

## **Proposals to establish a Limited Partnership Regime for Funds**

### **PURPOSE**

1. This paper sets out the Government's proposals to establish a limited partnership regime specifically for use by investment funds in Hong Kong.

### **BACKGROUND**

2. We have witnessed in recent years fast economic growth and wealth creation in Asia, increase in portfolio allocation to the Asian markets, and deepening financial market liberalisation in Mainland China. All these have contributed to Hong Kong's strong position as a premier international asset and wealth management ("WAM") centre in the region. The Government has been working to sharpen Hong Kong's competitive edge on WAM through a multi-pronged approach. Diversification of the structure that a fund can take to establish in Hong Kong is one of the key policy initiatives.
3. In recent years, private equity ("PE") funds are gaining popularity amongst investors and have become a key impetus to the growth of WAM business. As at end-2018, the total capital under management by some 520 PE firms operating in Hong Kong reached about HK\$1.21 trillion<sup>1</sup>. This puts Hong Kong second in Asia, after Mainland China. With an active initial public offering market for PE-backed companies and proximity to Mainland China with the availability of major PE deals, Hong Kong is well placed to expand its PE business.
4. Currently, a fund may be established in Hong Kong in the form of a unit trust or an open-ended fund company. These fund structures are, however, more popular among public funds or hedge funds. Meanwhile, it is more common for PE funds to be established in the form of a limited partnership.
5. In Hong Kong, our Limited Partnerships Ordinance (Cap. 37) ("LPO") was enacted about a century ago. It is not tailored to and cannot quite meet the needs of investment funds which are a relatively modern invention. For example, the LPO does not have

---

<sup>1</sup> Source: Asian Venture Capital Journal.

provisions which allow flexibility in capital contributions and distribution of profits, or allow a fund to have the necessary contractual flexibility, or provide a straightforward winding-up mechanism. The absence of these features under the LPO discourages fund managers from establishing PE funds in Hong Kong in the form of a limited partnership and hampers the development of a more thriving domestic PE market locally. At the moment, PE funds in Asia are typically established under the limited partnership regime in other jurisdictions such as the Cayman Islands.

6. The industry has been calling for an early introduction of a tailor-made limited partnership regime for attracting investment funds to establish and operate in Hong Kong. This will bring more jobs and business opportunities to the local fund and related industries. The industry also points out that it would be vital to grasp the opportunity of potential shifting of fund structures and activities from offshore to onshore, as a result of Base Erosion and Profit Shifting package of the Organisation for Economic Co-operation and Development which requires taxation to happen where asset management activities take place. This development should incentivise the funds to align their structures with business activities. Against such a backdrop, the Financial Secretary announced in his 2018-19 Budget that the Government would examine the feasibility of introducing a limited partnership regime specifically for funds in Hong Kong.
  
7. A task force led by the Financial Services Branch and comprising members from the Hong Kong Monetary Authority, the Securities and Futures Commission (“SFC”), the Treasury Branch and the Inland Revenue Department is looking into the matter and has come up with the proposals as set out in paragraphs 8 to 30 below. In doing so, the task force has taken into account the local market landscape, overseas regulatory experience<sup>2</sup>, as well as international market and regulatory trends. The objective is to facilitate industry development whilst maintaining market integrity and investor protection.

---

<sup>2</sup> Such as that of Cayman Islands, Delaware/USA, the United Kingdom, Ireland, Luxembourg and Singapore.

## **THE PROPOSALS**

8. We propose that Hong Kong should introduce a new piece of legislation to put in place a limited partnership regime specifically for funds<sup>3</sup> (“the LPF regime”).

### **Proposed key characteristics of a LPF**

9. Similar to the regime under the LPO and the common overseas practice in major fund formation centre, the LPF regime will be a registration scheme. A LPF will be an arrangement which shall meet the definition of a fund<sup>4</sup> that is structured in a limited partnership form and will be used for the purpose of managing investments for the benefit of its investors (i.e. the limited partners). The proposed LPF structure is not in itself a legal person. Like other limited partnerships, the general partner of a LPF has unlimited liability in respect of the debts and liabilities of the fund and ultimate responsibility for the management and control of the fund. Meanwhile, the limited partner(s) of a LPF, whose liability will generally be limited up to the commitment they make to the fund, will not have day-to-day management rights or control over the underlying assets held by the LPF. They, however, will have the right to participate in the income/profits arising from the management of the LPF’s assets and transactions.

