/single-rulebook/interactive-single-rulebook/1894.

We welcome efforts by SHCH to amend its clearing guidelines to address the methodology used to determine the close-out amount and to introduce a failure to pay/deliver event of default in respect of SHCH itself, which would enable the relevant non-defaulting clearing member to initiate close-out netting against SHCH.

Recommendation:

We would also recommend that SHCH update its legal opinion after such amendments have been made to its close out methodology set out in its revised clearing guidelines.

ii. QCCP Status of SHCH

The G20 derivatives regulations, introduced in the aftermath of the 2008 global financial crisis, require centralised clearing houses (CCPs) in jurisdictions operating mandatory clearing regimes to be recognised as a Qualified CCP (QCCP). Failure to be recognised by other jurisdictions as a QCCP could limit the participation of entities from those jurisdictions in the domestic OTC derivatives market. According to the SHCH website[217], as of 16 March 2023, the CCP has 93 Clearing Members, of which 19 are locally incorporated subsidiaries and 2 are branches of international banks domiciled in mainly the US, UK, Europe, Singapore, Japan and Australia.

In Europe, the European Securities and Markets Authority (ESMA) recognised the SHCH as a QCCP on 27 September 2022 after the PBOC and ESMA signed a joint Memorandum of Understanding[218] and shortly after the European Commission announced that it had granted equivalence to the regulatory framework of the PBOC for CCPs that are authorised to clear OTC derivatives in the interbank market and supervised by the PBOC.

In the US, there is a requirement under the Dodd Frank Act for third-country CCPs to either apply for recognition as, or exemption from, being a Derivative Clearing Organisation (DCO)[219]. Failure to do either will mean that US persons – US banks and their overseas branches but not their overseas incorporated subsidiaries – clearing on a third-country CCP will be in breach of Section 5b of the Commodity Exchange Act as modified by the Dodd Frank Act. The Commodities Futures Clearing Commission (CFTC) has, since May 2016, granted an annual no-action relief to the SHCH allowing it to temporarily clear swaps subject to the mandatory clearing obligation in China for the proprietary trades of US persons that are clearing members of the SHCH. However, in its last notification of no-

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[217] The member list of SHCH, https://www.shclearing.com.cn/hyfw/qshy/qshymd/ptqshy/201512/t20151202_118618.html.

[218] Memorandum of Understanding between the ESMA and the PBOC, https://www.esma.europa.eu/sites/default/files/library/esma-pboc_china_mou.pdf.

[219] SEC. 725. of the Dodd Frank Act, which provides "(h) EXEMPTIONS.—The Commission may exempt, conditionally or unconditionally, a derivatives clearing organization from registration under this section for the clearing of swaps…".

action relief, which expires on 31 July 2023, the CFTC stated that if it has not made a decision to approve the SHCH's application for an exemption by the expiry date, it does not plan to extend the relief and encourages any persons relying on the relief to unwind transactions as necessary[220].

3. Others

3a. Overseas FMIs

On 14 December 2022, the PBOC consulted on the draft *Measures on the Supervision and Administration of Financial Market Infrastructures* (《金融基础设施监督管理办法（征求意见稿）》, the "Consultation Measures"). The Consultation Measures are aligned with the CPMI-IOSCO *Principles for financial market infrastructures* (PFMI)[221].

These Consultation Measures stipulate regulatory requirements for systemically important FMIs in Articles 33, 37 and 38[222]. The PFMI recommend clearly defining and publicly disclosing the criteria for designation as systemically important FMIs. They specifically suggest the following criteria: (a) the number and value of transactions processed, (b) the number and type of participants, (c) the markets served, (d) the market share controlled, (e) the interconnectedness with other FMIs and other financial institutions, and (f) the available alternatives to using the FMI at short notice. We believe providing this clarity will be essential to both protect the Chinese market and provide certainty to the operators of FMIs.

The Consultation Measures introduce requirements for cross-border delivery of overseas FMIs in Article 13 and their reporting liability in Article 30. We would suggest the Consultation Measures clearly indicate that overseas FMIs will only be required to comply with Articles 13 and 30, and that the obligations apply only to the services that are being rendered to Chinese clients.

Recommendation:

We recommend developing a licensing or registration process authorizing the provision of cross-border services, with detailed requirements including scope and mechanism for reporting to ensure covered FMIs have a clear understanding of the regulatory expectations. The registration or licensing of overseas FMIs should only be required in cases where the services they provide are regularly used in the ordinary course of business by the domestic entities.

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[220] CFTC's Division of Clearing and Risk Issues No-Action Letter for Shanghai Clearing House, https://www.cftc.gov/PressRoom/PressReleases/8562-22.

[221] *Principles for financial market infrastructures*, https://www.bis.org/cpmi/info_pfmi.htm.

[222] According to the draft *Measures on the Supervision and Administration of Financial Market Infrastructures* (《金融基础设施监督管理办法（征求意见稿）》*)*, Article 33 provides the PBOC has the power to inspect the FMI where the inspection covers the compliance with the standards, the principle of prudence and financials etc.; Article 37 provides the criteria to determine the systematically important FMI; Article 38 provides the duty allocation in terms of supervision over the FMIs.

Recommendations for Market Infrastructure
In respect of **Payments**: 1. Permit the development of CNH PVP risk mitigation infrastructure for the protection from the loss of principal on payments for all market participants, both the Mainland and international entities. Introduction of PVP risk mitigation is a priority of central banks globally and supports adherence to both the Chinese (Article 146) and Global (Principles 35 and 50) FX Code. In respect of **Clearing**: 2. SHCH update its legal opinion after such amendments have been made to its close out methodology set out in its revised clearing guidelines. In respect of **Overseas FMIs**: 3. Develop a licensing or registration process authorizing the provision of cross-border services, with detailed requirements including scope and mechanism for reporting to ensure covered FMIs have a clear understanding of the regulatory expectations. The registration or licensing of overseas FMIs should only be required in cases where the services they provide are regularly used in the ordinary course of business by the domestic entities.

