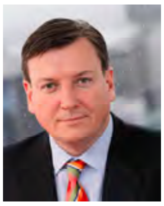
Asia Region Funds Passport

The future of the funds management industry in Asia

Foreword



John Brogden

Chief Executive Officer
Financial Services Council

The Australian Financial Services Council commissioned this research to explore the benefits arising from the development of an Asia Region Funds Passport as well as the regional attitudes towards this objective.

We are very pleased that the research has identified an overwhelmingly positive response to both of these questions.

This research confirms that the creation of an Asia Region Funds Passport presents a unique opportunity to facilitate cross-border investment within the region – bringing with it significant economic, industry and consumer benefits. Importantly, it is also clear from the research that there is widespread support for the creation of an Asia Region Funds Passport – with the region clearly signalling it is ready to embrace this exciting concept.

Through this research we hope to advance policy and regulatory discussions in the region with the aim that Governments and Regulators will begin working collaboratively with the industry to bring the Passport to fruition. The Financial Services Council stands ready to contribute to these discussions.

Robert Grome

Asset Management Leader Asia Pacific - PwC

The establishment of an Asia Region Funds Passport is a challenging first, but necessary, step in positioning Asia as a significant player in the global funds management industry.

In the coming decades Asia will need an efficient and effective funds management industry to support the pension challenges associated with a rapidly ageing population and increasing life expectancy.

The benefits for consumers, the industry and economies across the region are clear. An Asia Region Funds Passport will provide investors with access to new markets and diversification in a more efficient manner and at a lower cost, while also supporting the growth and liquidity of regional capital markets.

Once an Asia Region Funds Passport is established, mutual recognition with jurisdictions outside the region could also be developed - one Asian market, one Middle East market, one European market, one American market may eventually combine to be one global market.

Executive summary

Andrew Wilson

Asset Management Leader Australia
- PwC

The Asia region is enthusiastic about the development of an Asia Region Funds Passport[1] and appears ready to embrace the challenges involved in its establishment.

Industry support

This report incorporates the views of leading funds management industry bodies and participants across the Asia region. More than eighty per cent of industry bodies and market participants surveyed endorse the development of an Asia Region Funds Passport.

It is currently expensive and inefficient, and in some cases not possible, for fund managers to operate across the Asia region. An Asia Region Funds Passport would provide a uniform framework which would address some of these issues.

The economic and demographic fundamentals

The establishment of the Asia Region Funds Passport is considered to be important to the growth and prosperity of the region's funds management industry and in turn its ability to support growth across the region. The economic and demographic fundamentals of the Asia region support the view that it will be the "future growth engine" of the global funds management industry.

The GDP growth rate in the Asia region is forecast to be double the rate of the rest of the world. Within the region, there are many developing economies with a need for investment capital to fund the expected significant growth in their GDP. There are also developed economies with established pension systems and/or high rates of saving that have funds available to invest.

The population of the Asia region is over 4 billion, representing over 60% of the world's population. It is expected to grow by 25% by 2050[2] and ageing of the population will be at its most rapid between 2010 and 2030.[3]

Increased levels of savings and investments will be required in order to fund the retirement of this ageing population while avoiding unsustainable pressure on government finances.

Many economies have established pension and sovereign wealth funds in order to help fund the costs of these growing and ageing populations throughout retirement.

The benefits are clear

In addition to funding growth and supporting the liquidity and diversity of the capital markets in the region, the key benefits to the region of an Asia Region Funds Passport include:

- Improved efficiency and cost reduction. Cross border capital flows will provide fund managers access to larger savings pools and allow for greater economies of scale.
- Increased investor choice and ability to diversify, providing investors with access to otherwise inaccessible markets, investments and foreign expertise.
- Growth of funds management jobs and expertise in the region.

Similar regulatory frameworks

While there are diverse legislative and taxation requirements across the region, it was encouraging to note that most jurisdictions have similarities in their regulatory frameworks. For example, each jurisdiction requires the licensing of the promoter or issuer of the fund, the registration or approval of the fund itself and the registration or vetting of the offer documents.

This will provide a strong platform for establishing an Asia Region Funds Passport.

Europe may provide some answers

The increasing presence of UCITS compliant funds across Asia provides evidence that products which are established within an acceptable framework are very mobile.

The region can look to the UCITS framework as a starting point for establishing an Asia Region Funds Passport. However, to be competitive the region will need to be innovative in both the design and ongoing operation of the Asia Region Funds Passport.

Conclusion

The region is ready to act. While there are definitely complex challenges that we will need to overcome as we move forward, they are not insurmountable and the benefits to the region could be substantial.

1. A multilateral framework which would enable a complying fund or other Collective Investment Vehicle in a nation that signs up to the passport framework to offer that product in each of the other signatory nations

2. Population Division of the Department of Economic and Social Affairs of the United Nations Secretariat, World Population Prospects: The 2008 Revision, http://esa.un.org/unpp, 07/10/2010
3. Pensions in Asia/Pacific: Ageing Asia must face its pension problems, OECD, www.oecd.org/els/social/ageing

Contents

The Asia region funds management industry

A significant growth opportunity

The economic and demographic fundamentals of the Asia region support the view that it will be the "future growth engine" of the global funds management industry.

The total funds under management (FUM) across Asia is more than USD2.757 trillion representing just 13% of global FUM.[4]

Economic Growth

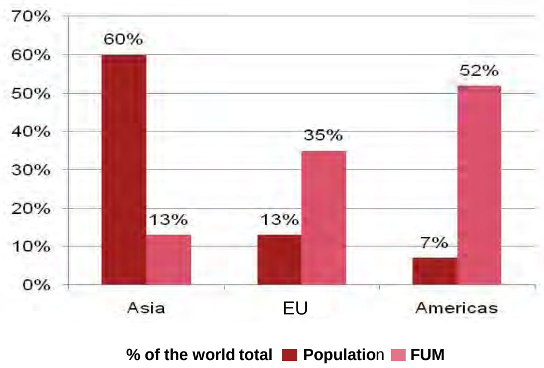
The Asia region produced USD16,652 billion[5] in GDP in 2010. Of the top 5 economies in the world in terms of GDP, two economies (China and Japan) are in Asia. GDP is forecast to grow to USD24,591 billion by 2015 - a growth rate that is almost double the rest of the world.[6]

This anticipated growth in the region makes it very attractive to investors and funds management organisations.

Within the Asia region, there are many developing economies with a need for investment to fund the expected significant growth in their GDP (for example, China and India). There are also economies that have established pension systems and/or high rates of saving that have funds available to invest (for example, Australia and Japan) and are keen to share in the huge growth opportunities presented by the developing economies.

The Asia Region Funds Passport should be designed to provide an efficient mechanism for this investment to occur, and should support the development of regional capital markets.

The amount of funds under management compared to population, highlighting the opportunity for growth in FUM in the Asia region



A large and ageing population:

The total population of Asia is over 4 billion representing over 60% of the world population and is expected to increase by 25% by 2050.[7]

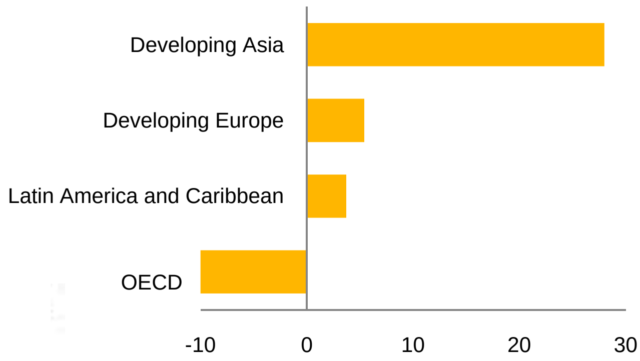
The ageing of Asia's population will be at its most rapid between 2010 and 2030. A recent report issued by the OECD[8] concluded that "*there is now a narrow window for many Asian economies to avoid future pension problems ... but it will soon be too late*". In many economies in the region, it is expected that there will be fundamental demographic change as the population ages, particularly with improvements in health care in all economies coupled with a reduction in the birth rate in many economies.

While many Asian economies have established pension schemes and sovereign wealth funds to help fund the costs of these ageing populations throughout their retirement, the extremely low levels of participation will need to be addressed. For example, pension coverage in Europe is estimated to be 60% of the working-age population, compared with East Asia and the Pacific, where it is a little over 15% and South Asia, where it is less than 10%.[9] An Asia Region Funds Passport will help provide greater investment choice at a lower cost, which will help improve retirement outcomes across the region.

Increasing middle class:

Asia's middle class has grown dramatically relative to other world regions in the last couple of decades, as outlined in the table below:

% Change in size of Middle Class (1990 – 2008)[10]



An increasing middle class will have many impacts within the region, including driving growth in GDP making the region attractive to investors. It will also lead to growth in savings pools within the region and in turn, demand for funds management services.

