



## **RESPONSE TO FEEDBACK RECEIVED – CONSULTATION ON REVIEW OF THE REGULATORY REGIME FOR FUND MANAGEMENT COMPANIES AND EXEMPT FINANCIAL INTERMEDIARIES**

### **1 Introduction**

1.1 On 27 April 2010, MAS conducted a consultation on the review of the regulatory regime for Fund Management Companies (“FMCs”) and exempt financial intermediaries (the “Consultation Paper”).

1.2 The consultation closed on 31 May 2010. MAS thanks all respondents for their comments on the proposals. A list of respondents is attached in Annex 1. MAS’ responses to comments which are of wider interest are set out below.

### **2 Proposed clientele for Notified FMCs (“NFMCs”) and Licensed Accredited/Institutional FMCs (“A/I LFMCS”)**

#### Institutional Investors and General Partners

2.1 Some respondents sought clarification on whether NFMCs will be able to serve institutional investors<sup>1</sup>. A number of respondents also asked whether a General Partner (“GP”) in limited partnership fund structures, which may not meet the accredited investor definition, can be allowed to hold interests in funds managed by NFMCs and Licensed A/I FMCs. In a typical limited partnership fund structure, the GP would typically be the FMC itself, or a holding company controlled by the FMC, while third party investors would participate as Limited Partners (“LPs”).

#### MAS’ Response

2.2 MAS will align the clientele class restrictions for NFMCs and A/I LFMCS. Both NFMCs and A/I LFMCS will be allowed to serve institutional investors. Although the range of institutional investors includes collective investment schemes (“CIS”) in general, NFMCs and A/I LFMCS will only be allowed to manage CIS, as well as closed-end funds, where the immediate underlying investors are all accredited and/or institutional investors<sup>2</sup>. NFMCs and A/I LFMCS should not circumvent the clientele class restrictions by the use of innovative investment vehicles to target retail investors.

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<sup>1</sup> As defined in Section 4 of the Securities and Futures Act.

<sup>2</sup> As referred to in the Securities and Futures (Licensing and Conduct of Business) (Amendments) Regulations 2008, to be read in conjunction with the Consultation Paper P011 – 2007, issued in Oct 2007.

2.3 MAS will also allow NFMCS and A/I LFMCS to serve limited partnership fund structures regardless of whether the GP can meet the accredited investor definition, so long as (i) the GP is ultimately owned by the key officers and/or shareholders of the FMCs, and (ii) the LPs are accredited investors and/or institutional investors.

2.4 However, MAS clarifies that the total number of clients served by NFMCS will continue to be limited to 30, and this will include Qualified Investors, institutional investors and limited partnerships fund structures, of which a total of no more than 15 can be funds (including feeder funds) and/or limited partnerships fund structures.

#### Employee Investments

2.5 Several respondents suggested that employees of NFMCS and A/I LFMCS, who do not meet the definition of an accredited investor (“AI”), be allowed to invest in funds managed by their employer. Respondents highlighted that employees’ investments would be a way to align their interests with other investors and the FMC.

#### MAS’ Response

2.6 MAS will only allow AI employees to invest in funds managed by NFMCS and A/I FMCs as such investors are better able to protect their own interests.

2.7 MAS will implement client priority and disclosure requirements to address potential conflicts of interests arising from employee investments. FMCs will be expected to put in place controls to ensure that these requirements are adhered to, if their employees are invested in the funds they manage.

### **3 Proposed Competency Requirements for FMCs**

#### Two Experienced Professionals

3.1 Most respondents agreed with the proposed competency requirements for FMCs. Several respondents, however, expressed concerns over potential cost burden to smaller FMCs, arising from the proposed requirement for two experienced individuals to be based in Singapore. Some respondents also highlighted practical difficulty in locating two investment professionals in Singapore when the bulk of the FMC’s investments are overseas, for example, in the case of most private equity or venture capital firms.

#### MAS’ Response

3.2 The rationale for requiring FMCs to have at least two experienced individuals based in Singapore is to ensure that there is adequate oversight and accountability for the FMC and to ensure an adequate level of checks and balances in the operations and conduct of the FMC. As such, MAS will require FMCs to meet the competency requirements as set out in the consultation paper.

### Feedback

3.3 Some respondents sought clarification on whether experience in proprietary trading with investment banks or licensed financial institutions or experience in legal and accounting functions in relation to the operations of a FMC, could be counted towards meeting the five year relevant experience requirement.

### MAS' Response

3.4 Proprietary traders in licensed financial institutions and persons with prior experience in supporting functions such as legal and accounting at financial institutions can satisfy the requirement for two professionals. The relevance of their prior experience should be assessed in the context of the role they will perform in the FMC.