M. Annexes

Annex 1 – Key listing rules of BSE, SSE and SZSE

		BSE	SSE/SZSE Main Board	SSE STAR	SZSE ChiNext
1.	Market Orientation	Innovative SMEs	Blue Chips	"Technology" enterprises (focusing on strategic emerging industries such as next-generation information technology, artificial intelligence, medicine and biology, and automation)	Enterprises that focus on innovation, entrepreneurship, and creativity or new technologies, new industries, new formats, and new models
2.	Listing process	The Exchange is responsible for accepting and reviewing the issuer's public offering and listing application, and if the issuer meets the issuance conditions and information disclosure requirements, the Exchange would submit the review opinion, issuer registration application documents and relevant review materials to the CSRC for registration. The CSRC shall perform the issuance registration procedures in accordance with the law after receiving the submitted review opinions, issuer registration application documents and relevant review materials. In terms of listing process, the three exchanges are basically the same.			
3.	Listing Conditions - Financial Indicators	Market capitalization and financial indicators should be met at least one of the following criteria: (1) The expected market value is not less than 200 million yuan, the net profit in the past two years is not less than 15 million yuan and the weighted average return on net	Market capitalization and financial indicators should be met at least one of the following criteria: (1) The net profit in the past three years is positive, and the cumulative net profit in the last three years is not less than 150	Market capitalization and financial indicators should be met at least one of the following criteria: (1) The expected market value is not less than RMB 1 billion, the net profit in the last two years is positive and the cumulative net	Market capitalization and financial indicators should be met at least one of the following criteria: (1) The net profit in the past two years is positive, and the cumulative net

		BSE	SSE/SZSE Main Board	SSE STAR	SZSE ChiNext
		assets is not less than 8%, or the net profit in the recent year is not less than 25 million yuan and the weighted average return on net assets is not less than 8%; (2) The expected market value is not less than 400 million yuan, the average operating income in the past two years is not less than 100 million yuan, and the growth rate of operating income in the recent year is not less than 30%, and the net cash flow generated by operating activities in the recent year is positive; (3) The expected market value is not less than 800 million yuan, the operating income in the recent year is not less than 200 million yuan, and the total proportion of R&D investment in the past two years is not less than 8% of the total operating income in the past two years; (4) The estimated market value is not less than 1.5 billion yuan, and the	million yuan, the net profit in the recent year is not less than 60 million yuan, and the cumulative net cash flow generated by operating activities in the past three years is not less than 100 million yuan or the cumulative operating income is not less than 1 billion yuan; (2) The expected market value is not less than 5 billion yuan, and the net profit in the recent year is positive, the operating income in the recent year is not less than 600 million yuan, and the cumulative net cash flow generated by operating activities in the past three years is not less than 150 million yuan; (3) The expected market value is not less than 8 billion yuan, and the net profit in the recent	profit is not less than RMB 50 million, or the expected market value is not less than RMB 1 billion, the net profit in the recent year is positive and the operating income is not less than RMB 100 million; (2) The expected market value is not less than RMB 1.5 billion, the operating income in the recent year is not less than RMB 200 million, and the cumulative R&D investment in the past three years accounts for not less than 15% of the cumulative operating income in the past three years; (3) The expected market value is not less than RMB 2 billion, the operating income in the recent year is not less than RMB 300 million, and the cumulative net cash flow generated by operating activities in the past three years is not less than RMB 100 million;	profit is not less than 50 million yuan; (2) The expected market value is not less than 1 billion yuan, the net profit in the recent year is positive and the operating income is not less than 100 million yuan; (3) The expected market value is not less than 5 billion yuan, and the operating income in the recent year is not less than 300 million yuan.

		BSE	SSE/SZSE Main Board	SSE STAR	SZSE ChiNext
		total R&D investment in the past two years is not less than 50 million yuan. Additionally, before an issuer applies for BSE listing, temporarily it needs to be listed on NEEQ and upon application it shall be an NEEQ Innovation Tier company and have been listed on NEEQ for at least 12 months.	year is positive, and the operating income in the recent year is not less than 800 million yuan.	(4) The expected market value is not less than RMB 3 billion, and the operating income in the recent year is not less than RMB 300 million; (5) The estimated market value is not less than RMB 4 billion, the main business or products need to be approved by the relevant state departments, the market space is large, and phased results have been achieved. Pharmaceutical industry enterprises need to have at least one core product approved for phase II clinical trials, and other companies that meet the positioning of the STAR Board must have obvious technical advantages and meet corresponding conditions.	
4.	Lock-up Period	The BSE only requires a 12-month post-listing restriction on controlling shareholders, actual controllers and	The Shanghai and Shenzhen markets require that the shares held by all shareholders holding pre-IPO shares be restricted for 12 months after listing, of which the shares held by the controlling shareholder and actual controller of the Shanghai and Shenzhen companies are		

