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Introduction of Newly-Issued Rules on the Pilot Program of Domestic Securities Investment by RMB Qualified Foreign Institutional Investors (“RQFII”)

James Wang, Kelvin Gao and Sheldon Chen

On December 16, 2011, China Securities Regulatory Commission (“**CSRC**”), the People’s Bank of China (the “**PBOC**”) and State Administration of Foreign Exchange (“**SAFE**”) jointly released the *Pilot Measures on Domestic Securities Investment by RMB Qualified Foreign Institutional Investors for Fund Management Companies and Securities Companies* (the “**Pilot Measures**”), a move showing that after deliberation for more than two years, RQFII, another measure to accelerate the backflow of offshore RMB funds as well as to push forward the internationalization of RMB, has been formally launched, in which case offshore RMB funds are generally permitted to invest in domestic securities market. Thereafter, CSRC, the PBOC and SAFE respectively promulgated its own implementing rules (i.e., the *Implementing Rules for the Pilot Measures on Domestic Securities Investment by RMB Qualified Foreign Institutional Investors for Fund Management Companies and Securities Companies* (the “**CSRC Implementing Rules**”), *Circular of the State Administration of Foreign Exchange on the Relevant Issues Regarding the Pilot Measures on Domestic Securities Investment by RMB Qualified Foreign Institutional Investors for Fund Management Companies and Securities Companies* (the “**SAFE Circular**”) and *Circular of the People’s Bank of China on the Relevant Issues Regarding the Pilot Measures on Domestic Securities Investment by RMB Qualified Foreign Institutional Investors for Fund Management Companies and Securities Companies* (the “**PBOC Circular**”, together with the CSRC Implementing Rules and the SAFE Circular, collectively, the “**Supporting Regulations**”), which specified the relevant issues of the Pilot Measures.

The promulgation and implementation of the Pilot Measures and its Supporting Regulations have provided detailed guidelines for launch of the pilot program of domestic securities investment by RQFII (the “**RQFII Pilot Program**”), which will play a significant role in the acceleration of the backflow of offshore RMB funds, the internationalization of RMB as well

as the development of domestic capital market. We set out below the general introduction and analysis of the Pilot Measures and the Supporting Regulations.

1. Applicant and Qualifications Applicable to RQFII Pilot Program

Pursuant to the Pilot Measures, so far only the Hong Kong subsidiaries of domestic fund management companies and securities companies are allowed to apply for RQFII (the “**HK Subsidiary**”).

The Pilot Measures also specifies the following qualifications of RQFII for a HK Subsidiary to invest in domestic securities market with RMB funds raised in Hong Kong shall satisfy the following conditions: (i) it has obtained the asset management business license (i.e., Type 9 License) issued by the Hong Kong securities governmental authority and has already operated the asset management business with stable and healthy financial conditions and good credit; (ii) it has effective corporate governance and internal control and its staff meet such qualification requirements as required in Hong Kong; (iii) both of such Hong Kong Subsidiary and its domestic parent company have been legally operating their business and neither of them is subject to any serious penalties imposed by the local competent governmental authorities in the past 3 years; (iv) its domestic parent company has obtained the license for securities asset management business; and (v) any other conditions required by CSRC based on principle of prudence.

2. Governmental Authorities in Charge of RQFII Pilot Program and Their Respective Responsibilities

Pursuant to the Pilot Measures and its Supporting Regulations, CSRC, the PBOC and SAFE are the main governmental authorities in charge of the RQFII Pilot Program, among which, CSRC shall be mainly responsible for the supervision and administration of domestic securities investment by Hong Kong Subsidiaries, while the PBOC for the administration of opening domestic RMB bank accounts by Hong Kong Subsidiaries and SAFE for investment quota administration on Hong Kong Subsidiaries. In addition, the PBOC, together with SAFE, will also monitor and administer capital inflow and outflow.

3. Approval Procedures for RQFII

According to the Pilot Measures, a Hong Kong Subsidiary shall (i) apply with CSRC for the qualification of RQFII Pilot Program; and (ii) apply with SAFE for its investment quota.

(a) Approval for RQFII Qualification

In order to apply for the RQFII qualification, a Hong Kong Subsidiary should submit such application documents to CSRC as set forth in Article 7 of the Pilot Measures. Within 60 days upon receipt of the completed application documents, CSRC will then decide whether

or not to grant the RQFII qualification. If granted, CSRC should issue the approval letter in writing as well as the operating permit for securities investment (the “**Operating Permit**”).

