



**SECURITIES AND
FUTURES COMMISSION**
證券及期貨事務監察委員會

Funds and ILAS

13-17 July 2009

Connie Lo
Manager, External Relations

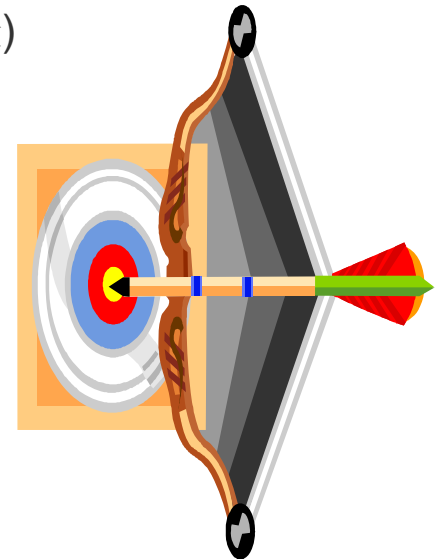
What are Funds?

■ Funds

- Collective investment schemes (集體投資計劃)
- Managed by fund management companies according to investment objectives

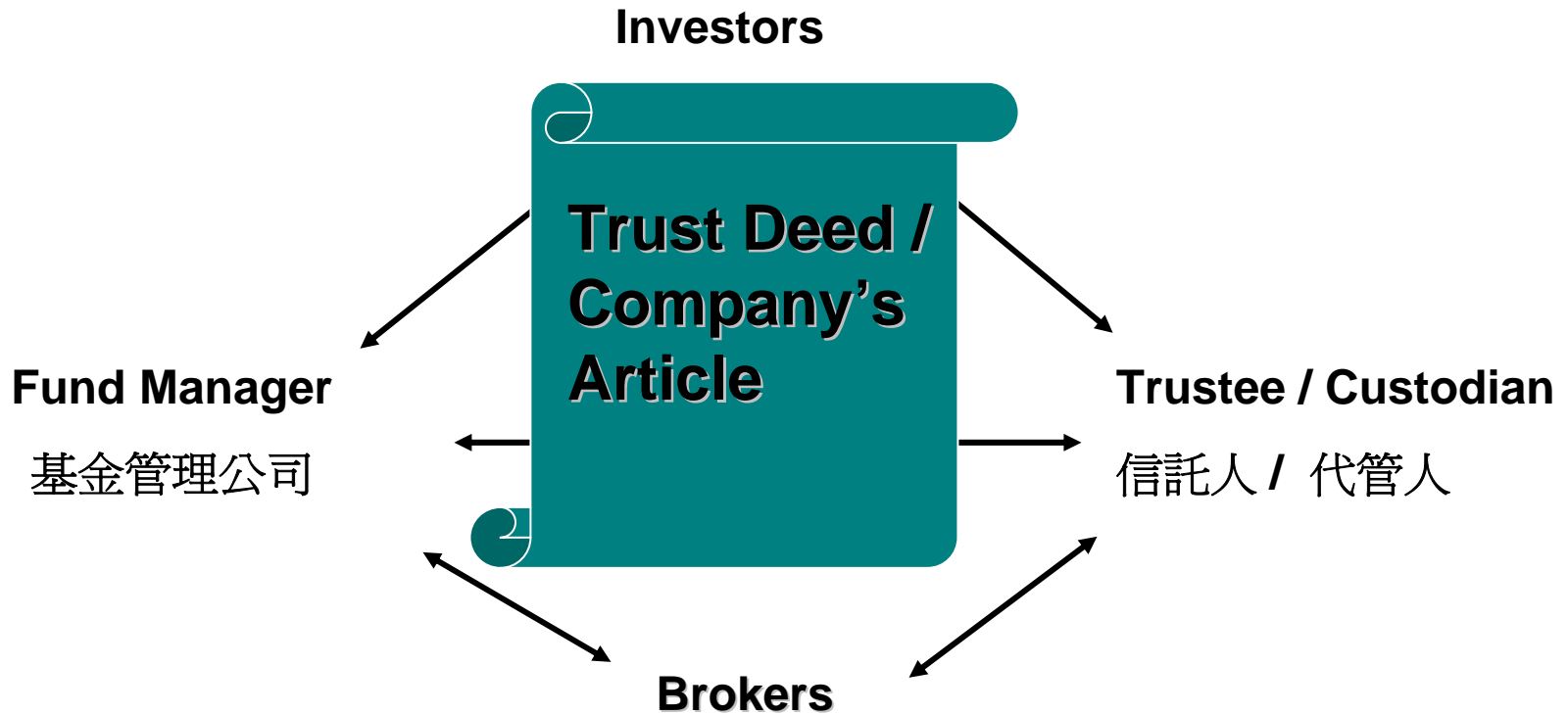
■ Mutual Funds vs Unit Trusts

- Mutual Funds (互惠基金) : Limited liability companies (有限責任公司)
- Unit Trusts (單位信託基金) : Trust structures (信託)



What are Funds?