4. National mutual fund associations, http://www.ici.org/research/stats/worldwide/ww_03_10
5. International Monetary Fund, World Economic Outlook Database, October 2010
6. World Economic Database, April 2009, http://www.imf.org/external/pubs/ft/weo/2009
7. United Nations Department of Economic and Social Affairs/Population Division – World Population to 2300
8. Pensions in Asia/Pacific: Ageing Asia must face its pension problems, OECD
9. Pension Reform and the Development of Pension Systems: An Evaluation of World Bank Assistance, Independent Evaluation Group – World Bank
10. Key Indicators of Asia and the Pacific 2010: The rise of the middle class, Asia Development Bank

The regulatory framework

Industry bodies and market participants consider that regulators in their own jurisdiction have a strong track record in enforcing the securities laws, albeit with some respondents indicating that there had been recent significant improvements in the performance of the regulators in their market.

If the Asia Region Funds Passport is to be established, regulators in the region will need to be satisfied that there are appropriate legal and systemic protections in participating markets, including the approach of the regulator and the strength of enforcement systems.

What are the licensing requirements for the promoter?

While each jurisdiction in the region requires a promoter to be licensed and each licensee must comply with minimum capital requirements, there is quite a wide variation in the detailed requirements for licensees.

In all jurisdictions, a promoter or issuer of a fund or other Collective Investment Vehicle (CIV) requires a licence from the local regulator. Most jurisdictions require a non resident to obtain a licence by undertaking the full application and compliance process and satisfying all the local requirements.

Typically, a licensee must maintain a minimum amount of liquid assets in the particular jurisdiction and the responsible employees of the licensee must comply with local requirements to demonstrate that they have expertise to undertake the activities covered by the licence.

There are ongoing licensing requirements in each jurisdiction and licence holders are typically subject to inspection by the local regulator.

These, together with other jurisdiction specific requirements, can act as an impediment to market entry for new market participants.

What are the authorisation/registration requirements for CIVs?

In each jurisdiction, a CIV must be authorised or registered with the local regulator before it can be offered to the public. The role of the regulator is varied. In some jurisdictions the regulator reviews and vets the particular CIV for local requirements before authorising it for distribution. For example, in many jurisdictions the CIVs must meet particular investment criteria or limitations (such as investment concentration limits or gearing prohibitions) before they can be authorised.

On the other hand, in Australia, the regulator does not approve any particular CIVs or limit the types of assets in which CIVs can invest. Rather, the regulator concentrates on ensuring that the relevant disclosure documents disclose all the information relevant to an investment decision and the benefits and risks of the particular CIV product.

What are the authorisation/registration requirements for disclosure documents?

In each jurisdiction, a disclosure document must be approved by or registered with the local regulator before it can be released to the public.

In almost all jurisdictions, the disclosure document must be available in the local language.

Is there consistency in regulatory frameworks across the region?

Appendix 1 summarises the licensing and authorisation requirements in each jurisdiction for each of the promoter, CIV and disclosure document.

Appendix 2 summarises the average time and minimum financial requirements to obtain a licence.

While there is a variety of specific legislative requirements across the region it is encouraging to note the similarities in relation to the regulatory frameworks.

These similarities across the region will provide a strong platform to move towards establishing an Asia Fund Passport.

All countries have regulatory frameworks in place that require:

Fund promoters to be licensed ●

Funds to be authorised/registered ●

Disclosure documents to be registered ●

Separate custodian of fund assets ●

Key: ● Similar requirements across the region
● Some differences across the region

The legislative requirements

Across the region there are a variety of fund structures that operate, although unit trusts are common in a number of jurisdictions. There are a variety of rules in relation to investments that are permitted, commonly (although not universally) prohibiting direct investments in infrastructure and real estate and limiting the use of derivatives.

Appendix 3 summarises the restrictions on how funds operate in each jurisdiction.

There are no legislative minimum income distribution requirements in any jurisdiction in the region, other than those set out in the individual fund's documents.

Almost all jurisdictions require a separate custodian for the fund's assets. In all jurisdictions, except Singapore, the custodian has to be located in the same jurisdiction though assets can be sub-custodied to foreign custodians in some locations. In Australia, the fund manager may act as custodian if it has more than AUD5 million of capital and custody systems in place.

In addition, in all jurisdictions, a foreign fund has to have a local agent to be authorised, registered or distributed (except for China where foreign funds may not be distributed).

There will be some challenges in establishing a passport regime that satisfies the current legislative requirements in each jurisdiction.

All countries have legislative requirements in place that specify:	
Types of Funds	●
Outsourcing restrictions	●
Diversification requirements	●
Derivatives restricted	●
Local currency required	●
Key: ● Some differences across the region	

The similarities in the existing regimes provide a strong platform for establishing an Asia Fund Passport

The tax environment

Whilst an Asia passport primarily considers regulatory matters, discriminatory tax outcomes can be a barrier to the cross border distribution of funds in the Asia region.

Non-discriminatory tax regimes will allow participating markets to maximise the benefits of an Asia Region Funds Passport. Accordingly, the tax regimes of participating markets will need to move towards a "level playing field" in relation to the tax treatment of funds in their home and foreign jurisdictions.

The process of tax reform is one that extends beyond regulatory change and regulators. Where changes in tax laws are needed, it will involve Government intervention. There will need to be a broad ongoing commitment to the underlying principle of a level playing field. Each jurisdiction will need to consider and undertake tax reform to enable and maintain this.

Tax regimes are complex. Appendix 4 summaries the key tax considerations for CIVs. Appendix 5 summarises the key tax considerations for investors in each jurisdiction.

Tax reforms that may be required in various jurisdictions represent a significant challenge to the establishment and efficient operation of an Asia Region Funds Passport.

The tax regimes in each jurisdiction have inherent differences across key areas of tax

Tax treatment of domestic fund	● (Significant differences)
Tax treatment of foreign fund	● (Significant differences)
Withholding tax	● (Some differences)
Double tax treaties	● (Some differences)
Individual resident	● (Significant differences)
Individual non-resident	● (Significant differences)

Key: ● Some differences across the region
● Significant differences across the region

The tax regimes in each jurisdiction are complex and represent a significant challenge to the success of an Asia Region Funds Passport

The Asia region's experience of offshore funds

The relative exposure of the investing public to offshore funds in each jurisdiction varies significantly.

Some jurisdictions, such as Hong Kong and Singapore, are dominated by internationally domiciled funds, whereas others such as Australia, Japan and Korea have more domestic managers. The proportion of all unlisted funds offered in the following economies that are domiciled outside of the region[11] is:

- Hong Kong 91%
- Singapore 79%
- Taiwan 59%

Over the past three years approximately 40% of all net sales into UCITS[12] funds have been sourced from Asia.

A key impact of the quantum of funds domiciled outside the region is that the Asia region is outsourcing an increasing range of funds management services. As can be seen in the table below there are already more than 5,000 UCITS products being sold into Asia, predominantly from Luxembourg.

The region may be missing out on opportunities to fully benefit from the growth in demand for funds management products across the region and associated development of skills and job opportunities in areas such as fund administration, custody, compliance, legal, tax and technology.

...the Asia region is outsourcing an increasing range of funds management services.

The following table summarises the number of UCITS funds distributed in the Asia region[13] in 2009

		Fund domicile							
		Belgium	France	Germany	Ireland	Luxembourg	UK	Other	TOTAL
Funds distributed	Australia				7	42		6	55
	Hong Kong		2		207	953	24	23	1,209
	Japan			4	3	50		10	67
	Korea					248	2		250
	Macau				96	433	5	45	579
	Singapore		10	19	399	1,599	48	185	2,260
	Taiwan	17	6	10	161	616	10	27	847
	Total	17	18	33	873	3,941	89	296	5,267

11 PricewaterhouseCoopers, Global Fund Distribution, 2010
12 Undertakings for Collective Investments in Transferable Securities issued under a European Union Directive
13 PricewaterhouseCoopers, Global Fund Distribution, 2010

Conclusion

Each jurisdiction in the Asia region has developed its own legislative and tax requirements
for funds, which presents both challenges and opportunities.

Although there are broad similarities, the various regulatory and tax regimes currently make it expensive and inefficient for fund managers to distribute their products in different markets across the region. The Asia Region Funds Passport would seek to address much of this inefficiency.

The similarities in the existing regulatory frameworks (for example, all jurisdictions require the funds, fund managers and offer documents to be registered and most require a separate custodian) provide a strong platform for establishing an Asia Region Funds Passport.

The similarities in the existing regulatory frameworks provide a strong platform for establishing an Asia Funds Passport

The industry generally consider the regulators in their own jurisdiction have a strong track record in enforcing the securities laws

An Asia Region Funds Passport would be a mechanism designed to facilitate the distribution across regional borders of Collective Investment Vehicles manufactured, distributed and administered within the region

The industry identified numerous benefits arising from the introduction of an Asia Region Funds Passport

An Asia Region Funds Passport

What is an Asia Region Funds Passport?