---

<sup>3</sup> We do not recommend amending the LPO in order not to inadvertently affect non-fund limited partnerships already formed (which include game centres, restaurants and consulting firms) or to be formed thereunder. A standalone, self-contained piece of legislation catering for the needs of funds would also make it more user-friendly to the fund industry.

<sup>4</sup> The definition would draw reference to the definition of “fund” under section 20AM of the Inland Revenue Ordinance (Cap. 112) (“IRO”) and the definition of “collective investment scheme” under the Securities and Futures Ordinance (Cap. 571), with suitable modification as may be necessary.

10. A fund registering under the LPF regime –

- (a) shall have at least two partners (one general and one limited). The general partner shall be a private company limited by shares incorporated in Hong Kong.<sup>5</sup> A limited partner may be an individual, a corporation, a limited partnership or any other body corporate;
- (b) shall be constituted by a written agreement (i.e. commonly known as a “limited partnership agreement”);
- (c) shall have a registered office in Hong Kong; and
- (d) shall apply for a business registration certificate under the Business Registration Ordinance (Cap. 310).

11. There is no need for SFC authorization of the LPF in general, unless any of the LPF’s activities fall under the regulatory remit of the Securities and Futures Ordinance (Cap. 571) (“SFO”) and no exemption under the SFO is applicable.

12. Under the LPF regime,

- (a) the general partner of a LPF will have unlimited liability for all the debts and obligations of the LPF that cannot be satisfied from its assets;
- (b) the general partner shall appoint an investment manager to carry out the day-to-day investment management functions<sup>6</sup>;

---

<sup>5</sup> The general partner, as a private company incorporated in Hong Kong in accordance with the Companies Ordinance (Cap. 622), will have to comply with all the applicable requirements prescribed under Cap. 622 and other laws and regulations, including application for a business registration certificate under the Business Registration Ordinance (Cap. 310).

<sup>6</sup> The investment manager appointed by a LPF shall be either an authorized institution, a licensed corporation, an accounting professional or a legal professional as defined in Schedule 1 to the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) (see paragraph 24 below). If an investment manager carries out any business of regulated activities in Hong Kong as defined in the SFO, it shall obtain the appropriate licence(s) or registration(s) from the SFC pursuant to that ordinance.

- (c) the general partner shall appoint an auditor, which should be a practice unit under section 2(1) of the Professional Accountants Ordinance (Cap. 50)<sup>7</sup>, to carry out audits of the financial statements of the LPF annually in accordance with the Hong Kong Financial Reporting Standards or equivalent standards;
- (d) the general partner shall ensure that there are proper custody arrangements for the assets of a LPF;
- (e) the limited partner(s) will not be liable for the debts and obligations of the LPF beyond the amount they have agreed to contribute, unless the limited partner has participated in the substantive control of the LPF in a manner that falls outside the scope of the prescribed safe harbour activities (see paragraph 22 below); and
- (f) there will be no minimum capital requirement of or restriction on the investment scope for a LPF.

### **Registration requirements**

13. It is proposed that a fund wishing to register under the LPF regime shall submit an application to the Registrar of Companies (“RoC”). The application shall be submitted by a registered Hong Kong law firm or a solicitor admitted to practice Hong Kong law in Hong Kong on behalf of the fund (“the presenter of the application”). The application shall contain the following documents/information and a fee at a fixed amount –
- (a) the name of the LPF. The name must end with the words “Limited Partnership Fund” (or in Chinese, “有限責任合夥基金”);
  - (b) the full name, address and signature of the general partner, together with a copy of its Certificate of Incorporation and Business Registration Certificate issued by the Companies Registry and the Business Registration Office respectively;
  - (c) the address of the registered office of the LPF in Hong Kong;

---

<sup>7</sup> The practice unit appointed by a LPF as its auditor shall be independent of the general partner and the investment manager.

- (d) the investment scope and principal place of business of the LPF;
  - (e) the name of the investment manager appointed by the LPF and relevant identification number (if any)<sup>8</sup>;
  - (f) a declaration and undertaking from the general partner that the LPF intends to operate as a fund and the partnership is limited, together with an acknowledgement that it is an offence to make a fraudulent, false or misleading declaration or to provide false and/or inaccurate information in the application; and
  - (g) the full name and contact information of the presenter of the application. If the presenter is a solicitor practising in sole proprietorship, the identification number as well.
14. Upon receiving an application, if the RoC is satisfied that the application contains the documents/information made in the prescribed manner as set out in paragraph 13 above and a fixed fee (see paragraph 20 below) is paid, the RoC will register the fund as a LPF and issue a certificate of LPF to the general partner as proof of registration.
15. The registration of a LPF will remain valid subject to the filing of an annual return to the RoC by the general partner on behalf of the fund. The return shall include a declaration by the general partner that the LPF has been and will be in operation as a fund during the year, together with a fixed fee. Failure to file the annual return on time shall render the fund deregistered by the RoC.
16. If there is any change in the particulars provided upon registration, the general partner of a LPF shall inform the RoC within a specified period of time. A fixed fee will be charged by the RoC for making changes.