- Structure

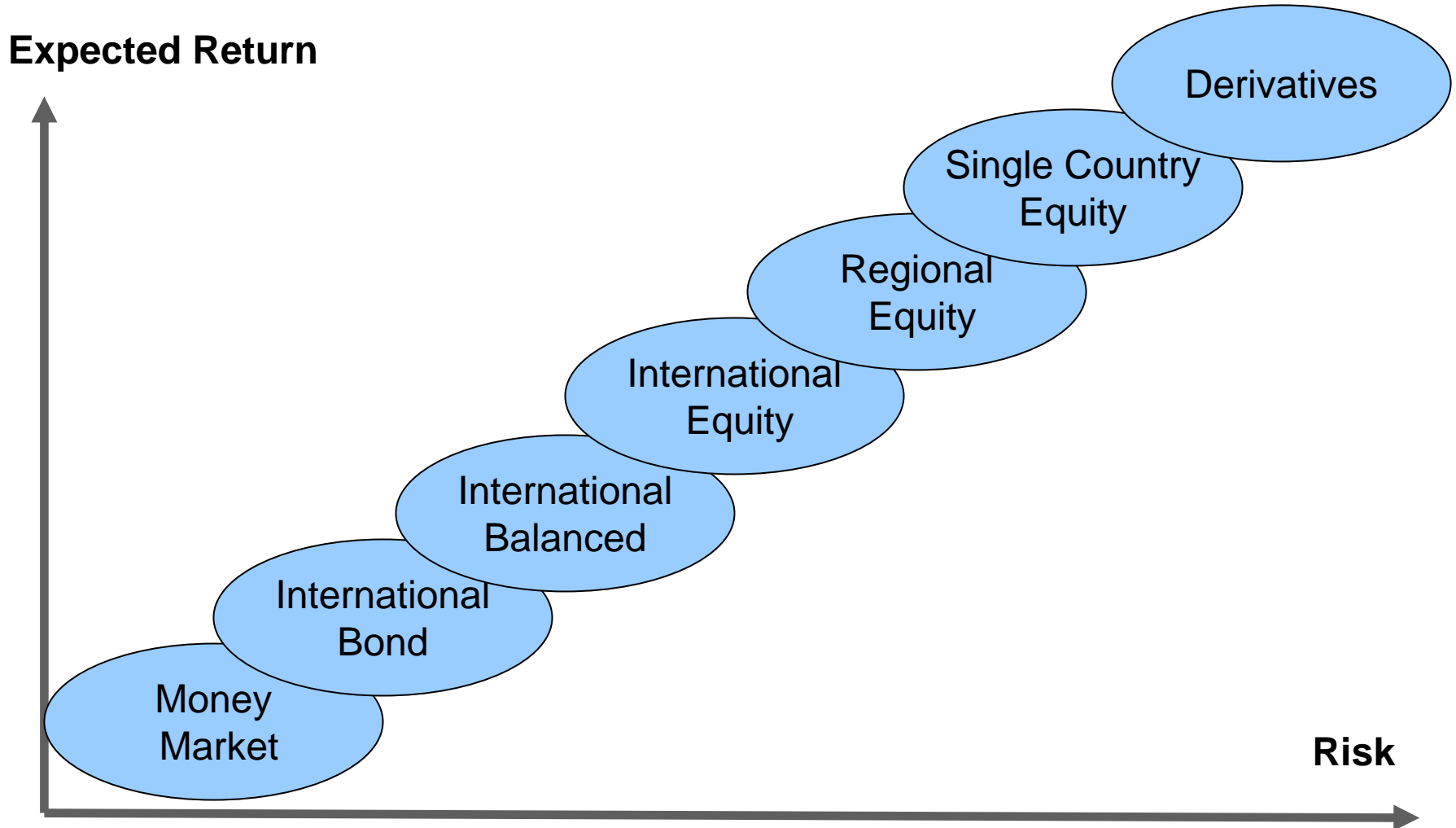


Categories of Funds

- **Open-ended vs Closed-ended**
- **Open-ended Funds (開放式基金)**
 - Size of fund fluctuates
 - Subscription and redemption facilities available
 - Trade at prevailing fund prices
- **Closed-ended Funds (閉端式基金)**
 - Size of fund cannot increase
 - Limited offering period
 - Fixed offer price during the offering period