An Asia region Collective Investment Vehicle Passport ("Asia Region Funds Passport") would be a mechanism designed to facilitate the distribution across regional borders of funds manufactured, distributed and administered within the region. It would require the development of an agreed set of funds management regulations amongst a group of like-minded economies in the Asia region.[14]

This agreed set of regulations would not necessarily be identical to the domestic regulations in any of the participating jurisdictions, but would be designed to provide a level of protection for investors that is acceptable to the regulator in each participating jurisdiction.

Funds that meet this agreed set of regulatory requirements would be certified to be "Asia Region Funds Passport compliant" by the regulatory authority in the home jurisdiction, and could then be sold both domestically and also across borders amongst the Passport jurisdictions.

The common set of passport regulations would need to cover a wide range of issues, including:

- the eligible investment asset classes
- custody arrangements
- offer document conditions
- registration arrangements
- licensing arrangements
- any limits on leverage
- liquidity requirements and
- investor protection and dispute resolution procedures.

This framework could be conceptually similar to the UCITS framework that has been established by the European Union.

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Given the penetration and apparent appeal of the UCITS regulatory framework within the region and elsewhere, the region could, initially at least, mould such an Asia Region Funds Passport regulatory framework reasonably closely on the current UCITS framework. However, if an Asia Region Funds Passport is going to provide an alternative for UCITS in the region we will need to innovate to ensure it is a competitive alternative (eg by providing access to different markets, more efficient registration process, etc).

Once in place, any changes to this framework would be determined by regulators and governments within the region on the basis of regional needs and developments to ensure the Asian Region Funds Passport remains competitive.

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An Asia Region Funds Passport is a mechanism designed to facilitate the distribution across regional borders of funds manufactured, distributed and administered within the region

14 Asia Region Funds Management Passport Proposal: Regional Benefits (unpublished manuscript) by the Financial Centre Task Force

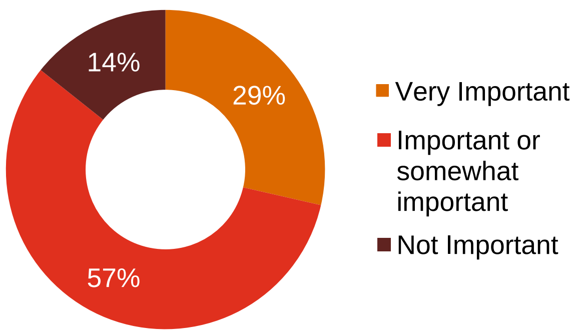
Is the region supportive of an Asia Region Funds Passport?

Based on survey responses received from 7 of the leading funds management industry bodies across the region, it is evident that there is strong support for the development of an Asia Region Funds Passport. 86% of industry body respondents indicated that it is of importance to the growth and prosperity of their funds management industry, as is illustrated in the graph below.

Similarly, there is strong support for an Asia Region Funds Passport from the surveyed market participants, with all respondents indicating that they consider the establishment of an Asia Region Funds Passport to be of importance to the growth and prosperity of their funds management industry, as can be seen in the following graph. We note that there may be some positive bias in the survey results, given that participants who consider the Asia Region Funds Passports to be important are most likely to respond to the survey.

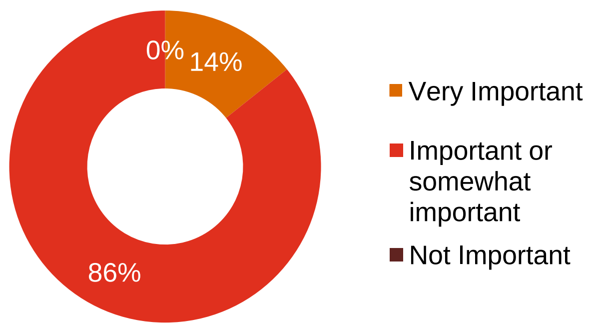
Industry bodies:

How important is the establishment of an Asia Region Funds Passport to the growth and prosperity of your funds management industry?



Market participants:

How important is the establishment of an Asia Region Funds Passport to the growth and prosperity of your funds management industry?



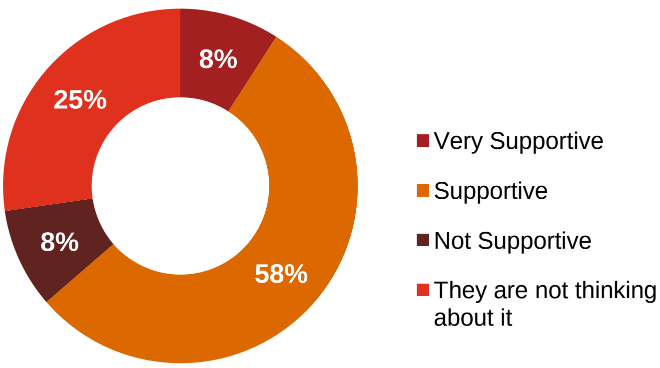
Is the region supportive of an Asia Region Funds Passport? (cont'd)

The surveyed market participants indicated that 66% of the wealth managers in their economy were either very supportive or supportive of an Asia Region Funds Passport, though 25% indicated that wealth managers in their country were not yet thinking about it. Not surprisingly, a number of these were in China where it is currently not possible to distribute foreign funds.

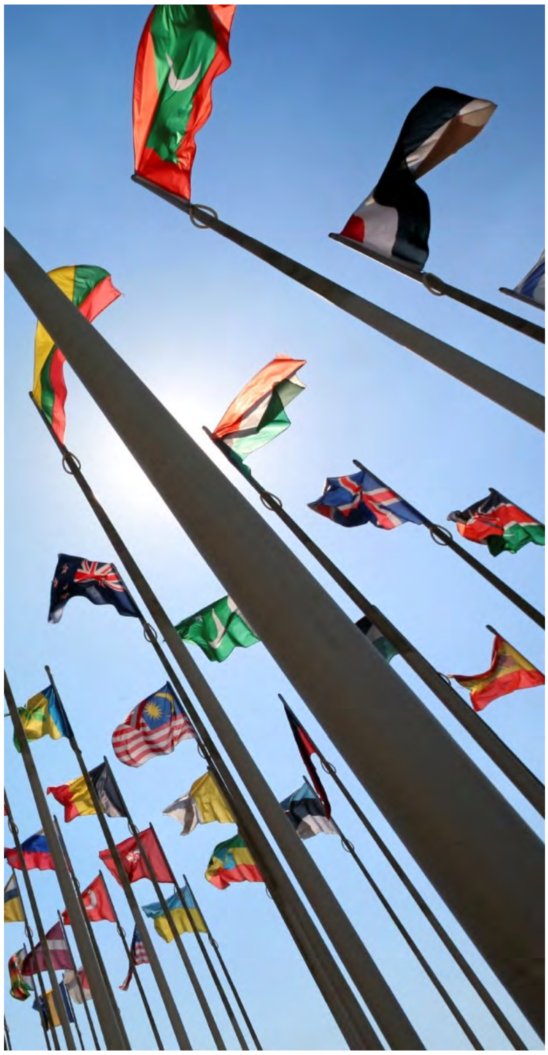
Also, there are a number of market participants that are currently selling UCITS products across the region. These participants have an established distribution channel and may be satisfied with the use of these products as a means of accessing a number of markets across the region, reducing the importance of establishing an Asia Region Funds Passport for them. This also highlights the need for innovation in the creation of the Asia Region Funds Passport to allow it to compete with existing products in the region, especially UCITS (for example, access to different markets, more efficient registration process, etc).

Market participants:

Are wealth managers in your jurisdiction supportive of the establishment of an Asia Region Funds Passport?



The surveyed market participants indicated that 66% of the wealth managers in their economy were either very supportive or supportive of an Asia Region Funds Passport



What are the benefits of an Asia Region Funds Passport?

The industry bodies and market participants identified numerous benefits arising from the introduction of an Asia Region Funds Passport, including the following:

- **Improved efficiency and therefore reduced fees/costs as a result of the following:**
  - Fund size would likely be much larger through the ability to offer a single fund across multiple markets
  - Fund managers and distributors would gain efficiency through an increased number of funds, increased funds under management and a larger client base i.e economies of scale
  - Increased competition putting further downward pressure on fees to the benefit of investors. Fees across the region currently range from 0.4% to 3% of net asset value per annum. As such, the opportunity for fee reductions especially in higher fee regions may be significant
  - Direct access to offshore funds rather than access via a local operator will likely result in the elimination of an extra layer of fees and commissions.
- **Increased investor choice which would result in the following benefits:**
  - There would be direct access to otherwise inaccessible markets, products and offshore expertise
  - A broader range of products available to investors which would enable greater diversification. This is particularly important as many investors have a high concentration of investments in their local securities which could be reduced by diversifying the portfolio geographically.
- **Improved services:**
  - Higher competition in the funds management industry should lead to improvement in innovation and service delivery

"The high concentration of domestic securities can be reduced by diversifying the portfolio geographically"

Market participant

"Investors would have more choices"

Market participant

- **Improved consumer protection as a result of the following:**
  - For those investors in countries in the region with less developed funds management industries, there will be easier access to more sophisticated industries with strong corporate governance and regulatory frameworks
  - Increased sophistication and expertise across the region through sharing of experiences and best practices between markets.