<table>
<tr><th></th><th></th><th>BSE</th><th>SSE/SZSE Main Board</th><th>SSE STAR</th><th>SZSE ChiNext</th></tr>
<tr><td></td><td></td><td>their relatives, directors, supervisors and senior personnel, and shareholders who held more than 10% of the shares before listing.</td><td colspan="3">limited to 36 months after listing, and if the issuer submits the application within 12 months before the new shareholders are submitted, the new shareholders shall undertake that the new shares held by them is not transferrable within 36 months from the date of acquisition.</td></tr>
<tr><td>5.</td><td>Sponsor Co-Investment</td><td>Not mandatory.</td><td>Co-investment is not allowed.</td><td>Co-investment is a must.</td><td>Under special circumstances, the sponsor needs to follow co-investment.</td></tr>
<tr><td>6.</td><td>Investor Threshold</td><td>Individual investors of the BSE should, before applying for trading authority, have daily average assets of no less than 500,000 yuan in their security account and capital account for 20 trading days, and also have more than 24 months of experience in securities trading.</td><td>There are no capital and trading experience requirements for access to the main board of Shanghai and Shenzhen.</td><td>The capital requirements of the STAR Board and the BSE are the same, and both STAR Board and BSE require more than 24 months of securities trading experience.</td><td>Individual investors of the ChiNext Board should, before applying for trading authority, have daily average assets of no less than 100,000 yuan in their security account and capital account for 20 trading days.</td></tr>
<tr><td>7.</td><td>Trading Rules (Daily Price Limit, Block Trades, etc.).</td><td>- There is no price limit on the first day of listing, and the price limit after that is 30%
- The effective price range of the BSE limit order is 5%
- Quantity of shares of a single block trade is not less than</td><td colspan="3">- There is no price limit in the first five trading days of the main boards and the STAR Board and ChiNext Board, and the price limit after would be 10% (main boards) and 20% (STAR Market and ChiNext Board).
- The effective price range for limit order on the main board of Shanghai and Shenzhen, the STAR Board and the ChiNext Board is 2%.
- Quantity of shares of a single block trade on the main board of Shanghai and Shenzhen, STAR Board and ChiNext Board needs to be no less than 300,000 shares or 2 million</td></tr>
</table>

		BSE	SSE/SZSE Main Board	SSE STAR	SZSE ChiNext
		100,000 shares or the transaction amount is not less than 1 million yuan - Market maker mechanism and margin trading business have been introduced	yuan. - Block trades are matched during 3 – 3:30pm window in general, except for STAR Market where block trades are matched during the entire trading session. - No market maker mechanism except for STAR Market.		
8.	Transfer to SSE/SZSE Boards	If a company listed on the BSE has been continuously listed on the BSE for more than one year, meets the corresponding transfer conditions of the STAR Market or ChiNext, and is willing to transfer the board, the company can realize the change of listing location after applying to the SSE or SZSE and being reviewed and approved by the SSE or SZSE, without performing registration procedures, and only filing with the CSRC.	Not applicable.		
9.	Delisting Mechanism	If a delisted company on the BSE meets the listing conditions of the Basic Tier or Innovation Tier of the NEEQ, it can also enter the corresponding level of the NEEQ to continue its trading and development, except for those	Shanghai and Shenzhen delisted companies can only be directly transferred to the delisting board that is managed by NEEQ.		

		BSE	SSE/SZSE Main Board	SSE STAR	SZSE ChiNext
		involving major violations of the law and not meeting the listing conditions of NEEQ. Those not meeting the listing conditions of NEEQ will be transferred to the delisting board.			

Annex 2 - Comparison between QFI and Stock Connect

	QFI	Stock Connect (Northbound)
Eligible investors	FIIs including fund management companies, commercial banks, insurance companies, securities companies, futures companies, trust companies, government investment management companies, sovereign funds, pension funds, charity funds, endowment funds, international organizations and other institutions recognized by the CSRC.	All foreign investors including individuals (but only institutional professional investors for SZSE ChiNext shares and SSE STAR shares).
Regulatory approval	CSRC license	None
Quota	None	Northbound daily quota of RMB 52 bn for each of Shanghai Connect and Shenzhen Connect
Account structure	Onshore account with custodian in the name of "QFI + Proprietary Funds", "QFI + Client Name", "QFI + Fund", or "QFI + Client Fund"	Offshore investor account in HK via custodian with onshore nominee omnibus account at CSDC
Holding structure	QFI maintains account directly with CSDC	HKSCC, as nominee holder for investor
Eligible investments	• All securities listed on SSE/SZSE/BSE/NEEQ • Publicly-offered Securities investment funds, including close-ended, open-ended and ETFs • Private investment funds issued by securities futures operating institutions and AMAC-registered private investment fund managers • Financial futures, commodity futures and options traded on approved exchanges	A constituent stock of the SSE A Share Index / SZSE-listed A shares that is a constituent stock of the SZSE Composite Index fulfils: • a daily average market capitalization in the last six months of RMB5 billion or above; • a daily average turnover in the last six months of RMB30 million or above; • ratio of trading suspension days lower than 50% in the last six months; and

	QFI	Stock Connect (Northbound)

	• IPOs, securities lending and margin trading and securities financing
	• FX derivatives (for hedging purpose only)
		• additional criteria for the first time inclusion of a stock with Differentiated Voting Rights (DVR stock):
		  ○ listed on SSE/SZSE for no less than six months and twenty SSE/SZSE trading days;
		  ○ a daily average market capitalization in the last 183 calendar days of RMB20 billion or above;
		  ○ an aggregated turnover in the last 183 calendar days of RMB6 billion or above; and
		  ○ never been publicly censured by SSE/SZSE due to any breach of any requirements under the SSE/SZSE Rules applicable to DVR stocks
		• A+H shares
		
		provided that:
		(i) they are not traded on SSE/SZSE in currencies other than RMB; and (ii) they are not under risk alert (ST/*ST companies or shares subject to the delisting process, etc.)

	QFI	Stock Connect (Northbound)
Investment currency	CNY and CNH	CNH, HKD and USD
Pre-funding	Required (cash available on T-1)	None
Repatriation limit	None	N/A
Block trading	Yes	No
Short selling	Yes	Yes
Stock borrow and lending	Yes	Permitted with restrictions

Annex 3 - Comparison between CIBM Direct and Bond Connect

	CIBM Direct	Northbound Bond Connect	Southbound Bond Connect	QFI
Pre-Investment Requirement	Registration with PBOC Shanghai Head Office through settlement agent	Registration with PBOC Shanghai Head Office through a member of the Central Moneymarkets Unit (CMU) via BCCL	Application for access to Southbound Bond Connect business and opening transaction account with CFETS	Regulatory approvals
Regulators	PBOC and SAFE	PBOC, SAFE and HKMA	PBOC, SAFE and HKMA	PBOC, SAFE and CSRC
Tradable Products	*<u>Foreign central banks and similar institutions, overseas RMB business clearing banks and overseas participating banks</u>*: All tradable products including cash bonds [223], bond repo, bond lending, bond forward, forward rate agreement and interest rate swap; *<u>Other overseas institutional investors</u>*: Cash bonds except bond repo; bond lending, bond forwards, interest	Cash bonds only.	Cash bonds only.	Cash bonds except bond repo; bond lending, bond forwards, interest rate forwards or swaps traded only for hedging purpose; all products of exchange bond market.

