

“Marketing In And From” Hong Kong: A Regulatory Case Study



CATHY BRAND
12 April 2023

Cross-border marketing of funds is an important topic that wealth managers, private banks and others must wrestle with. This article examines what happens in Hong Kong.

*Here is another article on matters concerning marketing alternative investment funds across specific jurisdictional borders. The article comes from **Sales Road Maps Online**, a UK-based group that has provided a number of expert commentaries in these pages. The author here is Cathy Brand, the firm's CEO. The editors are pleased to share this content and invite responses. The usual editorial disclaimers apply. Email: tom.burroughes@wealthbriefing.com*

Setting up regional marketing affiliates

Many alternative investment fund managers/asset managers begin their international fundraising efforts by conducting cross-border marketing from their home office headquarters. As their business develops over time, it makes commercial sense to set up affiliates outside their own home jurisdiction that can conduct marketing and client servicing activities from a regional hub.

By way of example, clients have asked us over the years: “We want to set up a new office in the Asia region to conduct fundraising in our funds from investors in that region. If we put our sales teams on the ground in Hong Kong to cover region Asia marketing, can the sales team market and sell our funds in Hong Kong and in the surrounding Asia region without licence registration with the local regulator, Hong Kong Securities & Futures Commission?”

To answer this question, we provide a background on licensing as it pertains to fund marketing activities.

Why get a licence to fundraise?

Marketing funds in any jurisdiction constitutes a regulated activity and is subject to the country's marketing regulations as well as licensing rules. You need a licence in order to conduct fund marketing/fundraising in any jurisdiction or to operate in that country under exemptions (if available) from the regulator's fund marketing licence requirements. All licensing regulations should be confirmed in advance of any fund marketing activity.

We always advise clients to check with local counsel as to which type of licence they may need, depending on their activity set conducted in that jurisdiction. For example, in Hong Kong there are various types of SFC licences available depending on the specific activities of the AIFM/asset manager and their sales teams.

The “truth” about AIFM/asset manager sales activities

What do sales teams do? They market and sell your funds. That is what they are paid to do.

It is a myth to think that AIFMs/asset managers can put sales teams on the ground in a new office/affiliate overseas without crossing the line of “fund solicitation,” a regulated activity subject to a licence (or operation under a licence exemption).

We have heard of some industry players who put sales teams on the ground in foreign jurisdictions, attempting to avoid triggering local licensing registration and compliance by “flying under the regulatory radar”: calling their local sales team’s activities only “investment capabilities presentations,” “brand awareness,” “research,” “client servicing,” “completing Requests for Proposals (RFPs)” and/or conducting “reverse solicitation.”

It is very difficult to keep sales teams in a box called “general capabilities” without speaking about your fund to potential investors. It is a very easy line to cross.

Secondly, regulators such as Hong Kong SFC apply the **substance test** to any activity that is conducted onshore in their jurisdiction. You can say your sales teams on the ground in Hong Kong are only doing “brand awareness” or “reverse solicitation.” However, be prepared for the local regulator to “**pierce the veil**” and take an in-depth look at the activities conducted by sales teams onshore in their jurisdiction. This is to check whether a regulated activity is conducted or not and whether you need a licence to conduct that regulated activity.

Case study: Hong Kong

Assuming that your local sales team activities from your office in Hong Kong include solicitation of the AIFM/asset manager’s funds to investors in Hong Kong and/or to investors outside Hong Kong (but conducted from Hong Kong), your local Hong Kong affiliate must apply for a Type 1 licence for “dealing in securities” from SFC.

Global Sales Compliance (GSC) has worked with AIFM/asset managers to set up a local affiliate in Hong Kong in order for the affiliate to market their funds to Hong Kong investors as well as service their region Asia client base.

Working with our Hong Kong legal counsel, we managed the project to register the client’s Hong Kong affiliate with the regulator Hong Kong SFC, to apply for the client’s Type 1 licence for “dealing in securities”. This license enables the client to market their funds “*in and from*” Hong Kong.

What is the concept of regulating “marketing in and from” Hong Kong?

Let’s assume that the AIFM/asset manager’s local office in Hong Kong applies for and receives its Type 1 SFC licence, permitting the local sales teams to conduct fund solicitation, a regulated activity that is subject to licence in Hong Kong.

Typically in most jurisdictions, when you get a licence to conduct fund solicitation (for dealing in securities, broker-dealer licence or other fund marketing licence according to local rules), the local regulator regulates your marketing activities in that jurisdiction where you have a licence. There may be some general questionnaires sent to licence registrants that ask the licensee to confirm that they comply with other country’s laws outside the principal jurisdiction of the licence, but the regulator’s compliance enquiry typically stops at the country’s borders where you are licensed.

Not so in Hong Kong.

Marketing “in Hong Kong”: Hong Kong SFC regulates your fund marketing activities to investors “in Hong Kong,” applying the fund marketing compliance rules according to your licence type. For example, if your Type 1 licence enables you to deal only with professional investors (there are 13 categories of professional investors), then you can only market your funds to professional investors in Hong Kong.

Marketing “from Hong Kong”: For Type 1 licence holders, Hong Kong SFC also regulates your marketing activities conducted “from Hong Kong” into other jurisdictions outside Hong Kong. This translates to 2-level regulatory scrutiny: application of Hong Kong regulatory requirements to clients outside Hong Kong if you conducted the activity from Hong Kong.

Is this extraterritorial application of Hong Kong's rules applicable to other countries?

Some would argue, yes. Some would argue that SFC's regulation application to other country's marketing rules could be viewed as "regulatory overreach." Others would argue that SFC holds its Type 1 licensees to a very high standard of compliance with Hong Kong's and other country's marketing regimes.

How do Hong Kong SFC's rules apply to you?

If you have a Type 1 licence for "dealing in securities" from Hong Kong SFC, be prepared for onsite visits by SFC auditing your books and records: You must prove to SFC that you comply with fund marketing regulations "in Hong Kong," prove you comply with all country marketing rules outside Hong Kong and prove you have applied Hong Kong's regulations to all clients you deal with outside Hong Kong if you marketed to them "from Hong Kong."

SFC regulatory enforcement: Hong Kong SFC is known to be an ever-vigilant regulator, ready to enforce Hong Kong's regulations at all times, especially to protect its individual investors.

Take SFC seriously: Any country regulator in perpetual enforcement mode could potentially put your business franchise and reputation at risk.

Summary: For some AIFM/asset managers, setting up regional affiliates to market and sell their funds as well as service regional clients makes sense for commercial and regulatory reasons.

Don't think you can put sales teams on the ground to market your funds without checking the local country's licencing requirements first. And if you want to set up your Asia region sales team in Hong Kong, you need to know what to expect in terms of SFC licensing requirements. And you need to understand how your SFC licence permissions will impact not just your Hong Kong fundraising approach but also your regional fundraising strategy.

Regulating "marketing in and from": a trend to come from other national regulators?

We're monitoring it.