- **Significant benefits to the wider economy**
  - Across the region economies are at different stages of development, with emerging markets undergoing significant development and therefore in need of capital, while some countries, particularly those with a well-developed pension/ superannuation system and sovereign wealth funds have assets to invest to meet this capital need. For example, in Australia, FUM is forecast to grow from AUD1.4 trillion to in excess of AUD5 trillion over the next two decades. The Asia Region Funds Passport would facilitate the flow of capital across the region
  - Investors across the region can choose to more readily access growth opportunities within member countries
  - Capital market liquidity and diversity across the region would be enhanced
  - Increased visibility of and interest in the Asia region's "locally-constituted" funds, resulting in greater global competitiveness of the Asia region funds management industry
  - Increased support for the growth of the funds management industry across the region and retention of expertise and employment within the region.

"Liquidity in the country is enhanced due to capital investments"

Market participant

"Direct access to otherwise inaccessible markets and instruments"

Market participant

What are the challenges to establishing an Asia Region Funds Passport?

It was generally recognised that there are some significant challenges to introducing an Asia Region Funds Passport. Almost all of the market participants surveyed indicated that establishing an Asia Region Funds Passport would be challenging, citing the following key reasons:

- Differing legislative and tax requirements
- Variety of languages and cultures
- Range of sophistication and size of markets and investors
- A potential desire by local regulators and/or governments to protect their domestic fund industry through the maintenance of barriers to entry
- Regulator resistance due to the inclusion of jurisdictions which may not appear to have a comparable level of regulatory supervision
- Local industry resistance should there not be a level playing field (regulatory and tax) between passport jurisdictions.

In addition, it may be more challenging to establish than UCITS because there is no body or framework in the Asia region equivalent to the European Union with its overarching regulatory and governance framework.

While the challenges faced by the Asia region in establishing an Asia Region Funds Passport are significant and complex they are not insurmountable. Similar challenges have been overcome in the EU in order to establish UCITS, and the Asia region can learn from the EU experience to expedite addressing these challenges.

What are the current arrangements for distribution of foreign funds in the Asia region?

Foreign funds may be distributed to particular jurisdictions in the region either through specific mutual recognition agreements or through recognition of UCITS compliant products. There are currently very few mutual recognition arrangements in place between markets that permit the distribution of funds which have been authorised in one country to be distributed to the public in another country without complying with the full range of the other country's approval requirements.

Examples of mutual recognition agreements in place between countries include Australia and Hong Kong and in Thailand the regulator may approve a fund operated from a country that is regulated by a member of IOSCO, as can be seen in Appendix 6.

There are currently very few arrangements for the mutual recognition between markets in the Asia region permitting the distribution of foreign funds

In practice, even where foreign funds can be distributed, the impediments to their success are currently quite significant. For example, in Japan, foreign funds may be offered for sale, however, there are language and tax impediments for investors which make off-shore products less attractive. In addition, other challenges exist such as whether the distributor's system can handle such funds. As such the market share of foreign fund sales relative to domestic products can be low.

Similarly, there has been very little use made of the Australia and Hong Kong mutual recognition agreement, primarily because of some of the restrictions imposed on the funds (for example, maximum foreign holdings), tax impediments and the timing of the agreement (July 2008, immediately before the global financial crisis).[15]

Where there is demand for offshore exposure, fund managers are commonly accessing foreign asset managers through other structures such as through the use of a foreign sub-advisor in a fund-of-funds structure. For example a Japanese fund manager may offer an Australian bond fund to Japanese investors. The Japanese fund manager would then access the Australian bond fund manager's expertise through investing in an Australian bond fund or entering into a direct fund management agreement (mandate) with an Australian fund manager. The Asia Region Funds Passport would allow the Australian bond fund to be offered directly to Japanese investors, thereby eliminating a layer of costs.

The industry does not underestimate the complexity in overcoming the impediments but appears ready to embrace the first steps

Conclusion

There is clearly significant and widespread support for the establishment of an Asia Region Funds Passport. The benefits to investors, to the industry and to the regional economies from reducing the barriers to funds flows across the region are significant, including increased investor choice, improved diversification opportunities and growth of the industry.

15 Asia Region Funds Management Passport Proposal: Regional Benefits, Financial Centre Task Force (unpublished manuscript)

UCITS: what it has meant for Europe and what the Asia region can learn

The UCITS[16] framework was created over 25 years ago, with the objective of establishing a single market for funds management services across the European Union ("EU").

Implemented in 1985, the UCITS directive aimed to develop a unified regulatory framework for mutual funds across Europe, to facilitate the distribution of funds domiciled in one member state across multiple EU member states and to offer investors in UCITS products a consistent level of protection and confidence. Many forms of vehicles can be UCITS compliant.

What was the initial experience of UCITS in Europe?

There was relatively slow growth in UCITS when the directive was initially introduced. The UCITS framework has subsequently undergone further development and the success of UCITS has grown significantly around the world.

On initial implementation the objectives of the directive and the reality were very different – largely due to a lack of cohesion across the local laws, regulations and distribution policies of individual EU member countries.

The success of the UCITS directive was also limited by the restrictions it placed on the permitted investments of UCITS vehicles, which were limited to a narrowly defined category of transferable securities and consisted mainly of equities and bonds. UCITS I prohibited 'higher risk' investments such as derivatives and alternative asset classes and structured products.

In the early 1990s, a second directive UCITS II was drafted with the objective of addressing these issues, but the initiative was abandoned when member states did not reach an agreement on the scope and form of the directive.

What is the current experience of UCITS in Europe?

UCITS III[17] was launched in 2001 and comprised of two directives. Together, the new directives aimed to provide for the regulation of management companies and simplified fund prospectuses (the "management directive"), as well as a wider range of investment powers (the "product directive").

In practical terms, once a fund has been certified as UCITS compliant in one EU member state, an application may be made to market that fund to the public in any other EU country.

UCITS III substantially broadened the investment powers of investors by allowing UCITS to invest in other financial products (such as certain derivative instruments).

Whilst product sophistication brings with it concerns that the existing UCITS brand may become tainted, it is recognized that a uniform set of rules governing the permitted investments by UCITS products has actually brought with it improved investor protection. Further, the differentiation between sophisticated and simple products may be addressed in a future UCITS V.

Since its introduction in 2001, UCITS III has achieved significant success, with rapid growth and penetration across the European market and more recently, increasing distribution across the global market.

UCITS has been at the heart of the development of the European funds industry for the last two decades - with assets of €5 trillion, representing over 75%[18] of the European investment funds market.

A significant number of the national tax and regulatory barriers that had previously restricted the flow of funds across Europe have been successfully reduced, and whilst differences still remain (mainly in relation to withholding taxes, tax credits on dividends and the ability to access double tax treaties),[19] the directive's objective of developing a unified regulatory framework for mutual funds across Europe is largely achieved.

16 Undertakings for Collective Investment in Transferable Securities (UCITS) Directive 85/611/EEC
17 UCITS Directive 2001/107/EC and 2001/108/EC
18 EFAMA – July 2010
19 Tax discrimination against foreign funds: Light at the end of the tunnel, PricewaterhouseCoopers, EFAMA, 2005

What is the experience of UCITS beyond Europe?

Beyond Europe, recent trends have shown a clear and significant growth in the distribution of UCITS products in the international market.

Asia, Latin America and the Middle East are predominant markets where UCITS have wide distribution. Within the Asia region, Singapore, Hong Kong and Taiwan are the main focuses of distribution – with nearly 2,300 cross-border registrations of UCITS products in Singapore at 31 December 2009.[20] 47 of the top 50[21] cross-border management groups are currently distributing in Singapore, Hong Kong, or Taiwan – or all three.

Currently, approximately 50% of all net sales into UCITS products are originating from outside the EU, with Asia representing between 30% and 40% of total net sales into UCITS. Assets from within Asia constitute approximately 20% of total FUM in UCITS.

There are significant funds currently flowing from Asia into UCITS products. It is clear from this experience that there is demand from Asian investors for foreign funds. Given the clear demand, and the head start that the EU, through UCITS, has in the Asia region, the development of an Asia Region Funds Passport is not only warranted, it is needed.

What are the benefits that have arisen for Europe from UCITS?

UCITS III has allowed the European funds industry to develop truly cross-border products, which offer investors greater choice, portability and investor protection. Using a mutual fund vehicle of their choice, it is now possible for investors to access markets and underlying assets which may otherwise have been inaccessible and do so through a globally recognised framework.