223 Government bond, PBOC bill, policy bank bond, finance bond, corporate bond, enterprise bond, commercial paper, mid-term note, etc.

	CIBM Direct	Northbound Bond Connect	Southbound Bond Connect	QFI
	rate forwards or swaps traded only for hedging purpose.			
Eligible Investors	(i) Foreign central bank-type institutions[224]; (ii) QFIs; (iii) Commercial banks, insurance companies, securities companies, fund management companies and other asset management institutions or the non-legal-person products issued by any of the above institutions; (iv) Pension funds, charitable funds, or donated funds; (v) Other mid- and long-term institutional investors recognized by the PBOC.	Same as left column.	49 domestic primary dealers for public market business[225]; QDII and RQDII	Overseas fund management companies, commercial banks, insurance companies, securities companies, futures companies, trust companies, government investment management institutions, sovereign funds, pension funds, charity funds, endowment funds, international organizations and other institutions recognized by the CSRC.
Currency of funds to be remitted into	Foreign Currencies or CNH	Foreign Currencies or CNH	Foreign Currencies or CNH	Foreign Currencies or CNH

[224] Foreign central banks or monetary authorities, international financial organizations and sovereign wealth funds

[225] Latest data as of May 20, 2022 sourced from the PBOC, http://www.pbc.gov.cn/zhengcehuobisi/125207/125213/125431/125469/4560724/index.html.

	CIBM Direct	Northbound Bond Connect	Southbound Bond Connect	QFI
and outside China				
Trading Counterparty	More than 22,000 participants in the CIBM including 92 onshore market makers[226]	56 onshore market makers[227]	13 offshore market makers[228]	More than 22,000 participants in the CIBM including 92 onshore market makers
Trading Platform	CFETS/Bloomberg, MarketAxess and Tradeweb (directly connected with CFETS)	CFETS/Bloomberg, MarketAxess and Tradeweb (directly connected with CFETS)	CFETS/Bloomberg and Tradeweb (directly connected with CFETS)	CFETS/Bloomberg, Tradeweb (directly connected with CFETS)
Trading Mechanism	Entrusting settlement agent to initiate transaction and make inquiry trading; Sending requesting for quotation (RFQ) to 92 onshore market makers	Sending RFQ to 56 onshore market makers	Sending RFQ to 13 offshore market makers	Entrusting settlement agent to initiate transaction and make inquiry trading; Sending RFQ to 92 onshore market makers
FX Hedging	Foreign banking institutional investors [229] and foreign non-banking	Hong Kong FX settlement banks[231]	Domestic investors investing in foreign currency bonds with RMB may conduct	Qualified custodian or onshore financial institutions

[226] Latest data as of May 20, 2023 sourced from CFETS, https://www.chinamoney.com.cn/chinese/mtmemrmb/.
[227] Latest data as of April 9, 2020 sourced from CFETS, https://www.chinamoney.com.cn/chinese/bccn/.
[228] HKMA publicized a list of designated market makers for Southbound Trading under Bond Connect on its website on September 17, 2021, https://www.hkma.gov.hk/eng/news-and-media/press-releases/2021/09/20210917-6/.
[229] Foreign banking institutional investors may choose to conduct FX hedging via (i) directly trading with custodian, settlement agent or other domestic financial institutions as a client thereof; (ii) trading in the China's Inter-bank Foreign Exchange Market ("CIFXM") through engaging the prime brokerage services after becoming a member of the CFETS; or (iii) trading in the CIFXM directly after becoming a member of the CFETS.
[231] Bond Connect investors may engage up to three banks.

	CIBM Direct	Northbound Bond Connect	Southbound Bond Connect	QFI
	institutional investors[230].		currency conversion and foreign exchange hedging via the CIFXM.	
Bond Settlement	Gross DVP	Gross DVP	Gross DVP	Gross DVP
Settlement Period	T+0/T+1/T+2/T+3/ T+N	T+0/T+1/T+2/T+3/ T+N	T+1/T+2/T+3/T+N	T+0/T+1/T+2/T+3/ T+N
Account Structure	Direct holding	Indirect holding (omnibus account, limited to one custodian)	Indirect holding	Direct holding
Quota	No individual or aggregate quota limit. An applicant is required to indicate its anticipated investment size on the PBOC registration form.	No individual or aggregate quota limit under Northbound Bond Connect.	The net outflow of funds under Southbound Bond Connect is subject to an annual aggregate quota of RMB 500 billion (or equivalent), and a daily quota of RMB 20 billion (or equivalent).	No individual or aggregate quota limit for CIBM.
Lock-in Period	No restrictions.	No restrictions.	No restrictions.	No restrictions.
Repatriation Restriction	No restrictions for a single currency (investment via RMB or a foreign currency); Certain restrictions for inward remittance of	No restrictions.	No restrictions.	No restrictions.

[230] Foreign non-banking institutional investors may choose to conduct FX hedging via (i) directly trading with custodian, settlement agent or other domestic financial institutions as a client thereof; or (ii) trading in the CIFXM through engaging the prime brokerage services after becoming a member of the CFETS.

