

# Legal Commentary

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## CSRC to Make QFII and RQFII Attractive Again

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On 31 January 2019, China Securities Regulatory Commission ("**CSRC**") issued consultation drafts of the *Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors* and the *Provisions on Issues Concerning the Implementation of the Measures for the Administration of Domestic Securities and Futures Investment by Qualified Foreign Institutional Investors and RMB Qualified Foreign Institutional Investors* (collectively the "**Consultation Drafts**")<sup>1</sup> to amend and consolidate rules related to qualified foreign institutional investors (**QFII**) and RMB Qualified Foreign Institutional Investors (**RQFII**) programs.

As one of the earliest financial market liberalization initiatives, QFII program used to attract many foreign institutional investors to the Chinese securities market and RQFII program has been an important supplement for such efforts. However, in recent years, with more alternative access channels becoming available (such as the Stock Connect and Bond Connect schemes), QFII and RQFII programs have gradually lost their attraction due to the relatively complicated application process, on-going compliance requirements and, more importantly, the limited investment scope which is largely overlapped with that of other schemes. The Consultation Drafts are intended to make the QFII and RQFII programs attractive again by further relaxing relevant restrictions and requirements. The key proposed changes under the Consultation Drafts include:

### 1. Merging QFII and RQFII regimes

Currently, QFII and RQFII programs are subject to separate rules and application procedures. The Consultation Drafts aim to consolidate all QFII and RQFII regulations into one set of unified rules to further synchronize the qualification requirements applicable to QFIIs and RQFIIs and mitigate regulatory arbitrage by investors. As a result, the only key difference between QFII and RQFII will be that RQFIIs will use offshore RMB for making investments while QFIIs will remit foreign currency into China, which will be converted into RMB for investments.

<sup>1</sup> The full versions of the Consultation Drafts are available at [http://www.csrc.gov.cn/pub/zjhpublic/zjh/201901/t20190131\\_350601.htm](http://www.csrc.gov.cn/pub/zjhpublic/zjh/201901/t20190131_350601.htm) (in Chinese) and [http://www.csrc.gov.cn/pub/csrc\\_en/newsfacts/PressConference/201901/t20190131\\_350613.html?from=timeline&isappinstalled=0](http://www.csrc.gov.cn/pub/csrc_en/newsfacts/PressConference/201901/t20190131_350613.html?from=timeline&isappinstalled=0) (in English).

## **2. Expanding investment scope**

The Consultation Drafts will significantly expand the investment scope for QFIIs/RQFIIs. In addition to the currently permissible asset classes which mainly include A-shares, bonds, public securities investment funds and stock index futures, QFIIs/RQFIIs will be able to invest in (i) shares traded on the National Equities Exchange and Quotations (NEEQ); (ii) bond repo; (iii) private investment funds; (iv) financial futures listed and traded on the China Financial Futures Exchange (CFFEX); (v) commodity futures traded on futures exchanges approved by CSRC; and (vi) options traded on futures exchanges approved by the State Council or CSRC. QFIIs/RQFIIs will also be allowed to participate in margin trading and securities lending on domestic stock exchanges.

It is worth noting that the investment scope of the permissible private investment funds shall be within the permissible investment scope of QFIIs/RQFIIs.

## **3. Facilitating engagement of investment advisors**

The Consultation Drafts explicitly permit a QFII/RQFII to engage its affiliated domestic private securities investment fund manager for investment advisory services.

## **4. Clarifying beneficial ownership of assets**

The Consultation Drafts stipulate that the assets under a "Qualified Investor + Client Name/Client Assets" account belong to the clients and are separate and independent from those of the QFII/RQFII and its custodian.

## **5. Enhancing ongoing supervision**

The Consultation Drafts reflect PRC regulator's intention to enhance ongoing supervision on QFIIs/RQFIIs, including account and trading monitoring by brokers, information sharing by exchanges and depositaries, additional information disclosure on offshore hedging positions related to onshore investment, and the "look-through" approach for underlying investors' compliance with holding limits and disclosure of interest requirements. The corresponding penalties for violations are also specified.

The issuance of the Consultation Drafts is seen as a very positive development and has shown CSRC's intent to address foreign investors' common concerns and promote inbound investments. In particular, allowing the QFIIs/RQFIIs to invest in onshore private investment funds and engage affiliated domestic private securities investment fund managers for investment consulting services will also benefit foreign asset managers' onshore private securities investment fund management (known as "WFOE PFM") business.

However, there may still be a few points worth further clarifying with CSRC such as the aggregation requirements on applying disclosure of interest/short swing profit rule to foreign managers and potential waiver grant.

The consultation period will end on 2 March 2019 and we will continue to closely monitor for any developments.

## ***Important Announcement***

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