## **4 Proposed Custody and Fund Administration Requirements**

### Custody Arrangements

4.1 Respondents were generally supportive of the proposal for all FMCs to place their customers' monies and assets with a third party custodian, which is licensed, registered or authorized in the jurisdiction where the monies or assets are being held. Some respondents sought clarification on whether they would be able to meet the proposed custody requirements by using global custodian arrangements, prime brokers, futures brokers or banks to hold clients' monies.

### MAS' Response

4.2 FMCs placing their client's assets and monies in a proper segregated accounts with third party financial institutions such as prime brokers, futures brokers and banks would generally be able to meet the proposed custody requirements. FMCs will also be able to place clients' assets with a global custodian who uses sub-custodians to hold client assets in the respective jurisdictions. In such cases, MAS expects that the global custodian and its sub-custodians would be suitably licensed, registered or authorized in their respective jurisdictions.

### Fund Administration

4.3 Respondents agreed with the proposal for FMCs to ensure that they have an independent fund administration function. Some respondents sought guidance on the level of segregation and independence expected of an FMC when the fund administration functions are performed in-house or by a related entity.

### MAS' Response

4.4 FMCs are expected to identify and manage conflicts that may arise as a result of the multiple roles and functions that they perform in the course of business. In managing such conflicts, they must be able to clearly demonstrate the effectiveness of the segregation of conflicting functions, for example, through having independent management reporting lines or physical segregation. Where the FMC is unable to

adequately enforce segregation, it should engage an external fund administrator to satisfy the proposed fund administration requirement.

#### Private Equity and Venture Capital Funds

4.5 Respondents representing private equity or venture capital (“PE/VC”) firms sought clarification on the applicability of the custody and fund administration requirements to PE/VC assets. It was noted that PE/VC assets are typically made in unlisted securities which are neither readily convertible to cash nor easily transferable, and that fund administration for PE/VC funds is largely carried out in-house by the FMC as third party valuations are not readily available for PE/VC assets.

#### MAS’ Response

4.6 MAS notes the concerns raised by FMCs who invest in PE/VC assets. Where a PE/VC fund is only offered to underlying investors who are accredited and/or institutional investors, MAS will require the FMC to either:

- a) Fully comply with the requirement on independent custody of clients’ assets and monies; or
- b) Obtain written acknowledgement from investors that they are aware that the custody arrangements for PE/VC assets do not meet regulatory requirements, and arrange for an independent auditor to audit and report to investors on the PE/VC fund assets on an annual basis.

4.7 The alternative set out at paragraph 4.6(b) will only apply to PE/VC assets. Notwithstanding this, FMCs managing PE/VC funds will continue to be required to fully comply with client segregation requirements for client monies<sup>3</sup>. MAS will provide further guidance on qualifying PE/VC assets in relation to the custody requirement.

4.8 With regards to fund administration function, MAS will maintain the proposed requirement for all FMCs, including PE/VC FMCs. This is necessary to provide for adequate checks and balances in valuation and reporting. We note the difficulty in arranging for PE/VC assets to be independently valued. The valuation function may be performed in-house provided that conflicts of interest are adequately mitigated with proper segregation of duties and responsibilities. In cases where proper segregation cannot be achieved, FMCs should engage an independent party to perform fund administration and valuation.

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<sup>3</sup> The handling of client money will continue to be subject to the trust account provisions in the Securities and Futures (Licensing and Conduct of Business) Regulations.

## Real Estate/Infrastructure Funds

4.9 Respondents who manage private real estate and infrastructure funds sought clarification on the applicability of the proposed custody and fund administration requirements to immovable assets such as real estate and infrastructural property. The respondents also highlighted that these real estate managers typically engage in the business of development, marketing and leasing of properties, as distinct from the management of securities portfolios.

### MAS' Response

4.10 The regulatory regime for FMCs is geared towards the regulation of fund management activity where the underlying investments are in financial assets rather than physical assets. With the exception of REITs, which are recognized under the SFA as a separate regulated activity from fund management and regulated because REITs are offered to retail investors, it has not been MAS' intent to regulate real estate managers who deal with sophisticated investors.

4.11 Considering MAS' fundamental regulatory intentions and the clientele profile for private property funds, MAS will exempt from licensing managers of funds that invest purely in physical or immovable assets, provided that the funds are offered only to accredited and/or institutional investors.

## **5 Proposed Requirement for Compliance Arrangements**

5.1 A few respondents sought clarification on the types of compliance arrangements which meet the proposed requirement in the consultation paper. Respondents also queried on the expected qualifications of compliance staff.