	CIBM Direct	Northbound Bond Connect	Southbound Bond Connect	QFI
	"RMB + foreign currency"[232]			
Non-trade Transfer	The same overseas institutional investor is allowed to make non-trade bond/funds transfer between its QFII/RQFII account and its CIBM Direct account.	Non-trade transfer is only allowed for a switch in local custodian (a CMU member) by an overseas investor.[233]	N/A	The same overseas institutional investor is allowed to make non-trade bond/funds transfer between its QFII/RQFII account and its CIBM Direct account.

[232] The outward remittance of RMB/foreign currency in total shall not exceed 120% of the RMB/foreign currency inward remittance, which can be relaxed as appropriate in the case of long-term investments in China's bond market. Specifically, the SAFE has suggested in its policy Q&As that in practice, the foregoing repatriation restriction can be relaxed in that:

(i) investing for no more than 1 year (as of the date of obtaining the Filing Notice of CIBM Access, the same below): not exceeding 120%;
(ii) investing for 1 to 3 years (inclusive), not exceeding 130%;
(iii) investing for 3 to 5 years (inclusive), not exceeding 140%;
(iv) investing for more than 5 years, not exceeding 150%.

SAFE's Q&A on Provisions on the Management of Funds Invested by Foreign Institutional Investors in China's Bond Market (《境外机构投资者投资中国债券市场资金管理规定》政策问答), http://www.safe.gov.cn/safe/2023/0321/22487.html.

[233] To avoid doubt, please also note that FOP transfer is not always necessary when an investor changes asset manager. If the new asset manager engages the same custodian bank, the investor may continue using the same securities account.

Annex 4 - List of FMC WFOEs, PFM WFOEs and BWMSs

Note: Names in English are generally translated from Chinese and are for reference only.

I. List of FMC WFOEs

(1) BlackRock Fund Management Co. Ltd (贝莱德基金管理有限公司)
(2) Manulife Fund Management Co., Ltd. (宏利基金管理有限公司)
(3) Neuberger Berman Fund Management (China) Limited (路博迈基金管理（中国）有限公司)
(4) FIL Fund Management (China) Company Limited (富达基金管理（中国）有限公司)
(5) Schroders Fund Management (China) Company Limited (施罗德基金管理（中国）有限公司)
(6) JPMorgan Asset Management (China) Company Limited (摩根基金管理（中国）有限公司)
(7) Morgan Stanley Investment Management (China) Company Limited (摩根士丹利基金管理（中国）有限公司)
(8) AllianceBernstein Fund Management Co. Ltd (联博基金管理有限公司)

II. List of PFM WFOEs

(1) UBS Asset Management (Shanghai) Limited (瑞银资产管理（上海）有限公司)
(2) Fullerton Investment Management (Shanghai) Co. Ltd (富敦投资管理（上海）有限公司)
(3) Man Investment Management (Shanghai) Co., Ltd. (英仕曼（上海）投资管理有限公司)
(4) Value Partners Investment Management (Shanghai) Limited (惠理投资管理（上海）有限公司)
(5) Invesco Investment Management (Shanghai) Limited (景顺纵横投资管理（上海）有限公司)
(6) Abrdn Private Fund Management (Shanghai) Company Limited (安本私募基金管理（上海）有限公司)
(7) AZ Investment Management (Shanghai) Co., Ltd. (安中投资管理（上海）有限公司)
(8) Winton Investment Management (Shanghai) Co., Ltd. (元胜投资管理（上海）有限公司)
(9) Bridgewater (China) Investment Management Co., Ltd. (桥水（中国）投资管理有限公司)
(10) APS CHINA Asset Management PTE LTD (毕盛（上海）投资管理有限公司)
(11) Eastspring Investment Management (Shanghai) Company Limited (瀚亚投资管理（上海）有限公司)
(12) Mirae Asset Investment Management (Shanghai) Co., Ltd. (未来益财投资管理（上海）有限公司)
(13) D. E. Shaw Investment Management (Shanghai) Co., Ltd. (德劭投资管理（上海）有限公司)
(14) Nomura Investment Management (Shanghai) Co., Ltd. (野村投资管理（上海）有限公司)
(15) Barings Investment Management (Shanghai) Limited (霸菱投资管理（上海）有限公司)
(16) Two Sigma China Co., Ltd. (腾胜投资管理（上海）有限公司)
(17) BEA Union Investment Management (ShenZhen) Limited (东亚联丰投资管理（深圳）有限公司)
(18) Russell Investment Management (Shanghai) Co., Ltd (罗素投资管理（上海）有限公司)

(19) Income Partners Investment Management (Shanghai) Limited (弘收投资管理（上海）有限公司)
(20) William O'Neil Investment Management (Shanghai) Limited (威廉欧奈尔投资管理（上海）有限公司)
(21) Power Pacific (Shanghai) Investment Management Co., Ltd. (鲍尔赛嘉（上海）投资管理有限公司)
(22) Metori Investment Management (Zhuhai Hengqin) Limited (迈德瑞投资管理（珠海横琴）有限公司)
(23) Baillie Gifford Investment Management (Shanghai) Limited (柏基投资管理（上海）有限公司)
(24) iFAST Investment Management China Ltd (上海首奕投资管理有限公司)
(25) Cephei Capital Management (Tianjin) Limited (润晖投资管理(天津)有限公司)
(26) Robeco Private Fund Management (Shanghai) Co., Ltd. (荷宝私募基金管理(上海)有限公司)
(27) Prescient Private Fund Management (Shanghai) Limited (先知私募基金管理（上海）有限公司)
(28) Anatole (Shenzhen) Investment Management Limited (晨曦（深圳）私募证券投资基金管理有限公司)
(29) Beijing Dao Tai Liang He Private Fund Management Co., Ltd. (北京道泰量合私募基金管理有限公司)
(30) AXA Investment Managers Private Fund Management (Shanghai) Limited (安盛私募基金管理(上海)有限公司)
(31) Shenzhen Victory Private Securities Investment Fund Management Co., Ltd. (深圳市胜利私募证券投资基金管理有限公司)