---

<sup>8</sup> For example, if the investment manager is licensed by or registered with the SFC, its central entity number. If it is a solicitor practising in sole proprietorship, the identification number given by the Law Society of Hong Kong. If it is an accounting professional, its registration number with the Hong Kong Institute of Certified Public Accountants.

## **Migration of LPO-fund**

17. Upon submission of the same documents/information as set out in paragraph 13 above, a fund already registered under the LPO can migrate to the LPF regime. Upon migration, the fund would have the same right and responsibility as any other LPF registered under the LPF regime (including the naming requirement as stated under paragraph 13(a) above). We will make it clear in the law that such migration will not affect the identity and continuity of the fund concerned. For example, all contracts, rights and obligations of the LPO-fund, as well as all legal proceedings by or against the LPO-fund will survive the migration. On the assumption that there is continuity of the LPO-Fund without any transfer of assets arising from the migration or change in beneficial ownership, there should be no profits tax and stamp duty implications.

## **The roles of the RoC**

18. The role of the RoC is a registrar for the LPFs, which is similar to her role performed under the LPO with regard to limited partnerships. It is the duty of an applicant to ensure that the documents/information submitted are factually correct and in order. Failure to provide documents/information which are factually correct and in order may have attendant legal consequences.
19. The RoC will maintain and publish a register of LPFs containing the documents/information submitted by a LPF in its application as mentioned in paragraph 13 (a), (b), (c), (e) and (g) and any subsequent changes reported. The register of LPFs will be open for public inspection upon payment of a fixed fee. Maintaining a register of LPFs will provide useful information to investors and parties which deal with a LPF. It is in line with the existing practice of publishing a register of companies.
20. The level of the fees for registration and filing of annual return under the LPF regime, as well as other services that the RoC will provide in relation to a LPF (e.g. change of particulars, inspection of the LPF register) will be set out in the law. The fees will basically be charged on a cost-recovery basis.

## **Contractual freedom among partners**

21. To cater for the operational needs of a PE fund, we propose that the partners of a LPF will have freedom of contract in respect of the key operation of the LPF. The aspects to be freely determined by a contract (i.e. limited partnership agreement) may include the following –
- (a) admission and withdrawal of limited partner(s), as well as transfer of partnership interests by limited partner(s);
  - (b) organisation, management structure, governance and decision-making procedures of the LPF;
  - (c) investment scope and strategy of the LPF;
  - (d) powers, rights and obligations of the partners (subject to other applicable statutory obligations of general partner under the LPF Regime);
  - (e) scope of general partner’s fiduciary duties, and remedies for breach or default; and
  - (f) financial arrangements among the partners, such as capital contribution, distribution of proceeds, clawback obligations of partners, etc.

## **Safe harbour activities for limited partner(s)**

22. We appreciate that clear-cut limited liability for limited partner(s) of a LPF lies at the core of its attractiveness to investors. With reference to overseas experience, we propose that a limited partner may conduct certain safe harbour activities without compromising its limited liability protection in respect of that LPF. For the avoidance of doubt, safe harbour activities do not constitute management of the LPF. Some examples of prescribed safe harbour activities may include –

- (a) acting, or authorising a person to act, as an agent, director, shareholder, member, contractor, officer or employee of the LPF or the general partner. Serving, or appointing a person to serve, on a board or committee of the LPF or the general partner, or revoking such appointment. Exercising any powers or authorities or performing any obligations in the capacity of the above positions;