Risk Levels of Funds



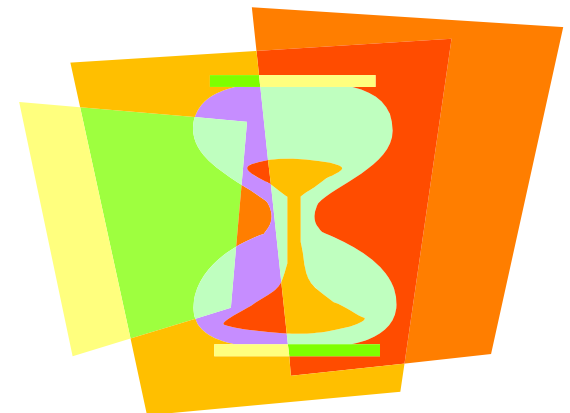
Dealing

- **Frequency**

- Daily / Weekly / Bi-weekly

- **Pricing Method**

- Forward Pricing (未知價) : Deal in unknown price
- Historical Pricing (已知價) : Deal in the price of the previous valuation day



Fees & Charges

- **Deducted directly from fund assets**
 - Management Fee
 - Trustee, Custodian and Auditor Fee
 - Brokerage Commissions
- **Payable by the unitholders**
 - Initial Charge (認購費)
 - Redemption Charge (贖回費)



Fees & Charges

Fund Type	Initial Charge	Annual Management Fee
Money Market	0%-2%	0.25%-1%
Bond	3%-5%	0.5%-1.5%
Equity	5%-6%	1%-2%

Source : HKIFA

Calculation of Prices

- Net Asset Value (NAV 資產淨值)

$$\begin{aligned} &= \frac{\text{Total fund assets - fees \& charges}}{\text{Total no. of units / shares}} \\ &= \text{Bid Price (買入價 / 贖回價)} \\ &\quad \text{(if no redemption charge)} \end{aligned}$$