### MAS' Response

5.2 While the use of Head Office ("HO") compliance function is acceptable for A/I FMCs and NFMCS, MAS expects the FMC in Singapore to demonstrate that the HO compliance function has designated adequate resources to handle the compliance needs of the FMC. In such cases, MAS also expects that there is an independent and dedicated compliance team at HO. Outsourced service providers may be used for A/I FMCs and NFMCS, and will be viewed favourably if the service provider is a member of a professional body, and has significant and meaningful onsite presence in the FMC. Regardless of the compliance arrangements, the Chief Executive Officer ("CEO") and Board of Directors of the FMC will be ultimately responsible for compliance.

5.3 Dedicated compliance officers may perform other non-conflicting roles to complement their functions. For example, a compliance officer may also concurrently assume the role of an in-house legal counsel for the FMC.

5.4 The CEO and Board of Directors of the FMC are expected to assess the relevance of the qualification of the compliance staff, having regard to the type and size of fund operations for the FMC.

## **6 Proposed Capital Requirements**

### Base Capital Requirements

6.1 While some respondents were supportive of the base capital requirements, other respondents had concerns on the requirement to maintain base capital of at least S\$250,000 at all times. Some respondents queried on the amount of additional capital buffer that FMC should maintain, in addition to the proposed minimum base capital.

### MAS' Response

6.2 The maintenance of base capital is important to ensure business continuity in times of turbulent markets or operational shocks. Given the disparate scope and scale of business models across the industry, FMCs should make a reasonable assessment of the amount of additional capital buffer required, as part of their business risk management in accordance to the scale and size of their operations.

### Operational Risk Requirement

6.3 Several respondents suggested the use of operating expenses, instead of gross income, as the basis for computing the operational risk requirement (“ORR”), explaining that expenses provided a better reflection of how much capital a licensed FMC should maintain to support their operations. Respondents also sought clarification on whether performance fees could be excluded from the gross income measure as the inclusion of such fees would increase the volatility of the ORR.

### MAS' Response

6.4 Computing the ORR based on operating expenses may potentially disincentivise expenditure on middle and back-office operations by licensed FMCs. A measure based on operating expenses may also not be appropriate as licensed FMCs could have similar levels of operating expenses but vary significantly in the scale of their activities and their operational risks.

6.5 Only income or expenses arising from activities which do not form part of the ordinary activities of the firm and which do not recur frequently or regularly may be excluded. Performance fees are derived from the ordinary activities of the firm and should not be excluded from the computation of the ORR. The changes proposed to the computation of the ORR, specifically the use of a three-year average of gross income and the deductions of key expense items such as staff bonuses, would reduce the volatility of the ORR.

### Scope of Deductions

6.6 Respondents queried on the scope of staff bonuses that may be deducted from the gross income measure, and whether dividend payments to key officers holding shares in the licensed FMC may be deducted from gross income as a proportion of principals' income could be in the form of dividend payments rather than staff bonuses. Respondents were also concerned that allowing deductions of staff bonuses may disadvantage licensed FMCs with remuneration structures that relied less on staff bonuses.

### MAS' Response

6.7 MAS had proposed the deduction of staff bonuses, commission and interest expenses from the gross income measure as these are key expense items that fluctuate with income. All forms of non-guaranteed staff bonuses that are reported as expenses in the audited statements submitted to MAS may be deducted from the gross income measure in computing ORR. Dividend payments to principals should not be deducted from the gross income measure as these are not expense items.

### Floor on Operational Risk Requirement

6.8 To maintain the proportionality of the ORR across licensed FMCs with differing remuneration structures and ensure that a minimum level of capital is being maintained for operational risks, MAS will introduce an additional ORR floor of 5% of the three-year average of gross income, before the deduction of staff bonuses, commission and interest expenses. Licensed FMCs will hence be subject to a minimum floor of the higher of \$100,000 or 5% of the three-year average of gross income (before deductions).

## **7 Provision of Sub-Advisory Services to another FMC**

7.1 Respondents sought clarification on the regulatory treatment of sub-advisors, i.e. persons who only carry out research and advisory functions in Singapore on behalf of clients who are fund managers, as well as on MAS' position on sub-advisors being named in prospectuses, offering documents or marketing materials of funds managed by another fund manager.