- (b) entering into, or acting under, a contract with the general partner or any limited partner(s) of the LPF, provided that the contract does not require, or the action under the contract does not involve, a limited partner taking part in the day-to-day management of the LPF business;
- (c) serving, or appointing a person to serve, on the board of directors, or a committee of any corporation in which the LPF has an interest, or any corporation providing management, consultation, custody or other services to the LPF or having a business relationship with the LPF, or revoking such appointment;
- (d) discussing, advising, approving or authorising the general partner, any limited partner(s) or the investment manager on the business, prospects or affairs or transactions of the LPF;
- (e) calling, requesting, attending or participating in a meeting of the partners;
- (f) exercising any right or power conferred under the limited partnership agreement, other than any power to carry out management functions, but including the right to vote on or signify the approval or disapproval to any proposed transaction of the LPF;
- (g) consulting, investigating, reviewing, approving or advising on the accounts, the valuation or the assets of the LPF or affairs of the LPF;
- (h) acting as a guarantor for the LPF or the general partner;
- (i) approving or disapproving any amendment to the limited partnership agreement or taking part in a decision about the variation of, or waiver of a term of, the limited partnership agreement or associated documents;
- (j) commencing or instructing someone to commence, continue or defend legal proceedings on behalf of the LPF where the general partner has refused to do so without good reason; and
- (k) taking part in a decision about:
  - (i) whether a person should become or cease to be a general or limited partner;

- (ii) whether the LPF should end or the term of the LPF should be extended;
- (iii) changes in the persons responsible for the day-to-day management of the LPF;
- (iv) the incurrence or renewal of indebtedness by the LPF;
- (v) a change in the investment scope of the LPF;
- (vi) entering into contract with other parties in relation to the business of the LPF;
- (vii) enforcing an entitlement under the limited partnership agreement, provided that the entitlement does not involve a limited partner taking part in the day-to-day management of the partnership business;
- (viii) the exercise of the LPF's rights in respect of an investment;
- (ix) the participation by a limited partner in a particular investment by the LPF; and
- (x) the creation, extension, variation or discharge of any other obligation owed by the LPF.

### **Winding-up of a LPF**

23. PE funds often have a limited term (normally around eight to 10 years). It would facilitate PE funds' operation by introducing a straightforward and cost efficient dissolution and/or liquidation mechanism for LPFs, without compromising the interest of investors. We will further consider the relevant legal issues involved in the dissolution in accordance with the limited partnership agreement and/or liquidation of a LPF.

## **Anti-money laundering / counter-terrorist financing (“AML/CFT”) requirements**

24. To fulfil the AML/CFT standards of the Financial Action Task Force, the investment manager of a LPF must be either an authorized institution, a licensed corporation, an accounting professional or a legal professional as defined in Schedule 1 to the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) (“AMLO”). The investment manager will be required to conduct preventive AML/CFT measures as stipulated under the AMLO, including for example, conducting customer due diligence in respect of all investors (including all general and limited partners as well as their beneficial owners) of the LPF, and keeping records for at least five year (see paragraph 25 (c) and (d) below).

### **Maintenance of records by a LPF**

25. A LPF will be required to maintain proper record of documents/information in relation to its operation and transactions. We propose that the general partner/investment manager of a LPF shall be responsible to ensure that the following records are kept at the registered office of the LPF or any other place in Hong Kong made known to the RoC –

- (a) accounting records of the LPF, including the financial account of the LPF audited by a practice unit (see paragraph 12(c) above), for at least seven years;
- (b) a register of partners containing the particulars of each general partner and limited partner (including their identities and total amount of capital contribution);
- (c) records and documents obtained in the course of customer due diligence and files relating to every customer’s account and business correspondence with the customer and any beneficial owner of the customer for at least five years (see s.20(1)(b) of Schedule 2 to the AMLO);
- (d) documents and record of each transaction carried out by the LPF for at least five years (see s.20(1)(a) of Schedule 2 to the AMLO); and

- (e) information, including beneficial ownership, of all partners of the LPF for Exchange of Information purposes as per the requirements of the Organisation for Economic Co-operation and Development<sup>9</sup>.
26. The above records (except items (c), (d) or (e)) shall be made available to all the general partner and limited partner(s) of the LPF. All the above records would not be open for public inspection. They, however, shall be accessible by the law enforcement officer as defined under section 653B of the Companies Ordinance (Cap. 622), the AMLO and the IRO for law enforcement purposes as and when necessary.

### **Proposed enforcement powers**

27. The RoC would require sufficient powers to properly oversee the LPFs' compliance with the registration requirements as proposed above. We intend to provide the RoC with the following major enforcement powers to perform its duties –
- (a) the power to refuse, suspend or revoke a registration of LPF under conditions such as when –
    - (i) the LPF does not fulfill the registration requirements;
    - (ii) the general partner makes a false or misleading statement in any of the returns to the RoC;
    - (iii) the LPF is not in operation as a fund for at least a continuous period of 12 months anytime commencing from the first anniversary of registration;
    - (iv) the LPF does not fulfil the requirement to file an annual return within the prescribed time; or

---

<sup>9</sup> A LPF meeting the definition of a reporting financial institution has obligations under the IRO to conduct due diligence procedures to identify reportable accounts held by tax residents of reportable jurisdictions, and also collect and submit the required information in respect of these reportable accounts to the Inland Revenue Department for automatic exchange of financial account information. In the Peer Review Report on Exchange of Information on Request (Second Round), published in March 2019, Hong Kong is recommended to ensure that accurate beneficial ownership information of all partnerships carrying on business in Hong Kong is available at all times and retained for at least five years.