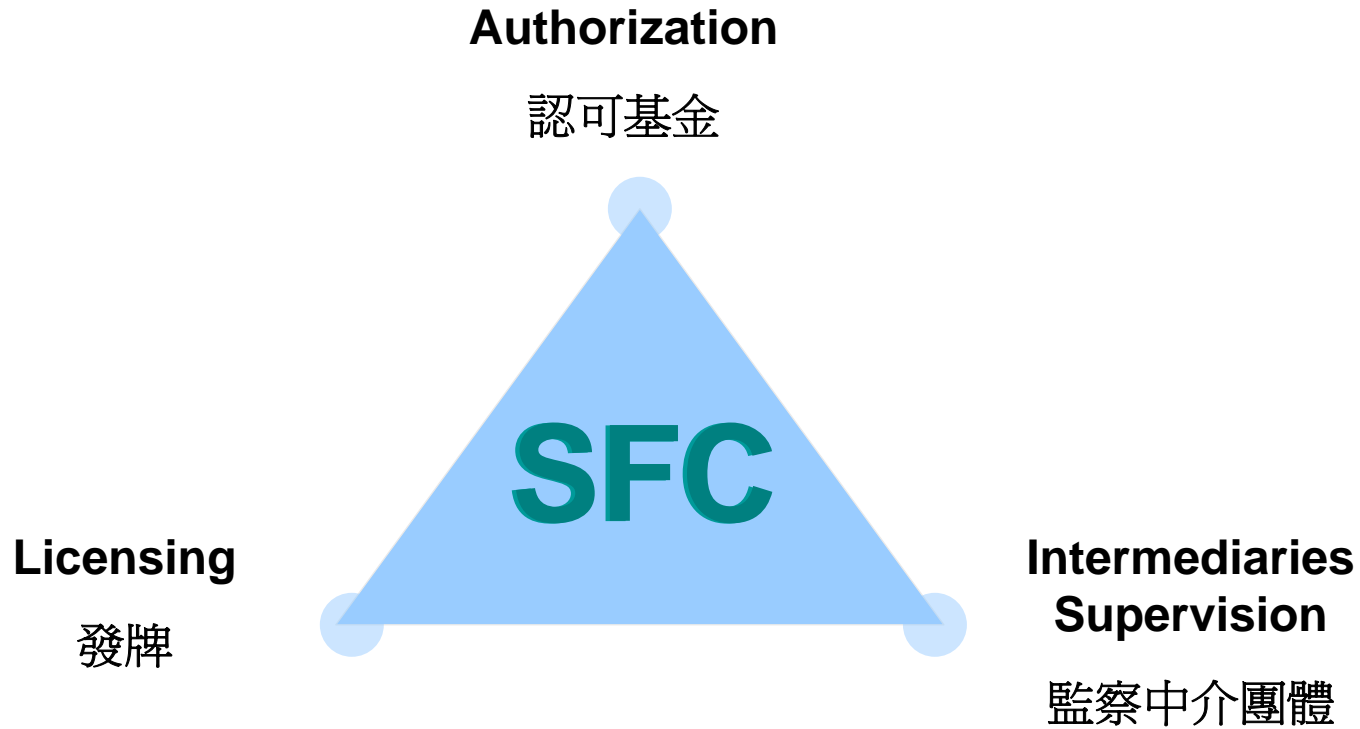
Calculation of Prices

$$\begin{array}{l} \text{Offer Price} \\ \text{賣出價 / 認購價} \end{array} = \frac{\text{NAV}}{1 - \text{initial charge}}$$

E.g. Initial charge = 5%, NAV = HK\$10.00

$$\begin{aligned} \text{Offer price} &= \text{HK\$10.00} / (1 - 0.05) \\ &= \text{HK\$10.53} \end{aligned}$$

SFC's Regulatory Role



Why SFC Authorization?

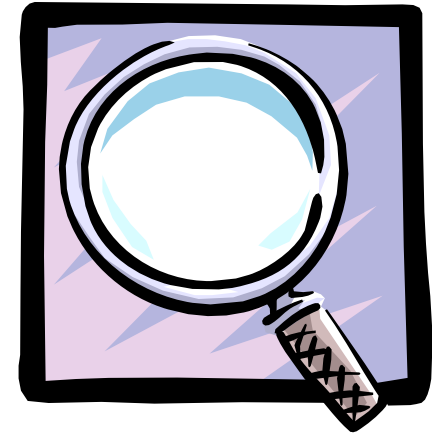
- **Securities and Futures Ordinance**
- **Empowers the SFC to authorize funds**
- **Prohibits the promotion of unauthorized funds to the Hong Kong public**
 - Fine of HK\$500,000 and
 - Imprisonment of 3 years



What is Authorization?

- **SFC's authorization seeks to ensure:**
 - Adequate built-in safeguards in the fund structure
 - Sufficient information disclosure

- **Authorization requirements mainly cover:**
 - Eligibility of fund manager
 - Appointment of a trustee / custodian to hold assets independently
 - Well defined investment policy and appropriate restrictions to ensure diversification and liquidity
 - Proper dealing and price calculation procedures
 - Accurate information disclosure in offering document and marketing materials



Authorization = Endorsement?

- **SFC authorization does not mean recommendation of that fund**
- **Investing in an authorized fund does not necessarily mean a profit will be made**



Documents for Investors

- **Before Investment**

- Fund prospectus / Explanatory memorandum
- Latest audited annual report
- Latest unaudited semi-annual report
- Application form

- **After Investment**

- Contract note
- Monthly statement



Deauthorization

- **A fund may apply for deauthorization when it no longer targets the Hong Kong public**
- **SFC has the right to de-authorize an authorized fund in case of any breach of the Code on Unit Trusts & Mutual Funds**

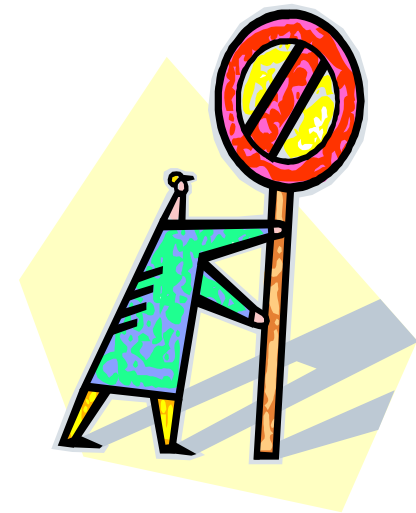
Suspension 暫停買賣

- Occurs on market closure, difficulties in valuing 10% of NAV in a fund, ...
- Decision taken by fund manager, in consultation with the trustee
- Notify holders in newspapers / on the website of the fund manager / by letters
- Immediate notification to the SFC