UCITS products have proved attractive to investors who are increasingly looking for balanced portfolios consisting of transparent, well regulated products with greater liquidity and less risk.

From the fund promoter's perspective, the strength of the UCITS brand amongst retail and institutional clients has greatly enhanced the marketability and distribution of product offerings across Europe and beyond. The number of fund managers operating cross-border fund platforms has increased significantly, from 35 in 1999 to 230 in June 2010.[22]

Investment fund assets in Europe have more than doubled in size over the last decade to €6,833 billion[23] and cross-border registrations of UCITS funds have increased from 11,338 at 31 December 1998 to 59,100 at 30 June 2010[24] - firmly establishing the European funds management industry as a strong and vital component of the European financial system.

It is anticipated that the many benefits seen in Europe and the European funds management industry through the implementation of UCITS could be equally realised in Asia through an Asia Region Funds Passport.

20 PwC, Lipper and Thomson Reuters - Global Fund Distribution 2010
21 PwC, Lipper and Thomson Reuters - Global Fund Distribution 2010
22 Lipper Feri
23 EFAMA, 31 December 2010
24 Lipper Feri

What does the future hold for UCITS?

The UCITS regime will continue to evolve to maximise the benefits that flow to member states.

Whilst UCITS III has expanded the investment alternatives for UCITS, it has become evident over time that there are still some continuing inefficiencies in the industry under the Directive.

A report which considered the potential of a fully integrated European funds market[25] predicted that annual savings of up to 17 basis points could be attained if average European equity fund sizes (average €148m)[26] were to increase to that of the average US fund (average €886m).[27] In addition a comparative study by Lipper found that the average Total Expenses Ratio of a Luxembourg fund with assets under USD 5 million is more than double that of a fund with over USD 250 million of assets.[28]

The Commission of the European Communities estimates that the potential annual savings to the European funds industry through improved efficiencies could be several billion Euros.[29]

The introduction of UCITS IV[30] in July 2011 aims to address some of these inefficiencies and promote cost savings through modifications such as the management company passport (which means that for the first time the management company of the fund will not be required to be located in the same EU member state as the fund's domicile), fund mergers, master feeder structures and the simplification of investor information.

It is hoped that the efficiency and consolidation measures under UCITS IV will bring greater flexibility to the industry, translating into new business opportunities for fund managers, increased competitiveness and a more consolidated funds market.

What are some of the learnings from UCITS?

UCITS has, over the last two decades, succeeded in creating an EU passport for funds and now for fund managers.

Some empirical evidence of the significant benefits that have flowed from the introduction of UCITS include increased investor choice, improved diversification opportunities, ongoing reduction in fees and growth of the industry.

The appetite for 'mobile' funds and products with 'passports' extends beyond investors in the EU. Hence the growth of UCITS funds around the world.

Industry players in the EU see this opportunity, and appear to be specifically targeting the Asia region as a growth area. UCITS funds are one of the fastest growing investment products in the Asian region.

It appears that the significant growth of UCITS occurred once the permitted classes of assets in which a UCITS product could invest was expanded, enabling a wider range of products to be offered. Ideally, the Asia Region Funds Passport would not need to start with such a restrictive regime as UCITS I, but rather adopt a regime more akin to UCITS III or even IV.

There has been and continues to be ongoing development of UCITS. Similarly, an Asia Region Funds Passport would require ongoing development to ensure that it remains competitive and relevant and the passport framework would need to embed such a function.

Perhaps the final learning is the need for patience – the success of UCITS that we see today was two decades in the making. While it is hoped that an Asia Region Funds Passport could be achieved more quickly, as the industry embarks on this process it must be mindful of the time required to achieve success.

The UCITS framework may provide a good starting point but the region will need to make some key decisions to tailor it for the region. For example, should the Asia Region Funds Passport be fully competitive with UCITS IV (inclusive of a fund manager passport) or would this require too much change to be an attainable goal in the foreseeable future? Would the Asia Region Funds Passport seek to differentiate itself from UCITS, other than through the markets available? If so, how?

It is clearly time to start considering these and many other questions. In many ways, the success of the Asia Region Funds Passport will be determined by the answers to these questions.

25 Potential cost savings in a fully integrated European investment fund market, CRA, September 2006
26 Potential cost savings in a fully integrated European investment fund market, CRA International , September 2006
27 Potential cost savings in a fully integrated European investment fund market", CRA International , September 2006
28 Economies of scale and consolidation in collective funds, Lipper, March 2005
29 Proposal for a directive of the European Parliament and of the Council on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), Commission of the European Communities
30 Recast UCITS Directive 2009/65/EC

Appendices

Appendix 1: Authorisation/registration requirements for promoters, funds and disclosure documents

Country	Regulator	Fund promoter licence	Investment manager licence	Fund authorization/ registration	Disclosure document registration	Disclosure document language requirement
Australia	Australian Securities and Investments Commission (ASIC) Australian Prudential Regulatory Authority (APRA)	Yes	Yes	Yes	Yes	English
China	China Securities Regulatory Commission (CSRC)	Yes	Yes	Yes	Yes	Chinese
Hong Kong	Securities and Futures Commission (SFC)	Yes	Yes	Yes	Yes	Chinese and English
India	Securities and Exchange Board of India (SEBI)	Yes	Yes	Yes	Yes	English
Indonesia	Capital Market Supervisory Board and Financial Institution (BAPEPAM – LK)	Yes	Yes	Yes	Yes	Bahasa
Japan	Financial Services Agency (FSA) Securities and Exchange Surveillance Committee (SESC)	Yes	Yes	Yes	Yes	Japanese
Korea	Financial Supervisory Commission (FSC)	Yes	Yes	Yes	Yes	Korean
Malaysia	Securities Commission	Yes	Yes	Yes	Yes	English or Bahasa Malaysia
Singapore	Monetary Authority of Singapore (MAS)	Yes	Yes	Yes	Yes	English
Taiwan	Securities and Futures Bureau of the Financial Supervisory Commission (FSC)	Yes	Yes	Yes	Yes	Chinese
Thailand	Securities and Exchange Commission (SEC)	Yes	Yes	Yes	Yes	Thai

Appendix 2: Average time and financial conditions required to obtain a licence, authorise a CIV or register a disclosure document in each jurisdiction

	Australia	China	Hong Kong	India	Indonesia	Japan	Korea	Malaysia	Singapore	Taiwan	Thailand
How long does it take to obtain a licence to market a fund?	1 to 4 months	Depends on regulator's approval	About 6 months (Approx)	12 to18 months for a license for a mutual fund	3 months to1 year	6 months to 1 year	3 months	3 to 6 months	4 to 6 months	2-3 months but currently the process may take much longer	Within 60 days and passed to Minister approval within 30 days
What are the practical impediments to a foreign entity obtaining a licence in your jurisdiction?	Minimum capital requirements, audit and compliance requirements	Regulator's approval	Periodic submission of financial resources returns, compliance requirements, resident responsible officers, etc	Minimum capital requirements and regulators approval	No clear regulations yet on issuance of a securities fund by a foreign entity	Language barriers, highly regulated environment and compliance risks/costs	Need to establish local branches or other business offices	Subject to approval of regulator	Meeting the capital and operational requirements and "fit and proper" test	Fund investment rules and asset allocation	Company under Civil and Commerce Law
What are the minimum capital requirements for a licence holder?	0.5% of assets of schemes operated with a minimum of $50,000 and a maximum of $5 million. Minimum of $5 million if no separate custodian	Rmb 20 million for security consulting institutions, Rmb 30 million for fund promotion institutions. No specific minimum capital for banks, security companies and fund managers which are subject to specific regulatory requirements	An asset manager must have a minimum paid up capital of HKD 5 million and liquid capital of HKD 100,000 if it does not hold client assets	An asset management company must have a net worth of INR 100 million. A foreign entity proposing to invest in our Indian mutual fund must have an asset management company incorporated in India	Rp 100 billion	JPY 50 million and net capital ratio to risks calculated based on prescribed formulae depending on the licence	Initial minimum capital : KRW 8 billion Ongoing minimum capital : 70% of initial minimum capital	Depends on the licence	SGD250,000 to SGD1,000,000 depending on type of licence	At least 300 million New Taiwan Dollars of paid-in capital	500 million baht for the application submitted from 1 January 2012. 100 million baht pre 31 Dec 2011

Appendix 2: Average time and financial conditions required to obtain a licence, authorise a CIV or register a disclosure document in each jurisdiction (cont'd)