(b) Approval for Investment Quota

The Hong Kong Subsidiary obtaining the RQFII qualification (the “**RQFII Pilot Institution**”) will need to submit the application documents to SAFE as set forth in Article 8 of the Pilot Measures to apply for its investment quota. Within 60 days upon receipt of the completed application documents, SAFE will then decide whether or not to grant the investment quota. If approved, SAFE should issue the approval letter in writing as well as the registration permit. It is reported that the total amount of investment quota for RQFII Pilot Program will be RMB20 billion at the early stage.

4. Domestic Investment by RQFII Pilot Institutions

The Pilot Measures and its Supporting Regulations have provided the following specific rules to govern the investment activities in domestic securities market by RQFII Pilot Institutions:

(a) Type of Securities Allowed for Investment

It is provided under the CSRC Implementing Provisions that an RQFII Pilot Institution is allowed to invest, within its approved investment quota, in stocks, bonds, warrants, securities investment funds listed or traded in stock exchanges and such other securities as permitted by CSRC and the PBOC.

(b) Investment Portfolio Requirement

Pursuant to the CSRC Implementing Rules and the PBOC Circular, an RQFII Pilot Institution will need to meet the following requirements on its investment portfolio: within its approved investment quota, the funds for investment in stock or stock securities investment funds should be no more than 20% of the total amount of the funds raised, while the funds for investment in fixed-income securities (including various kinds of bonds and fixed-income securities investment funds) should be no less than 80% of the total amount of funds raised. CSRC and the PBOC may have the right to adjust such investment portfolio requirement based on principle of prudence.

(c) Information Disclosure

According to the Pilot Measures and CSRC Implementing Rules, when conducting investment in domestic securities market, an RQFII Pilot Institution should be in compliance with the general rules under applicable PRC laws and regulations with respect to shareholding ratio and information disclosure as well as other regulatory requirements (e.g., in the event that the domestic securities investment by an RQFII Pilot Institution triggers the information disclosure requirements, as the obligor of information disclosure, it should

submit the contents of information disclosure to stock exchange).

In addition to the above-mentioned compliance requirement on information disclosure, an RQFII Pilot Institution shall report to CSRC, the PBOC and SAFE in the event of any change of its onshore custodian and chair person, shareholding restructuring, increase or decrease of its registered capital, merger or consolidation with any other institution, involvement in any material litigations and any other major event, being subject to any serious penalty overseas and any other circumstance specified by CSRC, the PBOC and SAFE.

It is noteworthy that each of CSRC, the PBOC and SAFE may require an RQFII Pilot Institution, its onshore custodian, securities companies and other institutions to provide the relevant materials with respect to such RQFII Pilot Institution, and conduct necessary inquiry and examination.

(d) Entrustment of Securities Companies

Pursuant to the Pilot Measures and the CSRC Implementing Rules, an RQFII Pilot Institution is required to entrust domestic securities companies for securities trading. Each RQFII Pilot Institution may entrust no more than 3 domestic securities companies in Shanghai Stock Exchange and Shenzhen Stock Exchange respectively for securities trading. Additionally, an RQFII Pilot Institution may also entrust domestic fund management companies and securities companies to manage its domestic securities investment.

5. Asset Custody

(a) Custodian

It is required under the Pilot Measures that an RQFII Pilot Institution should entrust a domestic commercial bank with the custodian qualification for qualified foreign institutional investors (the “**Custodian**”) to deal with the asset custody. The main duties of the Custodian include: (i) to maintain all assets entrusted by RQFII Pilot Institutions; (ii) to supervise the operation of RQFII Pilot Institutions in domestic securities investment; (iii) to deal with capital inflow and outflow for RQFII Pilot Institutions; (iv) to make statistics declaration of the payment balance in accordance with relevant provisions; (v) to submit relevant business reports and statements to CSRC, the PBOC and SAFE; and (vi) to perform other duties specified by CSRC, the PBOC and SAFE based on principle of prudence.

(b) Opening Bank Accounts

Pursuant to the PBOC Circular, an RQFII Pilot Institution will need to select a domestic commercial bank (the “**Custody and Settlement Bank**”) with custodian qualification for both qualified foreign institutional investors and settlement agent qualification for inter-bank bond market concurrently to open a foreign institution RMB basic deposit account (the “**Basic**

Deposit Account”) and a foreign institution RMB special deposit account (the “**Special Deposit Account**”). Unless otherwise provided by the PBOC, a RQFII Pilot Institution is not allowed to open ordinary deposit accounts or non-temporary deposit accounts.

With respect to the Special Deposit Account, an RQFII Pilot Institution can open three types of Special Deposit Accounts in a Custody and Settlement Bank for the purpose of stock trading, inter-bank bond trading, stock exchange bond trading, respectively. Transfer of funds is allowed among such three types of Special Deposit Accounts. However, fund transfer is forbidden between any Special Deposit Account and the Basic Deposit Account, and no cash can be drawn from any Special Deposit Account.