Merger & Termination 合併及結束

- **Conditions set out in constitutive documents**
 - Typical reasons : Fund size becomes too small
- **Situations not set out in constitutive documents**
 - Example : Business decision
- **Must follow the legal process of liquidation**
- **Holder should be offered options**



Regulation of the Fund Industry

- **All parties involved in selling / providing investment advice on funds in Hong Kong**
 - Fund houses
 - Fund managers
 - Retail sales staff
 - Investment advisers
 - (For banks, their front-line regulator is the HKMA)



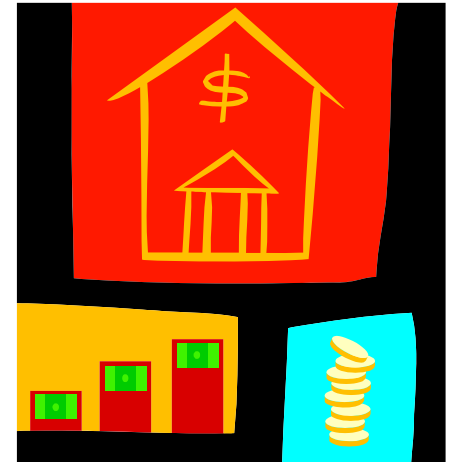
Fund Dealing Channels:

Direct Sale - Pros & Cons

- **Channel : Fund Management Companies /
Hong Kong Representatives**
- **Pros**
 - Direct contractual relationship
 - First hand information
- **Cons**
 - Deal with only one fund management company at a time
 - Restricted choices

Fund Dealing Channels: Agent Sale - Pros & Cons

- **Agent : Investment Advisors / Banks**
- **Pros**
 - Less paper work
 - Provides advice on selection of funds offered by different fund management companies
- **Cons**
 - Unable to obtain first hand information from fund management companies
 - Choices restricted to funds sold by that intermediary



Fund Dealing Channels: Agent Sale - Pros & Cons

- **Agent : Investment Advisors / Banks**

- **Legal title of fund units**
 - Investor's own name
 - Nominee's name (代名人義)
 - No direct contractual relationship with the fund management companies
 - May have to pay additional handling charges for the nominee services

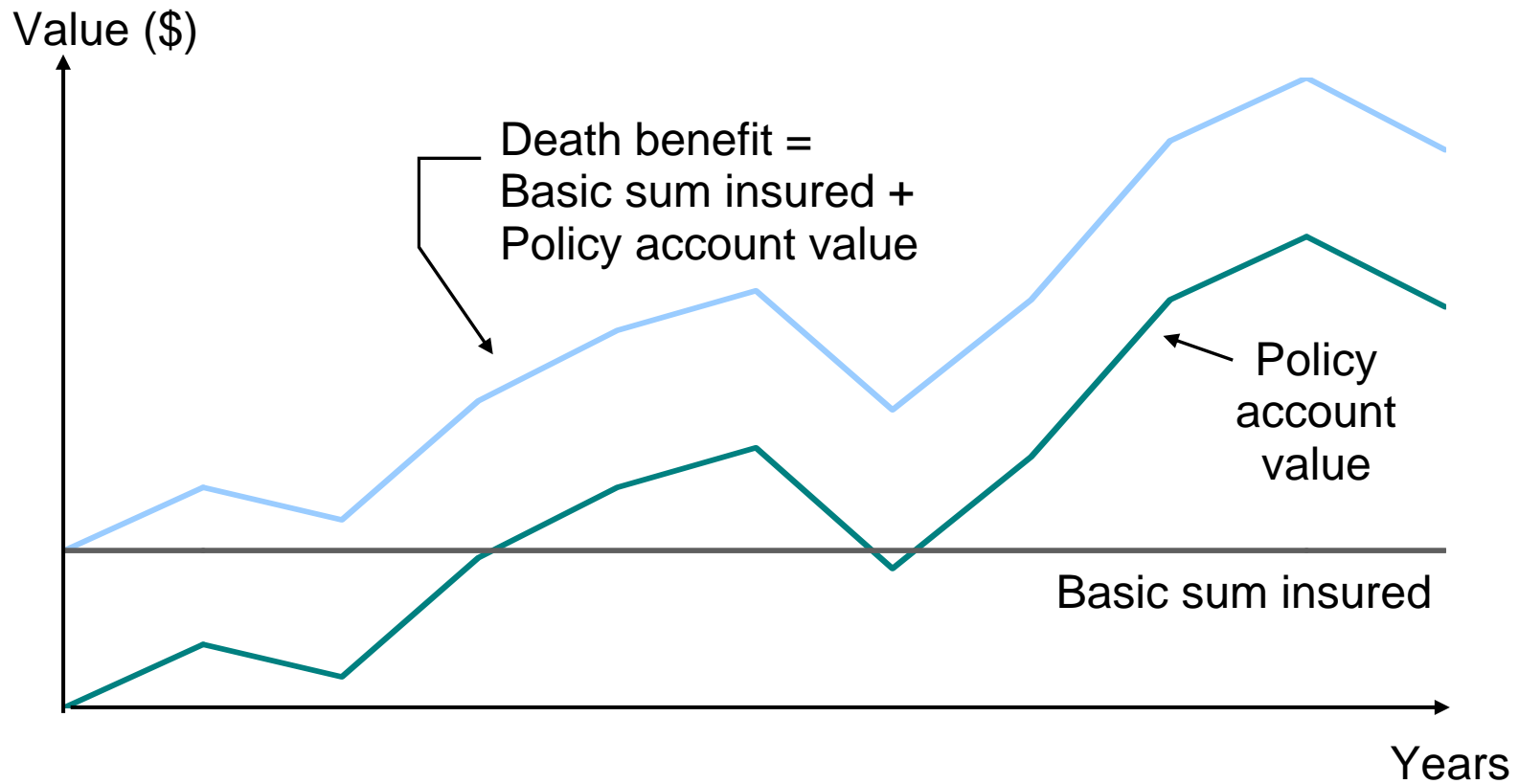
What is an ILAS?