	Australia	China	Hong Kong	India	Indonesia	Japan	Korea	Malaysia	Singapore	Taiwan	Thailand
How long does it take to authorise or register a fund?	Usually 1 to 2 months. The actual formal period is 14 days	Depends on regulator's approval	3 to 6 months	After obtaining the Mutual Funds licence a scheme can be launched for which documentation needs to be submitted 21 days before opening the offer	Minimum 1 month	1 to 6 months	20 days from application date	Not known	2 to 3 months	At least 2-3 months but currently the process may take much longer	Within 60 days and passed to Minister for approval within 30 days
How long does it take to achieve approval or registration of the disclosure document?	No formal approval period. ASIC usually asks questions within the first 10 business days	Depends on regulator's approval	3 to 6 months	The document needs to be submitted 21 days before opening the offer	Minimum 1 month	15 days to 1 month after application is lodged	15 days	Normally 1 to 2 months	3 to 4 months	At least 2-3 months but currently the process may take much longer	90 days
Does the disclosure document have an expiry date?	No, but the information must be up-to-date	A fund must be launched in 6 months after CSRC's approval	No, but the information must be up-to-date	Annual. The additional information has to be up-to-date	Annual	Yes – Semi-annually	No	No	Yes	No, but the information must be up-to-date	No

Appendix 3: Restrictions on how a fund operates in each jurisdiction

Country	Types of CIVs offered	Investment types not permitted	Restrictions on outsourcing	Diversification requirements	Leverage restricted	Derivatives restricted	Local currency denomination required
Australia	Unit trusts and superannuation funds	None identified	No, but the licensee must comply with outsourcing guidelines	No	No, except for superannuation funds which may not grant security over their assets	No	There is no specific requirement
China	Open-ended and close-ended funds, multi-client segregated accounts	Real estate, infrastructure	No, if the service provider has the appropriate license	Yes – the fair value of the fund's investment in the stocks issued by one company cannot exceed 10% of the fund's net assets, the investment held by all funds managed by the same fund manager in the securities issued by one company cannot exceed 10% of the securities on issue. There may be other diversification requirements in fund contracts	Yes – only through repos. Monetary market funds could have repos of no more than 20% of its net asset value, other funds no more than 40%	Yes – especially warrants and stock index future	Yes
Hong Kong	Unit trusts, eg equity fund, hedge fund, index fund, warrants fund, REIT etc.	Infrastructure	No	Yes – extensive. A securities scheme may not hold more than 10% of its net assets in securities issued by a single issuer. It may not hold more than 15% of its net assets in unlisted or unquoted securities. There are a range of "specialised funds" under the Unit Trusts Code, such as cash management funds, hedge funds and structured funds, which have specific diversification requirements	Yes – depends on the asset class, but generally between 10% and 25% of gross assets	Yes for general securities funds which may invest in options and warrants for hedging purposes, but subject to a 15% diversification restriction. A scheme may invest in futures contracts for hedging purposes, but subject to diversification restrictions. It is possible to establish specific funds to invest in derivatives with increased levels of disclosure	There is no specific requirement
India	Mutual funds. Other funds such as Domestic Venture Capital Funds, Collective investment schemes can have private placement	Restrictions on derivatives. Investment in physical assets (eg gold, real estate) is subject to restrictions	Outsourcing of core functions could require approval	Yes	A Mutual Fund cannot borrow except to meet temporary liquidity needs for the purpose of repurchase, redemption of units or payment of interest or dividend to the unit holders	Yes (only securities futures and options permitted)	Yes

Appendix 3: Restrictions on how a fund operates in each jurisdiction (cont'd)

Country	Types of CIVs offered	Investment types not permitted	Restrictions on outsourcing	Diversification requirements	Leverage restricted	Derivatives restricted	Local currency denomination required
Indonesia	Protected fund (RDPT) Discretionary fund	Real estate, infrastructure	No	No	Yes	No	No
Japan	Investment Trusts (ITM Funds). For alternative investments, other types of CIVs are used (eg investment corporation, TK,TMK)	ITM Funds may invest in various products	Yes – must have internal portfolio management function but can outsource some asset management	Yes.	Yes – The use of leverage should be within net asset value of the fund, and the borrowings are allowed only for the purpose of paying redemption and/or distribution to investors	Yes – for hedging purposes such investments should not go over the scope of hedging, or should be defined in its contract document	While there are no laws prohibiting an ITM Fund from being denominated in foreign currencies, from an operational perspective it is extremely difficult to do so. No such limitations exist for foreign funds
Korea	Investment trust, Investment company, Investment limited liability company, Investment limited partnership company, Investment limited partnership, Investment undisclosed association	Private equity and hedge funds cannot be offered to the public	Yes. Asset management compliance, internal audit, risk management are restricted to outsource. However, foreign investment management function can be delegated to other asset managers	Yes. Diversification requirements depend on types of assets invested by funds (eg 10% rule)	Yes. Generally, fund portfolios are prohibited from using leverage. However, in the case of private placement funds for qualifying investors, total borrowing is limited	Yes. Basically, the total risk exposure to derivatives should not exceed net asset of the fund	Yes. However, foreign funds can be denominated in foreign currencies and may issue different classes of units in different currencies
Malaysia	Unit trusts are most common	Some restrictions on certain assets, such as derivatives	Generally no, especially for overseas investments	Only for specific fund types, for example, REITs must have a certain percentage invested in completed property	Yes	Only permitted for hedging purposes	Yes
Singapore	Unit Trust Limited Partnerships	Generally none	No, but guidelines on outsourcing need to be complied with	Yes. Depends on type of funds, ie Equity/bond/balanced have no restrictions, but fund of hedge funds do	Yes	No	No. Funds may issue different classes of securities denominated in different currencies

Appendix 3: Restrictions on how a fund operates in each jurisdiction (cont'd)

Country	Types of CIVs offered	Investment types not permitted	Restrictions on outsourcing	Diversification requirements	Leverage restricted	Derivatives restricted	Local currency denomination required
Taiwan	Contractual-type vehicles operated by a Taiwan securities investment trust company ("SITE"). The SITE is the settlor and a custodian acts as the trustee of fund assets	Government Bonds. Securities must be listed, traded on the over-the-counter market or approved by FSC. Funds may not invest directly in commodities, gold, or real estate but may invest directly	Yes, asset management functions may not be outsourced. Only registrar/transfer agent functions may be outsourced	Yes – extensive. For example, no individual investment may exceed 10% of the fund value, the investment may not constitute more than 10% of the investee company and the total amount invested by all funds under the common management of a SITE may not exceed 10% of the total issued shares of that company	Yes and funds cannot lend to or provide guarantee for any other entity	Yes, only allowed for hedging purpose, to improve investment efficiency, or as otherwise approved by the FSC. There are various risk exposure limits	Yes, local funds are denominated in New Taiwan Dollars. Offshore funds marketed in Taiwan may be denominated in other currencies
Thailand	Mutual Fund, Property Fund, Private Fund, Thai Provident Fund and Venture Capital Fund	Infrastructure.	Such asset manager has to be member of IOSCO but subject to approval by SEC	Depends on fund type. All have been notified in the Prospectus	No	Yes	Yes

Investment types:

The table above considers the types of assets in which publicly available funds may invest and listed our understanding of the most common asset classes, being fixed interest, shares, government bonds, company bonds and other debt securities, derivatives (options, warrants, foreign exchange contracts, swaps), real estate and infrastructure. In the table above, we have indicated that there are no restrictions on investment types with a response of "none identified", as we were informed that all those asset classes were permitted investments. However, they may be subject to other restrictions or limits on the types or size of investments in a particular asset class set out in the relevant regulators guidelines.

Appendix 4: Key tax considerations for CIVs in each jurisdiction

	Taxation of the fund			Withholding tax	Double tax agreements
	How would each of the fund vehicles in your jurisdiction be regarded for tax purposes?	What are the tax implications for a domestic fund domiciled in your jurisdiction, including annual reporting requirements?	What are the ongoing tax implications for a foreign fund being distributed into your jurisdiction?	What income withholding tax or capital gains withholding tax exposures arise on investments held in your jurisdiction?	To what extent can domestic funds benefit from double tax treaties?
Australia	Funds are not taxed at the fund level, but are instead regarded for tax as flow through entities (provided investors are entitled to all the income of the fund)	There is no tax at the fund level. Australian funds are required to lodge an annual tax return and also must report information to their investors annually so that they can complete their personal tax returns	Usually none	Australian funds are responsible for withholding tax on distributions to non-residents	Tax treaties exist but limitations may arise if the treaty requires beneficial ownership (due to the trust legal form)
China	Funds are free of capital income tax	Not applicable	Unclear	Minimal – as individual residents are free of capital gain tax, unclear for foreign investors	It is unclear whether funds would be able to access double tax agreements as funds do not pay domestic tax for their income arising from overseas investments
Hong Kong	All authorised funds are exempt for tax purposes	None	None if the foreign fund is an authorised fund in Hong Kong and there is no permanent establishment of the fund in Hong Kong	Generally none	Hong Kong has a growing number of Double Tax Treaties
India	A view can be taken that a Mutual fund registered with SEBI is exempt from tax.	Domestic entities are generally required to file an annual income tax return/wealth tax return. Other reporting requirements include withholding tax return, advance tax payments etc	Foreign funds cannot be directly distributed in India	No withholding tax on capital gains for resident and certain categories of foreign investors.	A domestic Mutual Fund could benefit from the treaty if it is regarded as resident under the relevant Double Taxation Avoidance Agreement