III. List of BWMSs

(1) Amundi BOC Wealth Management Co. Ltd (汇华理财有限公司)
(2) BlackRock CCB Wealth Management Limited (贝莱德建信理财有限责任公司)
(3) Schroders BOCOM Wealth Management Co. Ltd (施罗德交银理财有限公司)
(4) Goldman Sachs ICBC Wealth Management Co. Ltd (高盛工银理财有限责任公司)
(5) BNP Paribas ABC Wealth Management Co., Ltd. (法巴农银理财有限责任公司)

Annex 5 - "1+N" System

1	Department	Document
Top-level design	Central Committee of CPC and State Council	Opinions on Completely, Accurately and Comprehensively Implementing the New Development Concepts and Effectively Carrying out the Work of Peak Carbon Emission and Carbon Neutrality
	State Council	Action Plan for Peak Carbon Emission by 2030
Series N	**Department**	**Document**
Action for Green and Low-carbon Transformation of Energy	NDRC, National Energy Administration	Plan for Modern Energy System during the 14th Five-Year Plan Period
	NDRC, National Energy Administration	Medium and Long-term Plan for the Development of the Hydrogen Energy Industry (2021-2035)
Action for Energy Saving, Carbon Emission Reduction and Efficiency Improvement	State Council	Comprehensive Work Plan for Energy Saving and Carbon Emission Reduction during the 14th Five-Year Plan Period
	NDRC, Ministry of Industry and Information Technology, MEE and National Energy Administration	Implementing Guidelines for the Reform and Upgrading of Energy Saving and Carbon Emission Reduction in Key Areas of High Energy-consuming Industries (2022 Edition)
Action for Peak Carbon Emission in Industry Sector	Ministry of Industry and Information Technology, NDRC and MEE	Guiding Opinions on Promoting the High-quality Development of the Iron and Steel Industry
	NDRC, Ministry of Industry and Information Technology, MEE and National Energy Administration	Implementing Guidelines for the Reform and Upgrading of Energy Saving and Carbon Emission Reduction in the Cement Industry
	Ministry of Industry and Information Technology, NDRC, Ministry of Science and Technology, MEE, Ministry of Emergency Management, National Energy Administration	Guiding Opinions on Promoting the High-quality Development of the Petrochemical and Chemical Industry during the 14th Five-Year Plan Period

	Ministry of Industry and Information Technology, NDRC	Guiding Opinions on the High-quality Development of the Chemical Fiber Industry
	Ministry of Industry and Information Technology, NDRC	Guiding Opinions on the High-quality Development of the Industrial Textiles Industry
Action for Peak Carbon Emission in Urban and Rural Construction	Ministry of Agriculture and Rural Affairs	Guiding Opinions on Expanding Various Functions of Agriculture and Promoting the High-quality Development of Rural Industries
	Ministry of Housing and Urban-Rural Development	Action Plan for Promoting Urban and Rural Construction in the Yangtze River Economic Belt during the 14th Five-Year Plan Period
	Ministry of Housing and Urban-Rural Development	Action Plan for the Ecological Protection and High-quality Development of Urban and Rural Construction in the Yellow River Basin during the 14th Five-Year Plan Period
	Ministry of Housing and Urban-Rural Development	Science and Technology Development Plan for Housing and Urban-rural Development during the 14th Five-Year Plan Period
Action for Green and Low Carbon Transportation	Ministry of Transport, National Railway Administration, Civil Aviation Administration of China and State Post Bureau	Implementing Opinions on Promoting High-quality Development of Transportation in the Central Region in the New Era
Action for Promoting Circular Economy in Carbon Reduction Purpose	NDRC	Development Plan for the Circular Economy during the 14th Five-Year Plan Period
Action for Promoting Green and Low-Carbon Science and Technology Innovation	Ministry of Science and Technology, NDRC, Ministry of Industry and Information Technology, MEE, Ministry of Housing and Urban-Rural Development, Ministry of Transport, Chinese Academy of Sciences, Chinese Academy of Engineering, National Energy	Implementation Plan for the Science to Support Peak Carbon Emission (2022-2030)

	Administration	
Action for Carbon Sequestration Capacity Enhancement	National Forestry and Grassland Administration	Guidelines for Approval and Certification of Forestry Carbon Sequestration Projects
	Ministry of Natural Resources	Economic Value Accounting for Marine Carbon Sequestration
Action for Green and Low Carbon Society	Ministry of Education	Work Plan for Strengthening the Construction of the Cultivation System for Talents of Peak Carbon Emission and Carbon Neutrality in Higher Education
Action for Promoting All Regions to Peak Carbon Emission Hierarchically and Orderly	Each province implements policies specifically in the form of strategic guidance documents, supporting documents and local regulations.	
Safeguard Policies	China Development Bank	Action Plan for Implementing Green and Low-carbon Finance Strategy and Supporting the Peak Carbon Emission and Carbon Neutrality
	General Office of the MEE	Guidelines for Accounting Methods and Reporting of Greenhouse Gas Emissions by Enterprises: Power Generation Facilities (Revised in 2022)
	NDRC	Announcement on Clarifying the Act of Driving up Prices by Operators in Coal Sector