- Life insurance policies with benefits linked to the performance of your selected investment options, e.g. funds
- Policy holders are not investing in any underlying assets of the investment option and hence have no rights or claims in any of the assets of the insurance company
- Pays a lump sum at the beginning / A premium on a regular basis
- Capital + / - Accumulated returns → Investor on maturity
- Lump sum → Beneficiary if policy holder dies within the term of the scheme



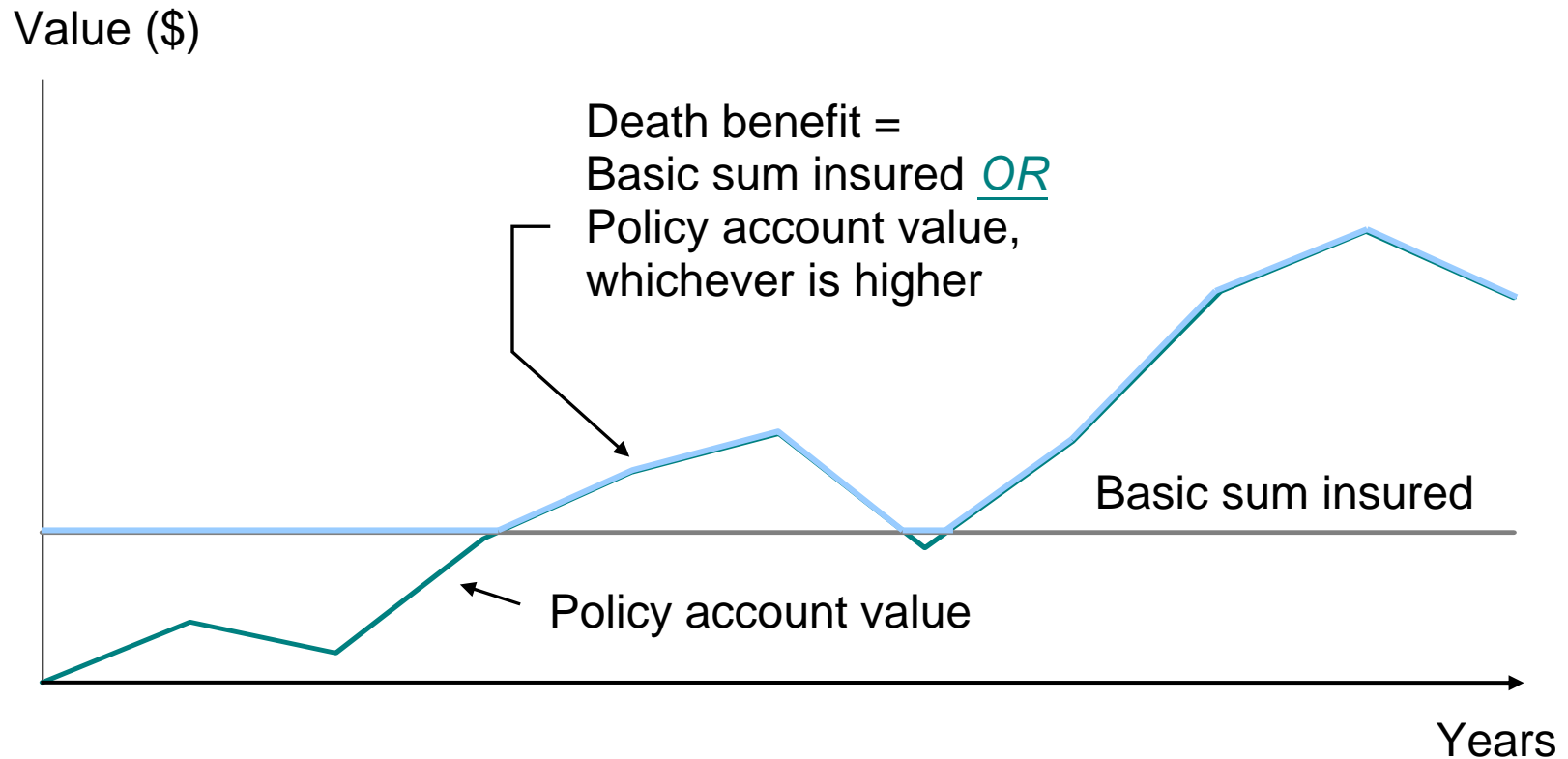
Modes of Death Benefit

- Increasing benefit (遞增賠償)



