HKVCA 私投募資
香港創業及私募投資協會
The Association for Private Capital in Asia

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Head, Market Development
Hong Kong Monetary Authority
55th Floor, Two International Finance Centre
8 Finance Street, Central
Hong Kong

Dear Kenneth,

Comments on Guideline on Auditor's Report for Application for Certification of Funds Issued by the Monetary Authority for Funds and their Investment Managers

HKVCA appreciates the Monetary Authority consulting the industry on the matters of application for certification of funds. We are pleased that we can be helpful to provide practical and useful recommendations. Given the process of the certification for application of the carried interest concession has been ongoing for several months, we want to stress that unless the process is transparent and simple, we are afraid that industry take-up of the concession will be low. Hope that Monetary Authority can take note.

In response to the guideline on Auditor's Report for certification of funds, we have consulted HKVCA members, and share with you below some specific comments. We look forward to further discussing with you and providing our input as needed.

i) In paragraph 2.1, there is a new additional "Option B" which is stated as the encouraged option in the footnote 3. As the level of information to be provided vary significantly between the two options, we recommend that the guidance should make clear the consequence of adopting either Option A and Option B, for example in terms of review process or level of queries from the IRD.

ii) In the paragraph 2.1 and footnote 2, the 70% testing coverage of Eligible Carried Interest refers to those Specified Securities transaction ("SST") post return of total principal of the fund. We would like to emphasize that carried interest is accrued from the disposal of all transactions which occurred over a fund's life on an accumulated basis, and carried interest paid to individual carried interest recipients include those related to SST occurred before return of total principal of the fund. We recommend that the MA clarify that this post return of total principal concept applies only in the context of sampling transactions, and that the eligible carried interest should still apply to all the SST regardless of timing of the disposal.

iii) Besides, if the 70% coverage means the percentage of entire allocation of carried interest from the fund, it is a significant number on the reporting level. The fund manager may be reluctant to satisfy this requirement. We would recommend that the MA clarifies that this requirement is only applied on SST that occurred during the period being reviewed.

iv) In paragraph 2.3(a) with regards to the ownership structure of the issuer of Specified Securities; while the structure is readily available at the date of acquisition (i), it may not be readily available at each accounting period end and in particular, date of last disposal. We recommend that in case such information is not available, the auditors can obtain alternative evidence, such as checking the sales and purchase agreement at disposal date to prove the ownership of the Specified Securities or sending a direct confirmation to the issuer of specified securities to confirm ownership.

v) In the paragraph 2.3(b), we understand that the purpose of obtaining audited financial statements or management accounts is to verify the principal activities of SPEs or the issuer of Specified Securities. However, the principal activity is typically not stated in the management accounts. We recommend that in case audited financial statements are not available, instead of requesting for management accounts per 2.3(b)(i)(B), it is sufficient to rely on management representation on the principal activities per 2.3(b)(iv).

vi) In the paragraph 2.3c(i), we would like to clarify that the definition in footnote 5 applies only to Hong Kong incorporated companies. The latter part of the definition refers to companies incorporated outside of Hong Kong, but the threshold of 50 members may not be applicable to overseas incorporated companies, as many other jurisdictions have a higher threshold for "public" companies. In addition, we believe applying the 50 members threshold to Hong Kong incorporated companies may disadvantage Hong Kong enterprises, as some privately-held successful Hong Kong-based technology companies may have over 50 shareholders, given many companies now rely on private capital for growth for much longer periods of time before going for listing. We would suggest that to simplify this requirement to have the GP confirm that the entity is not listed on any exchanges.

vii) Similar to above, in the Annex 3 paragraph 1. Private company, it requires that the original text of the relevant section / paragraph in the article of association on prohibition from issuing an invitation to the public. Most overseas incorporated companies would not have such provisions in their Article of Association. We recommend that alternative sample wordings can be included, for example for the GPs to confirm that the entity is not listed on any exchanges.

viii) In the paragraph 2.4, a minority shareholder may not be able to access the details of immovable property in Hong Kong from the investee. If such information is not readily provided, we suggest the auditors can employ alternative such as direct confirmation to the investee companies.

We hope that these comments will help your decision process on finalizing the guidelines. In particular, whether all SST give rise to eligible carried interest regardless of timing of disposal, and the definition of

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private companies, are important issues which may impact the adoption rate of the concession, and it would be worthwhile to arrange a small group discussion with your team on the details in the next few days.

Kind regards,

Bonnie Lo
Chair, HKVCA Technical Committee

About the HKVCA
The HKVCA is a member-based trade association was established in Hong Kong in 1987. It currently has 480 members, of whom 300 are Hong Kong based private equity managers. Our members work across the full spectrum of the industry, from venture capital, through growth capital and growth buyouts, to institutional fund investors, fund of funds and secondary investors. The HKVCA represents small teams investing in startups as well as the world’s 10 largest private equity firms.