Annex 6 - Details of 9 local pilot carbon emission right trading platforms

Name	Overview	Carbon emission products
China Beijing Green Exchange (CBEEX)[234]	CBEEX is one of the first batch of Chinese VER trading institutions filed with competent authorities of the State. It initiated the development of China's first VER standard, "Panda Standard", and participated in the drafting of the PBOC's *Environmental Equity Financing Tool* and other green finance industry standards. It provides carbon accounting and consulting services for the carbon neutrality plan for the 2022 Olympic and Paralympic Winter Games.	Beijing Emission Allowances (BEA), Chinese Certified Emission Reduction (CCER), VER and Voluntary Energy Saving Amount
Shanghai Environment and Energy Exchange (SEEE)[235]	SEEE is the designated trading platform for the Shanghai carbon trading pilot scheme, the CCER trading platform filed with the national competent authority of carbon trading, and the construction and operation institution of the national carbon emission trading system designated by the MEE. On July 16, 2021, the national carbon emission right market was officially launched for trading. SEEE undertakes the specific work such as operation maintenance of the national carbon emission trading system.	Shanghai Emission Allowances (SHEA), CCER, and Shanghai Emission Allowances Forward (SHEAF)
Guangzhou Emissions Exchange (GEE)[236]	It is one of the first batch of institutions accredited by the NDRC for CCER trading, and the only dual pilot institution in the Greater Bay Area that concurrently serves as a national carbon trading pilot scheme and a green finance reform and innovation experimental zone. GEE opened China's first primary market allowance auction, completed the first CCER online trading in China, and is the first exchange with allowance trading volume exceeding 100 million tons in China.	Guangdong Emission Allowances (GDEA), Guangdong Carbon Inclusion Certified Emission Reduction, CCER, Ecological Compensation Certified Emission Reduction etc.
China Emissions Exchange (Shenzhen)[237]	It is a comprehensive environmental rights and interests trading institution and low-carbon financial service platform that promotes energy conservation and emission reduction based on the market mechanism.	Shenzhen Emission Allowances (SZEA) and CCER

[234] China Beijing Green Exchange (cbeex.com.cn).
[235] Shanghai Environment and Energy Exchange (cneeex.com).
[236] Guangzhou Emissions Exchange (cnemission.com).
[237] China Emissions Exchange (Shenzhen) (szets.com).

Tianjin Climate Exchange (TCE)[238]	It is one of the first batch of comprehensive environment and energy trading platforms in China. TCE is the designated trading platform of Tianjin carbon trading pilot scheme, and one of the first batch of trading institutions of voluntary emission reduction of greenhouse gas in China. It has undertaken many national green and low-carbon research projects.	Tianjin Emission Allowances (TJEA), CCER, VER
China Hubei Emission Exchange[239]	It is one of the first pilot institutions for carbon emission trading in China that has been filed with the MEE and established with the approval of the provincial government. It has pioneered carbon financial products such as carbon funds, carbon custody and carbon pledge.	Hubei Emission Allowances (HBEA), and CCER
Chongqing Carbon Emissions Trading Center[240]	It is a comprehensive element resources trading market. It provides integrated carbon neutrality services, allowance trading and certified emission reduction trading products.	Chongqing Emission Allowance (CQEA), CCER
Haixia Equity Exchange[241]	It studied and launched the Forest Carbon Emission Reduction projects that can be traded in carbon market within Fujian province.	Fujian Emission Allowance (FJEA), CCER, Fujian Forest Carbon Emission Reduction (FFCER)
Sichuan United Environment Exchange[242]	It is the first carbon trading institution that has been filed with the State in non-pilot areas in the country. At present, it is the only environmental resources trading platform in the country which covers the trading of carbon emission, energy use right, pollution discharge right and water right as the core main business.	CCER

[238] Tianjin Climate Exchange (chinatcx.com.cn).
[239] China Hubei Emission Exchange (hbets.cn).
[240] Chongqing Carbon Emissions Trading Center (tpf.cqggzy.com).
[241] Haixia Equity Exchange (hxee.com.cn)
[242] Sichuan United Environment Exchange (sceex.com.cn).

N. Glossary

Word or Acronym	Expanded version
ABN	Asset Backed Note
ABS	Asset Backed Security
ADT	Average Daily Turnover
ALM	Asset Liability Match
AMAC	Asset Management Association of China
AML	Anti-Money Laundering
APAC	Asia Pacific
API	Application Programming Interface
ASEAN	Association of Southeast Asian Nations
ASIFMA	Asia Securities Industry and Financial Markets Association
AUM	Assets Under Management
BCBS-IOSCO	Basel Committee on Banking Supervision and International Organisation of Securities Commissions
BCCL	Bond Connect Company Limited
BEA	Beijing Emission Allowances
BIL ESP	Bilateral Executive Streaming Price
BIS	Bank for International Settlements
BRBR	"Belt and Road Bankers" Roundtable
BRI	Belt and Road Initiative
BSA	Bond Settlement Agent
BWMS	bank wealth management subsidiary
CAC	Cyberspace Administration of China
CBEEX	China Beijing Environment Exchange
CBIRC	China Banking and Insurance Regulatory Commission
CCASS	Central Clearing and Settlement System
CCCP	China Connect Clearing Participants
CCDC	China Central Depository & Clearing Co., Ltd.
CCER	Chinese Certified Emission Reduction
CCP	central clearing counterparty
CD	Interbank Certificates of Deposit
CEA	carbon emission allowances
CERDS	China Enterprise Reform and Development Society
CFETS	China Foreign Exchange Trade System

CFFEX	China Financial Futures Exchange
CFTC	Commodities Futures Clearing Commission
CFXC	China Foreign Exchange Committee
CGB	Chinese Government Bond
CGBP	China Green Bond Principles
CIBM	China Interbank Bond Market
CIFXM	China's Inter-bank Foreign Exchange Market
CII	Critical Information Infrastructure
CIPS	Cross-border Interbank Payment System
CIT	Corporate Income Tax
CMU	Central Moneymarkets Unit
CNAPS	China National Advanced Payment System
CNH	offshore RMB
CNS	Continuous Net Settlement
CNY	Chinese Yuan or Renminbi funded in the onshore market
COFER	Currency Composition of Official Foreign Exchange Reserve
COP26	United Nations Climate Change Conference
CPC	Communist Party of China
CPMI-IOSCO	Committee on Payments and Market Infrastructures – International Organization of Securities Commissions
CQEA	Chongqing Emission Allowance
CRR	Capital Requirements Regulation
CRS	Common Reporting Standard
CSA	Credit Support Annex
CSDC/CSDCC	China Securities Depository and Clearing Corporation
CSL	Cybersecurity Law
CSOE	state-owned enterprises directly under the central government
CSP	Cloud Service Provider
CSRC	China Securities Regulatory Commission
CTF	Counter-Terrorist Financing
DCO	Derivative Clearing Organisation
DLT	Distributed Ledger Technology
DNS	Deferred Net Settlement
DSL	Data Security Law
DVP	Delivery versus Payment