Appendix 4: Key tax considerations for CIVs in each jurisdiction (cont'd)

	Taxation of the fund			Withholding tax	Double tax agreements
	How would each of the fund vehicles in your jurisdiction be regarded for tax purposes?	What are the tax implications for a domestic fund domiciled in your jurisdiction, including annual reporting requirements?	What are the ongoing tax implications for a foreign fund being distributed into your jurisdiction?	What income withholding tax or capital gains withholding tax exposures arise on investments held in your jurisdiction?	To what extent can domestic funds benefit from double tax treaties?
Indonesia	Collective investment fund regarded as a corporation for tax purposes. These funds are subject to tax	There are monthly and annual tax reporting requirements	No Indonesian tax implication if the fund is not Indonesian tax resident	For investment in a Mutual Fund irrespective of the residency, there should be no tax. Other types of investment may be subject to withholding tax, eg listed share, bonds and savings	Domestic mutual funds can benefit from double tax treaties
Japan	Investment trusts are not subject to Japanese corporate tax if certain criteria are met Investment trusts are treated as opaque under Japanese tax law. Income is recognized by the beneficiary at the time when a profit distribution form the trust is made	No tax reporting requirement for the investment trust itself if certain criteria are met. There are information sharing requirements for the withholding tax agents which require reporting of certain information to tax authorities annually	Generally foreign investment trusts are not subject to Japanese corporate tax. Foreign corporate funds are generally not subject to Japanese corporate tax (except certain Japan source income) provided that there is no permanent establishment in Japan There are no tax reporting requirements for the foreign fund itself; however, there are information sharing requirements for the withholding tax agent in Japan	Foreign funds may be subject to withholding tax on interest or dividend , earned in Japan	CIVs should be eligible (although some technical uncertainty remains)
Korea	A qualified trust type fund is not a taxable entity and not subject to income tax (it is however subject to annual "license tax" of KRW 45,000 (approx. USD 40)) A corporate type fund is subject to the normal corporate income tax. However, a qualified fund is entitled to a dividend declaration deduction	A qualified trust type fund is not subject to tax filing obligations. A corporate type fund is in principle subject to the normal corporate income tax filing	Unless a foreign fund has a permanent establishment ("PE") in Korea, it is not subject to any tax filing/reporting requirement. However, a local distributor of the fund is liable to deduct withholding tax at the time of remitting the profits from the foreign fund to the Korean individual investors and subject to the withholding tax filing requirement	Withholding tax applies	A reduced treaty rate on dividends/interest and exemption on capital gains may be available

Appendix 4: Key tax considerations for CIVs in each jurisdiction (cont'd)

	Taxation of the fund			Withholding tax	Double tax agreements
	How would each of the fund vehicles in your jurisdiction be regarded for tax purposes?	What are the tax implications for a domestic fund domiciled in your jurisdiction, including annual reporting requirements?	What are the ongoing tax implications for a foreign fund being distributed into your jurisdiction?	What income withholding tax or capital gains withholding tax exposures arise on investments held in your jurisdiction?	To what extent can domestic funds benefit from double tax treaties?
Malaysia	Generally taxed as a company however tax exemptions apply for most of the investments made by a unit trust REITs can achieve tax transparency provided 90% of its current year chargeable income is distributed	Filing of tax returns and paying tax (if any) as a normal company	Foreign funds cannot be distributed directly into Malaysia unless approval has been obtained from the Securities Commission and are made through domestic licensed fund managers	A withholding tax mechanism operates for payments to investors depending on the class (ie individuals or foreign investors)	Tax treaties should be applicable
Singapore	Fund vehicles are generally exempt from tax provided they apply for the various tax incentives offered for certain types of investment income	Annual tax filing is required despite the fund being exempt from tax	None	Withholding tax will only apply in certain cases for non-exempt dividend income	Potential benefits, but not clear as of yet
Taiwan	The fund itself is not a tax assessable entity	No tax or reporting requirements for the fund	None for the fund itself, except with regards to withholding tax. The Fund is liable to withholding tax when it distributes assessable income to underlying investors (domestic funds rarely distribute income to underlying investors)	Generally, interest income from domestic bond investments is subject to withholding tax. Withholding tax rate for interest income is higher for offshore investors, and dividend income derived by offshore investors would be subject to income tax If offshore investor has a permanent establishment in Taiwan, capital gains from securities trading would be subject to Alternative Minimum Tax	Taiwan adopts a look-through approach for funds that seek to access tax treaty benefits. If the underlying investors are tax resident and beneficial owners of the underlying income, tax treaty benefit may apply
Thailand	Thai mutual fund established under the Securities law is not subject to tax	Thai mutual fund is not required to file tax returns	Foreign funds are not subject to tax in Thailand. No annual tax reporting is required	The foreign investor is subject to 15% withholding tax on capital gain. However the rate may be reduced or exempt by the virtue of certain double tax treaty agreement	The domestic funds established under the Securities Law is not tax entity so they will not be entitled to benefit from double tax treaties

Appendix 5: Key tax considerations for investors in each jurisdiction

	Taxation of investors		
	What are the tax implications for an individual resident in your territory investing in a domestic fund?	What are the tax implications for an individual resident in your territory investing in a foreign fund?	What are the tax implications for non-resident individuals or entities investing in domestic funds in your jurisdiction? For example, how are non-resident individuals or entities taxed in your jurisdictions on income and gains arising in the fund?
Australia	Australian resident individuals investing in Australian funds are taxed on their share of the tax net income (including capital gains) of the fund in the year in which their present entitlement arises. This applies irrespective of whether the actual distribution from the fund is paid in a subsequent year The disposal of units in the fund will have capital gains tax implications. Australian individual investors are taxed on income at their marginal tax rate (up to 45% plus Medicare levy). Capital gains (on assets held for more than a year) may be taxed at concessional rates	The Foreign Investment Fund (FIF) regime has now been repealed and replaced by the proposed Foreign Accumulation Fund (FAF) rules (anti-roll up provisions) Unlike the FIF rules, Foreign funds will only be regarded as FAFs if they meet the legislative definition. Broadly, the FAF regime is directed at schemes entered into by an investor where they acquire an interest in a FAF with the sole or dominant purpose of obtaining a 'tax deferral benefit' and tax may be assessed on the fund when the Commissioner makes a written determination More substantial investments may be taxed under the Controlled Foreign Company (CFC) rules. In this case, the investor may be taxed on an accruals basis on a share of the income of the foreign fund even if not distributed by the foreign fund. The CFC rules are currently under reform	Foreign investors are assessable on their Australian sourced income Distributions of interest or unfranked dividends to non-residents may be subject to Australian withholding tax at the general rate of 10% and 30%, respectively. The rate on unfranked dividends is generally reduced to 15% (or potentially less) under a double tax agreement (where applicable). Franked dividends are free of withholding tax Where the fund is a managed investment trust, certain distributions of Australian sourced income or capital gains from taxable Australian property made to foreign investors will be subject to a 30% rate of withholding. This rate is reduced where the recipient is a resident of a foreign jurisdiction with which Australia has effective exchange of information on tax matters. The countries and territories that qualify as an “information exchange country” for these purposes are prescribed in Australian taxation regulations. The reduced rate of withholding is 15% for the 2009/10 income year and 7.5% for later income years
China	Individual resident is free of income tax	Unclear	Unclear
Hong Kong	Provided an individual is making a personal investment, they are not subject to tax in Hong Kong on their investment income and gains If however, the individual is investing in the course of running a business, any investment gains and losses would be regarded as business revenue and treated for tax accordingly	Tax implications are as for a domestic fund	For authorised funds there is no withholding tax and there are no reporting requirements
India	An individual investor would be liable to capital gains tax in cases where units of Mutual Funds are sold. The tax rate may vary from 0-30% depending on the nature of the income, type of scheme invested in and the period of holding the unit. Individuals are taxed at a progressive rate	Residents and ordinary residents are taxed on their worldwide income. The tax rate may vary from 20-30% depending on the nature of the income, type of entity invested in and period of holding. Individuals are taxed at a progressive rate	A foreign investor under the domestic laws would be liable to capital gains tax in cases where units of Mutual Funds are sold. The tax rate may vary from 0-40% depending on the nature of the income, type of entity, type of scheme invested in and period of holding the unit

Appendix 5: Key tax considerations for investors in each jurisdiction (cont'd)