- (v) the LPF is not formed for a lawful purpose.
  
- (b) the power to access any records or information relating to the operation and business activities/transactions of a LPF, including but not limited to the records mentioned in paragraph 25 above; and
  
- (c) the power to give directions regarding the RoC's functions in relation to the registration requirements, e.g. direction to change the name of a LPF in case of a "same name" situation, direction regarding the withholding of registration of documents.

### **Power of the Chief Executive in Council ("CE in C") and the Court**

- 28. We propose that CE in C (or other authorities<sup>10</sup> as may be appropriate) will be given powers to make rules to set out the details of the LPF regime. Such details include those relating to the conduct of registration, duties or additional duties to be performed by the RoC or other relevant agencies, forms used, and fees charged under the LPF regime.
  
- 29. Meanwhile, subject to our consultation with the Judiciary, we may give power to the Court for rectification of, for example, omission or misstatement of any documents/information submitted under the LPF regime, as well as for granting relief in certain proceedings.

### **Offences and penalties**

- 30. Modelling on the offences and penalties applicable to conventional companies, we propose to make it an offence under the LPF regime for certain actions taken or not taken by a LPF. They may include the making of false statement; destruction of registers, books or documents; failure to maintain registers and records; failure to have a registered office; failure to make required disclosures; failure to notify the RoC of changes in particulars of registration; and failure to comply with a direction given by the RoC. When proposing the

---

<sup>10</sup> Such as the Financial Secretary, the Secretary for Financial Services and the Treasury, or the RoC.

penalty levels for the offences, we will draw reference to those applicable to conventional companies.

## **TAX AND STAMP DUTY TREATMENT**

31. Like other funds operating in Hong Kong, a LPF meeting the definition of “fund” under section 20AM of the IRO and subject to certain exemption conditions set out in the IRO can enjoy profits tax exemption on transactions in qualifying assets in Schedule 16C to the IRO and incidental transactions for any year of assessment commencing on or after 1 April 2019. Since the limited partners are not expected to manage the LPF though allowed to perform safe harbour activities, the general partner of a LPF has to comply with all requirements and bear all obligations under the provisions of the IRO (e.g. record keeping requirement, filing of profits tax returns and employer’s returns within time limits, and payment of tax due on time).
  
32. We intend to keep the same stamp duty arrangements applicable to a limited partnership to a LPF. An interest in a LPF is not a share, stock, debenture, loan stock, fund, bond or note issued by the LPF, nor is it a unit under a unit trust scheme. It does not fall within the definition of “stock” under section 2 of the Stamp Duty Ordinance (Cap. 117). Accordingly, an instrument under which an interest in a LPF is contributed/transferred/withdrawn is not chargeable with stamp duty. Meanwhile, a LPF may accept capital contributions in cash or in kind as provided in its limited partnership agreement. In-kind capital contributions in relation to the transfer of dutiable assets (e.g. Hong Kong stock or immovable property) would be subject to stamp duty. The distribution of profits and assets of LPF to the limited partner(s) will also be permitted in accordance with the terms of the limited partnership agreement. Transfer of dutiable assets by a LPF to a limited partner would be subject to stamp duty.

## **VIEWS SOUGHT AND WAY FORWARD**

33. Please send us your views, if any, on the proposals as set out in paragraphs 8 to 30 above by 30 August 2019 by mail, email or fax to

Address	:	Financial Services Branch, Financial Services and the Treasury Bureau, 24/F, West Wing, Central Government Offices, 2 Tim Mei Avenue, Tamar, Hong Kong
Fax	:	2294 0460
Email	:	<a href="mailto:fundconsultation@fstb.gov.hk">fundconsultation@fstb.gov.hk</a>

34. Please mark on the envelope/fax/subject line of an email “Proposals to establish a Limited Partnership Regime for Funds”.

35. Please indicate if you do not want your views to be published or if you wish to remain anonymous when your views are published. Unless otherwise specified, all responses will be treated as public information and may be published in the future.

36. The Government will consider views received in the compilation of a bill on the LPF regime for consideration by the Legislative Council.

**Financial Services Branch  
Financial Services and the Treasury Bureau  
31 July 2019**