EBS	Electronic broking service
EMIR	European Market Infrastructure Regulation
ESG	Environmental, Social and Governance
ESMA	European Securities and Markets Authority
ETF	Exchange-Traded Fund
EU	European Union
EUR	European Dollar
FDL	China's Futures and Derivatives Law
FFCER	Fujian Forest Carbon Emission Reduction
FI	Financial Institution
FII	Foreign Institutional Investor
FJEA	Fujian Emission Allowance
FMC	public fund management companies
FMI	Financial Market Infrastructure
FTSE Russell	Financial Times Stock Exchange International Ltd., a British provider of stock market indices and data services
FX	Foreign Exchange
G10	Group of 10
G20	Group of 20
GBA	Guangdong-Hong Kong-Macao Greater Bay Area
GBSC	Green Bond Standards Committee
GC	General Collateral
GDEA	Guangdong Emission Allowances
GDP	Gross Domestic Product
GEE	Guangzhou Emissions Exchange
GFB	green financial bond
GFTF	China-Singapore Green Finance Taskforce
GFXC	Global Foreign Exchange Committee
GIP	Green Investment Principles for the Belt and Road
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GMRA	Global Master Repurchase Agreement
GMSLA	Global Master Securities Lending Agreement
HBEA	Hubei Emission Allowances
HKD	Hong Kong dollar
HKEX	Stock Exchange of Hong Kong
HKFE	Hong Kong Futures Exchange Limited
HKMA	Hong Kong Monetary Authority
ICBC	Industrial and Commercial Bank of China

ICMA	International Capital Market Association
ICSD	International central securities depository
ICVCM	Integrity Council on Voluntary Carbon Markets
IMF	International Monetary Fund
IM	Initial Margin
IPO	Initial Public Offering
IPSF	International Platform on Sustainable Finance
IRA	International Rating Agency
IRD	Interest Rate Derivative
IRS	Interest Rate Swap
ISDA	International Swaps and Derivatives Association
ISIN	International Securities Instrument Number
KYC	Know Your Client
LCS	Local Currency Settlement
LDI	Liability Driven Investment
LOF	Listed Open-Ended Fund
LPR	Loan Prime Rate
MLPS	Multi-Level Protection Scheme
MOF	Ministry of Finance
MRF	Mutual Recognition of Funds
NAFMII	National Association of Financial Market Institutional Investors
NCD	Negotiable Certificate of Deposit
NDB	National Data Bureau
NDRC	National Development and Reform Commission
NAFR	National Administration of Financial Regulation
NGFS	Central Banks and Supervises Network for Greening the Financial System
NPC	National People's Congress
OB	Overseas Broker
ODM	Order Driven Model
OI	Overseas Intermediary
OMO	Open Market Operations
OPB	Offshore Participating Bank
OTC	Over-the-Counter
PBOC	People's Bank of China
PBU	Participant Business Unit
PCAOB	Public Company Accounting Oversight Board
PFM	Private Fund Management company
PFMI	Principles for Financial Market Infrastructures

PIPL	Personal Information Protection Law
PPN	Private Publication Notes
PRB	Principles for Responsible Banking
PRC	People's Republic of China
PVP	Payment-versus-payment
QCCP	Qualified Central Counter-Party Clearing House
QDLP	Qualified Domestic Investment Partnership
QDII	Qualified Domestic Institutional Investor
QDM	Quote Driven Model
QFLP	Qualified Foreign Limited Partnership
QFI	Qualified Foreign Investor
QFII	Qualified Foreign Institutional Investor
RCEP	Regional Comprehensive Economic Partnership
REIT	Real Estate Investment Trust
RFM	Request for Markets
RMB	Renminbi, or Chinese Yuan, a unit of currency
RQFII	Renminbi Qualified Foreign Institutional Investor
RTGS	Real-time Gross Settlement
S&P	Standard & Poor's Financial Services
SAFE	State Administration of Foreign Exchange
SAR	Special Administrative Region (China)
SASAC	State-owned Assets Supervision and Administration Commission
SBL	Securities Borrowing and Lending
SHCH	Shanghai Clearing House
SDR	Special Drawing Rights (IMF)
SEC	Securities and Exchange Commission
SEEE	Shanghai Environment and Energy Exchange
SFC	Securities and Futures Commission
SGX	Singapore Exchange
SHEA	Shanghai Emission Allowances
SHEAF	Shanghai Emission Allowances Forward
SHIBOR	Shanghai Interbank Offered Rate
SPSA	Special Segregated Accounts
SSE	Shanghai Stock Exchange
SSO	Single Stock Options
STA	State Taxation Administration
STAR	Science and Technology Innovation Board
STP	Straight-Through Processing

SWIFT	Society for World-wide Interbank Financial Communication
SZEA	Shenzhen Emission Allowances
SZSE	Shenzhen Stock Exchange
TC260	National Information Security Standardization Technical Committee
TCE	Tianjin Climate Exchange
TJEA	Tianjin Emission Allowances
TSE	Tokyo Stock Exchange
UK	United Kingdom
UMR	Unclear Margin Rules
US	United States
US CFTC	US Commodity Futures Trading Commission
USD	US Dollar
UTI	Unified Transaction Identifier
VCU	Verified Carbon Unit
VCS	Verified Carbon Standard
VM	Variation Margin
VIE	Variable Interest Entity
VAT	Value Added Tax
WFOE	Wholly Foreign-Owned Enterprises
WHT	Withholding Income Tax
WMC Scheme	Wealth Management Connect scheme
WVR	Weighted Voting Rights

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