	Taxation of investors		
	What are the tax implications for an individual resident in your territory investing in a domestic fund?	What are the tax implications for an individual resident in your territory investing in a foreign fund?	What are the tax implications for non-resident individuals or entities investing in domestic funds in your jurisdiction? For example, how are non-resident individuals or entities taxed in your jurisdictions on income and gains arising in the fund?
Indonesia	Income received by individual resident (unit holder) from Mutual Fund is not subject to tax	Subject to Individual Income Tax at progressive rate, max. 30%	Income and gains received by non-resident individuals or entities investing in domestic Mutual Funds is not subject to Indonesian tax
Japan	Distributions from domestic funds (ie Japanese investment trusts) are subject to withholding tax at the rate of 20% (reduced to 10% until 31 December 2011, provided the fund is a publicly offered stock investment trust) If the domestic stock fund is not publicly traded, the distribution is subject to income tax at progressive individual income rates (up to 50%), reportable upon filing a Japanese individual tax return. The withholding tax should generally be creditable against the Japanese individual investor's final tax liability Capital gains realised by Japanese individual investors from the sale of units in a domestic stock fund is subject to income tax at the rate of 20% (however, a transitional rate of 10% applies to capital gains on publicly offered stock investment trust until 31 December 2011 where the sale is made to, or through, a broker-dealer acting in Japan) Capital gains realised by Japanese individual investors from the sale of units in a domestic bond fund is not subject to income tax	The tax implications for a Japanese individual investor investing in a foreign investment trust are generally the same as those relating to an investment in a domestic fund where the distribution is made through a payment handling agent in Japan However, where the distribution is made directly (not through a payment handling agent in Japan), withholding tax is not imposed, however, the income is subject to income tax at progressive individual income rates (up to 50%), reportable upon filing a Japanese individual tax return Japanese CFC rule may apply to the foreign corporate fund under certain conditions	Dividends paid by a domestic fund to non resident individuals or entities without a permanent establishment in Japan are subject to Japanese withholding tax at the rate of 20% (reduced to 7% until 31 December 2011 and 15% thereafter, provided the domestic fund is publicly offered stock investment trust) for stock investment trust and 15% for bond investment trust, subject to the availability of any treaty relief Under Japanese tax law, non resident individuals or entities without a permanent establishment in Japan are not subject to capital gains tax on the disposal of units in Japanese investment trust
Korea	Profit distributions from a qualified trust type fund are taxed as dividends in the hands of the investors and subject to withholding tax at 15.4%. Where the sum of dividend and interest income derived by a Korean individual during a year exceeds KRW 40 million (approx. USD 35,000), the excess is subject to global taxation at the individual's progressive marginal tax rate of up to 38.5% with a credit for an interim withholding tax	Profit distributions from a foreign fund are generally characterized as dividends in the hands of the Korean investors regardless of the legal form of the foreign fund. A Korean paying agent (including a local distributor of a foreign fund) is required to deduct withholding tax at 15.4% at the time of distributing the profits from the fund to the individual investor	The foreign investor may be entitled to a reduced withholding rate on dividends (eg 10~15%) and an exemption on capital gains is available. Without treaty protection, the domestic withholding tax (22% for dividends, the lower of 11% of sale proceeds and 22% of gain for capital gain) would apply

Appendix 5: Key tax considerations for investors in each jurisdiction (cont'd)

	Taxation of investors		
	What are the tax implications for an individual resident in your territory investing in a domestic fund?	What are the tax implications for an individual resident in your territory investing in a foreign fund?	What are the tax implications for non-resident individuals or entities investing in domestic funds in your jurisdiction? For example, how are non-resident individuals or entities taxed in your jurisdictions on income and gains arising in the fund?
Malaysia	Individuals are generally exempt from tax on unit trust distributions received. If it is REIT distributions, there would already be a 10% withholding tax deducted. No capital gains tax regime in Malaysia for investments in securities or funds	Normally tax exempt unless such gains are regarded as part of the business of dealing in investments by the individual	Generally no tax unless a permanent establishment is in Malaysia. Certain investments such as REITs would have a withholding tax which will be deducted (eg REIT withholding tax at 25% for foreign corporations and 10% for foreign institutional investors)
Singapore	No tax implication. There is no capital gains tax in Singapore, and income from investment is tax-free	None	None
Taiwan	Generally, if a domestic fund distributes assessable income to individual residents, income tax may apply depending on the nature of distributed income (although this is rarely seen in practice). Dividend income is income tax exempt if the investor is domestic tax resident. Capital gains from trading Taiwanese securities are generally exempt from income tax	Income derived from investments in offshore funds is regarded as foreign source income, which is subject to Alternative Minimum Tax at the rate of 20% (with an exemption threshold of NTD 6 million)	Interest and dividend income distributed by domestic funds to non-resident individuals or entities are subject to withholding tax. Withholding taxes may differ and the reduced tax rate on treaty depends on residency of beneficial owners of such investment. Capital gains from redemption of units of a Taiwanese fund are generally exempted from income tax
Thailand	Profit sharing is subject to 10% withholding tax Redemption gain is subject to personal income tax at progressive rate (including with other income) Gain on sales of unit trust is exempt	Income from investing in a foreign fund is subject to Thai personal income tax at progressive rate (including with other income) if such income is brought into Thailand within the same calendar year as receiving such income	Non-resident entities are not taxed on the gains and income from investment in domestic funds. Non-resident individuals are subject to tax on gains and income from investment in domestic funds on progressive rate. The payer is not required to deduct the tax when making the payment of such income to non-resident individuals. Therefore, it is the duty of non-resident individuals to pay tax in Thailand

Appendix 6: Current arrangements for distribution of foreign CIVs in the Asia region

	Australia	China	Hong Kong	India	Indonesia	Japan	Korea	Malaysia	Singapore	Taiwan	Thailand
Does the jurisdiction have a system of recognition of foreign funds for distribution to the public?	Yes, but currently limited to those in recognised jurisdictions	No	Yes. The SFC may accept that some schemes already comply in substance with certain provisions of the Unit Trust and Mutual Funds Code by virtue of prior authorization in a regulated jurisdiction	No	No	Yes, but currently limited to those in recognised jurisdictions	No	No	Yes, but currently limited to those in recognised jurisdictions	No	Currently, SEC allows only foreign issuer who has listed securities in their home countries to be listed in Stock Exchange of Thailand
If so, which countries have achieved recognition?	Hong Kong, New Zealand, UK, Guernsey, Jersey, Isle of Man, Singapore, USA and Germany	Not applicable	Australia, France, Germany, Guernsey, Ireland, Isle of Man, Jersey, Luxembourg, Malaysia Taiwan, UK, USA	Not applicable	Not applicable	Luxemburg, Ireland and Cayman	Not applicable	Not applicable	Luxembourg and Ireland	Not applicable	Not applicable

Glossary

Asia Region Funds Passport

A multilateral framework which would enable a complying fund in a nation that signs up to the Passport framework to offer that product in each of the other signatory nations.

Asian region or the region

The jurisdictions covered by the survey being Australia, China, Hong Kong, India, Indonesia, Japan, Korea, Malaysia, Singapore, Taiwan and Thailand.

CIV or Collective Investment Vehicle

Collective investment vehicle referring to all of the different structures used for funds management, commonly taking the form of unit trusts. We have used the terms ‘CIV’ and ‘funds’ interchangeably.

Disclosure document

The document for each fund that sets out the key considerations for that fund. It typically includes such information as the investment strategy, fees and risks.

EU

European Union

FUM

Funds under management.

Funds management

The collective or mutual pooling of financial assets to take advantage of investment management services.

Promoter

The promoter, or issuer of securities is the entity responsible for creating the CIV.

UCITS

Undertakings for Collective Investment in Transferable Securities issued under a series of European Union directives.

About the report

PwC partnered with the Financial Services Council in the preparation of this report.

This report in relation to the Asia Region Funds Passport proposal is based on a survey conducted in September and October 2010, together with other research and analysis. Respondents to the survey were from industry bodies, a wide range of organisations operating in the industry and member firms of the PwC network throughout the Asia region.

The survey questions covered the opinions and attitude of market participants and industry bodies and sought to collect factual information about the regulatory and operating environment in each country.

Survey responses were received from Australia, China, Hong Kong, India, Indonesia, Japan, Korea, Malaysia, Singapore, Taiwan and Thailand.

This report provides an overview of the survey findings, together with analysis and interpretation of the results.

We thank the respondents for their time and insight.

Important Notice

This report is based on data collected from industry bodies, PwC network firms in the Asia Pacific region and a range of other organisations, and information published by other third parties. PwC Australia has not independently verified the information provided by survey respondents and makes no representation or warranty in relation to the accuracy or completeness of the data collected. In addition, in completing the surveys, no member firm in the PwC network performed detailed reviews of the legislative requirements, the interpretation of which is normally handled by legal firms. Rather the information is based on the experience and observations of practice in the relevant jurisdictions.

Any expressions of opinion (direct or implied) that are distillations or interpretations of the responses from the surveys do not represent the views of PwC Australia or any other PwC network firm.

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