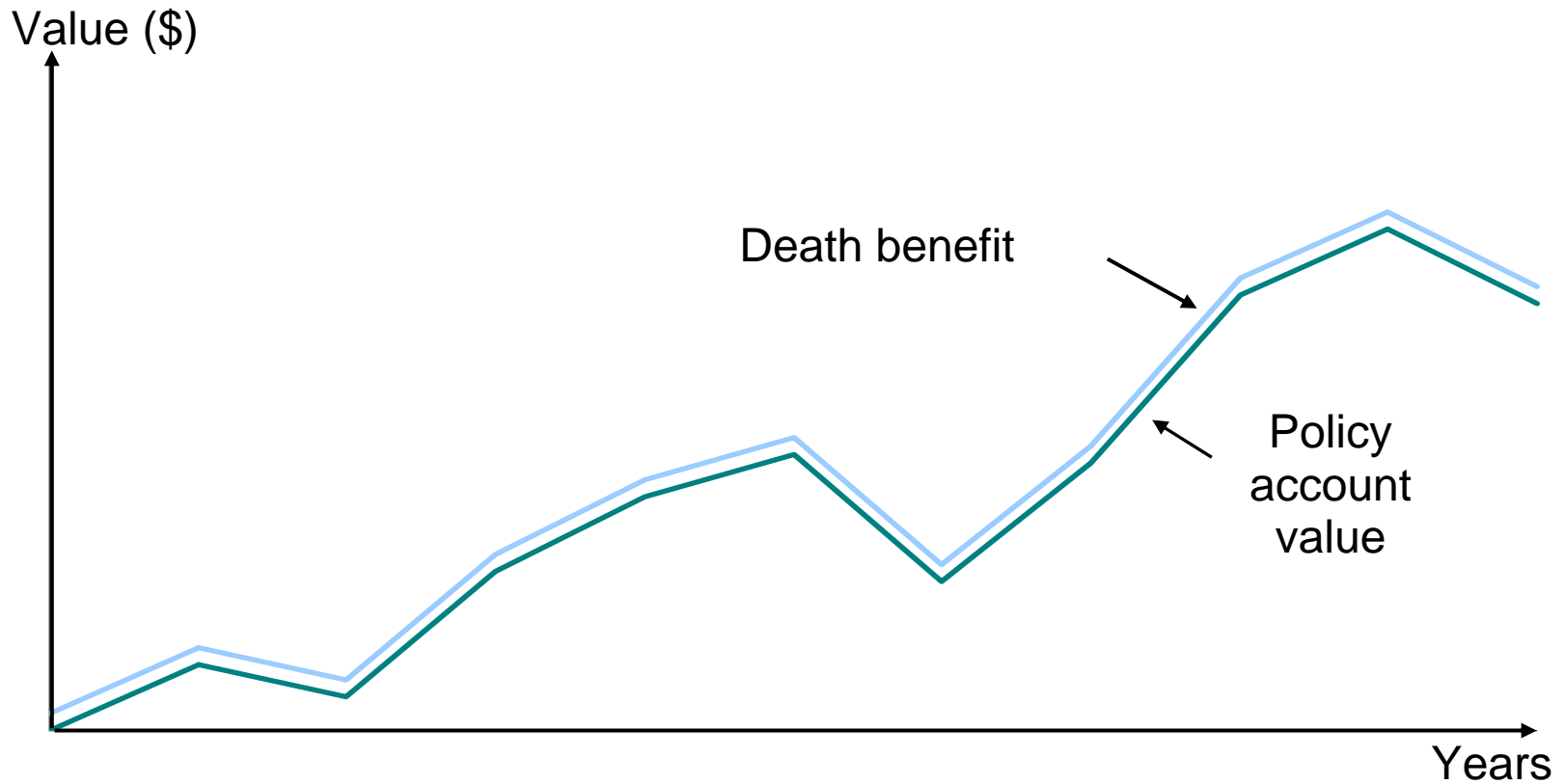
Modes of Death Benefit

- Level benefit (固定賠償)



Modes of Death Benefit

- 101 plan (101 計劃)



Benefits / Considerations of Investing in an ILAS

■ Benefits

- Provide life protection as well as investment opportunities in funds
- Regular contributions create a dollar-cost averaging (成本平均化) effect

■ Considerations

- The insurance company owns the assets that you put into an ILAS, you do not own any underlying assets of an ILAS
- Often have heavy fee loadings at the early stages of the term / Premature encashment may attract a heavy penalty
- Early surrender value may be significantly smaller than the money invested

Fees & Charges of an ILAS

■ Policy Level

- Initial charge (初期費)
- Surrender charge (退保費用)
- Withdrawal charge (提款費)
- Insurance charge (保險費用), administration charge (保單行政費)

■ Fund Investment Level

- Similar to those of retail investment funds, e.g. initial charge, fund management fee, switching charge

Regulation on ILAS

- **Product**

- ILAS & marketing materials must obtain SFC's authorization before selling to HK public

- **Issuer Insurance Co & Selling Intermediaries**

- Insurance Authority / self-regulatory bodies within the insurance industry
- Depending on activities & services provided, some insurance intermediaries are also licensed with the SFC



Protective Measures to ILAS Investors

- Principal brochure
- Illustration document (退保説明文件)
- Cooling-off period (冷靜期)



Principal Brochure

- **Name of the ILAS**
- **Investment objectives & strategies**
- **Calculation of investment returns**
- **Fees & charges**
- **Details of the guarantee, if any**
- **Name of the HK representatives**
- **Available in Chinese & English**