### MAS' Response

7.2 Sub-advisors whose research and advisory services are provided to other fund managers would generally be considered to be conducting fund management activity and be regulated under the SFA. A sub-advisor in Singapore may only operate under the Financial Advisers Act ("FAA"), either as a licensed or exempt financial advisor, if it does not carry out functions which constitute fund management, whether in form or in substance. MAS will consider a sub-advisor to be conducting fund management activity if –

- (a) the sub-advisor has discretion over the construction of its client's portfolio;

- (b) the sub-advisors and/or its key officers are able to exercise control over its client;
- (c) the sub-advisor is named in the prospectus, offering documents or marketing materials circulated by its client or representatives of its client; or
- (d) the sub-advisor has full knowledge of, or access to the holdings of the client's fund or portfolio.

## **8 Transitional arrangements for existing FMCs**

8.1 Respondents sought clarification on the transitional arrangements for licensed Boutique Fund Managers ("BFMs") and Start-up BFMs, as well as for existing exempt fund managers ("EFMs"). Some respondents queried if MAS would continue to accept new EFM lodgments until the proposed regime comes into effect.

### MAS' Response

8.2 The current regulatory regime for FMCs will remain status quo until legislative amendments are implemented to give effect to the proposed regulatory regime set out in the consultation paper. BFMs and Start-up BFMs which already hold a Capital Markets Service Licence will not need to reapply for a new licence under the A/I FMC regime. Existing EFMs will be required to either notify MAS of their commencement of business as a NFMC or to apply for a licence during the transitional period.

8.3 MAS will be issuing draft amendments to the legislations to implement the proposals outlined in the Consultation Paper and in this Response Paper, and will consult the industry on these amendments in due course.

**MONETARY AUTHORITY OF SINGAPORE**  
**28 September 2010**



**LIST OF RESPONDENTS TO POLICY CONSULTATION ON REVIEW OF REGULATORY REGIME FOR FUND MANAGEMENT COMPANIES AND EXEMPT FINANCIAL INTERMEDIARIES**

- 1 Accel-X Management Pte Ltd
- 2 Aisling Analytics Pte Ltd
- 3 AI Wealth Partners Pte Ltd
- 4 Allen & Gledhill LLP
- 5 Allen & Overy LLP
- 6 Alpha Advisory Pte Ltd
- 7 Alpha Investment Partners Limited
- 8 AXA Rosenberg Investment Management Asia Pacific Ltd
- 9 Baker & McKenzie.Wong & Leow
- 10 Bamboo Capital Pte Ltd
- 11 BB Asia Investments Pte Ltd
- 12 Beaconsfield Investment Management Pte Ltd
- 13 Bollard Strategic Advisers Pte Ltd
- 15 Boswell Capital Management Pte Ltd
- 16 Capitaland Limited
- 17 CarVal Investors Pte Ltd
- 18 Clifford Chance Pte Ltd
- 19 ComplianceAsia Consulting Pte Ltd
- 20 Copar Finance Asset Management Singapore Pte Ltd
- 21 DBS Bank Ltd
- 22 Deloitte & Touche LLP
- 23 Dollars Pounds Holdings Pte Ltd
- 24 Duxton Asset Management Pte Ltd
- 25 EOF Services (Asia) Pte Ltd
- 26 Equine Capital Pte Ltd
- 27 Ernst & Young LLP
- 28 FIL Investment Management Singapore Ltd
- 29 Firth Investment Management Pte Ltd
- 30 Harry Elias Partnership LLP
- 31 Haven Capital Pte Ltd
- 32 Helvetic Investments Pte Ltd
- 33 High Value Management Pte Limited
- 34 IL&FS Singapore Asset Management Company Pte Ltd
- 35 Independent Asset Managers
- 36 KMA Financial Advisory Pte Ltd
- 37 Kunlun Capital Pte Ltd
- 38 Larkfield Asset Management Pte Ltd
- 39 Lighthouse Advisors

- 40 LIM Investment Management Pte Ltd
- 41 Lotus Peak Capital Pte Ltd
- 42 Managed Funds Association
- 43 Morgan Stanley Asia Ltd
- 44 Octagon Capital Management Pte Ltd
- 45 Pangolin Investment Management Pte Ltd
- 46 Pemberton Investments Pte Ltd
- 47 Phillip Private Equity Pte Ltd
- 48 Phillip Securities Pte Ltd
- 49 Rajah & Tann LLP
- 50 Rexiter Capital Management Limited
- 51 Schroder Investment Management (Singapore) Ltd
- 52 Shidan Capital Pte. Ltd.
- 53 ShookLin & Bok LLP
- 55 Singapore Venture Capital and Private Equity Association
- 56 Stat Arb Pte Ltd
- 57 State Street Bank and Trust Company, Singapore
- 58 The Alternative Investment Management Association Limited - Singapore Branch
- 59 Trust Company (Asia) Limited
- 60 United Overseas Bank Ltd
- 61 Willis (Singapore) Pte Ltd
- 62 Wong Partnership LLP