The scope of incomes under the Special Deposit Accounts of an RQFII Pilot Institution generally cover investment principal remitted from outside of China by an RQFII Pilot Institution, capital gain by selling securities, cash dividend, interest income and other income provided by the PBOC, the scope of payment under the Special Deposit Accounts of an RQFII Pilot Institution generally cover funds used to buy securities, principal and capital gain and other payments provided by the PBOC.

Besides, it is also provided under the PBOC Circular that if an RQFII Pilot Institution sets up open-ended securities investment funds, each such open-ended securities fund should open a separate Special Deposit Account.

6. Administration of Foreign Exchange

According to the SAFE Circular, SAFE adopts balance administration for RQFII’s investment quota. The aggregate amount of RMB funds remitted into China by an RQFII Pilot Institution should be capped at its approved investment quota, and such quota should not be transferred to any other institution or individual.

In addition, it is specified in the SAFE Circular that an RQFII Pilot Institution should entrust its Custodian to proceed with the capital inbound and outbound remittance as well as purchase of foreign exchange. Meanwhile, the Custodian should review the authenticity and compliance on the corresponding capital remittance as well as collection and payment of funds, and submit relevant statements to SAFE in accordance with the requirements under the SAFE Circular.

7. Other Noteworthy Issues

Pursuant to the Pilot Measures and its Supporting Regulations, an RQFII Pilot Institution failing to submit the investment quota application to SAFE within 1 year after obtaining the Operating Permit should return the Operating Permit to CSRC. Further, if an RQFII Pilot Institution fails to effectively use its investment quota within 1 year upon approval of the investment quota, SAFE is entitled to adjust or reduce the investment quota or even revoke

the quota based on the then-applicable circumstances.

8. Conclusion

The promulgation and implementation of the Pilot Measures and its Supporting Regulations will make domestic capital market more open, stimulates the development of international business by domestic securities institution, optimizes the backflow mechanism of RMB funds, and further push forward the internationalization of RMB. However, for the purpose of protecting the domestic capital market from the adverse impact to be caused by the huge inflow of overseas hot money and other factors, the governmental authorities took a prudent attitude towards RQFII's scale, investment scope and portfolio. The total amount of initial investment quota for RQFII Pilot (i.e., RMB20 billion) equals to approximately 3.2% of the RMB deposits in Hong Kong which is RMB 627.3 billion as stated by Hong Kong Monetary Authority as of November 2011. Furthermore, compared with the A-Share market with a total market value of RMB25 trillion and an average daily turnover of RMB174.4 billion in 2011, the funds permitted to invest in stock market (i.e., no more than RMB4 billion) based on portfolio requirement (i.e., 20% of the total investment quota) is negligible. Comparatively, the current total investment quota for qualified foreign institutional investors ("QFII") is USD21.6 billion (or RMB136 billion), among which approximately 40% has been invested in stock market. It can be foreseen that there is a huge room for RQFII's future development.

According to the information recently released by CSRC, RQFII Pilot Program develops smoothly as of the date hereof. 9 fund management companies and 12 securities companies have been granted the RQFII qualification as well as the investment quota. In addition, the relevant governmental authorities are considering further expanding the scale of RQFII Pilot Program, trying to achieve breakthroughs in the areas of institution forms, investment scope and investment portfolio. Meanwhile, CSRC is actively researching the feasibility of RQFII Pilot Institutions to issue RMB-denominated A-Share ETF products as well as the issuance of RMB-denominated bonds and stocks by H-Share companies. We will continue to keep an eye on the latest development of RQFII Pilot Program and other RMB cross-border investment and will give you an update in a timely way.

Important Announcement

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If you have any questions regarding this publication, please contact **James Wang, Head of Fund Formation & Management (+86-10-8525 5553; james.wang@hankunlaw.com)**, or any of the following Han Kun lawyers:

Contact Us

Beijing Office

Tel.: +86-10-8525 5500
Suite 906, Office Tower C1, Oriental Plaza
No. 1 East Chang An Ave.
Beijing 100738, P. R. China

Estella CHEN Attorney-at-law

Tel.: +86-10-8525 5541
Email: estella.chen@hankunlaw.com

Shanghai Office

Tel.: +86-21-6080 0909
Suite 5709, Tower 1, Plaza 66, 1266 Nanjing
West Road,
Shanghai 200040, P. R. China

Anita SUN Attorney-at-law

Tel.: +86-21-6080 0907
Email: anita.sun@hankunlaw.com

Shenzhen Office

Tel.: +86-755-3680 6500
Suite 4709, Excellence Times Plaza, 4068
Yitian Road, Futian District,
Shenzhen 518048, P. R. China

Jason WANG Attorney-at-law

Tel.: +86-755-3680 6518
Email: jason.wang@hankunlaw.com