Illustration Document

- **Based on 2 assumed rates of return**
- **Demonstrates the projected surrender values over the term of the ILAS: the sum on redemption net all fees & charges at the end of the first 5 years, & for every 5th year until maturity**
- **Requires the signing of the investor to confirm understanding**

The rates used are HYPOTHETICAL!

Cooling-off Period

- **Enables investors to rethink purchase decision**
- **The Period (whichever is later):**
 - 14 days after the issue of the ILAS OR
 - 21 days after the date on which the application form is signed OR
 - 5 days after the date of a notice issued by the insurance company informing investors of the availability of the ILAS & the expiry date of the cooling-off period



Qs to Ask Before Investing in an ILAS

- How is the death benefit structured?
- Do the fund options suit your investment needs?
- How long do you have to contribute?
- What is the charge structure?
- What options do you have if you need instant cash? Partial withdrawal? Contribution holidays? Policy loan?
- Will reducing your contribution amount attract a penalty? How about stopping contribution or redeeming before the end of the term?



Class Activities

Activity 1

- Click the following hyperlink to show students a video alerting common fallacies about funds, then remind students the importance of reading fund documents to make informed decisions
 - SFC’s InvestEd website: [2. Common fallacies about managed funds](#)

Activity 2

- Click the following hyperlink to show students a sample of an illustration document, then highlight the functions of this document
 - SFC’s InvestEd website: [Illustration Document](#)

Thank you

SFC Website: www.sfc.hk

InvestEd Website: www.InvestEd.hk