

Oversight

Wealth Management Connect

October 2021

Introduction

On 10 September 2021, the Hong Kong Monetary Authority (HKMA) issued a [circular](#) entitled *Implementation Arrangements for the Cross-boundary Wealth Management Connect Pilot Scheme in the Guangdong-Hong Kong-Macao Greater Bay Area* (Circular), which set out for registered institutions in Hong Kong the implementation arrangements and specific regulatory requirements of the pilot cross-boundary wealth management connect (WMC) between the nine Mainland cities in the Greater Bay Area (GBA) and Hong Kong. Specific guidance in respect of the Southbound and Northbound Schemes is provided in [Annex 1](#) and [Annex 2](#) respectively, as well as the Frequently Asked Questions (FAQs) at the [Appendix](#).

The HKMA, the People's Bank of China (PBOC) and the Monetary Authority of Macao first announced the decision to implement WMC in the GBA on 29 June 2020, with the objective deepening and widening mutual access between the financial markets of the Mainland and Hong Kong. Under the WMC, eligible residents in the Mainland cities in the GBA and Hong Kong will be able to invest in wealth management products distributed by banks in each other's market through a "closed-loop funds flow" system. It is anticipated that WMC will come into operation across the GBA in October 2021.

This *Oversight* gives an overview of the Hong Kong implementation details in respect of the Southbound and Northbound Schemes and examines the implications WMC for Hong Kong's financial industry, in particular, the significant opportunities it affords to Hong Kong based retail fund managers as well as international managers who are able to structure retail fund products out of Hong Kong.

Wealth Management Connect

The WMC consists of a Southbound Scheme and a Northbound Scheme: The Southbound Scheme refers to southbound investment, i.e. investment by eligible residents of Mainland cities in the GBA investing in wealth management products distributed by eligible banks from Hong Kong, whereas the Northbound Scheme refers to northbound investment, i.e. investment by eligible residents in Hong Kong investing in wealth management products distributed by eligible banks from the Mainland. Eligible banks under the Circular refer to registered institutions, i.e. banks under the Banking Ordinance regulated by the HKMA which are registered by the Securities and Futures Commission (SFC) under the Securities and Futures Ordinance (SFO) to carry out Type 1 (dealing in securities) regulated activity, engaging in retail banking or private banking business (Hong Kong banks).

To embark on Southbound or Northbound Scheme activities, the Circular stipulates that a Hong Kong bank should partner with an eligible Mainland bank (Mainland partner bank) by entering into a cooperation agreement to undertake cross-boundary funds remittance and transfer and the sale of wealth management products services (as applicable). A Hong Kong bank may at the same time partner with more than one Mainland partner bank to carry out WMC activities.

Hong Kong banks do not need to obtain approval from the HKMA before carrying out WMC activities but are required to notify the HKMA and submit a self-assessment at least one month in advance. After receiving a “no-objection” notification from the HKMA and after ensuring that Mainland partner banks also received similar confirmation from relevant Mainland regulatory authorities, Hong Kong banks may then embark on WMC activities.

The Southbound Scheme

The following sets out the arrangements and regulatory requirements provided for in the Circular that Hong Kong banks are expected to comply with when participating in the Southbound Scheme (under which Mainland investors invest in eligible wealth management products offered by Hong Kong banks via designated channels).

Eligible investors

Investors must be residents of the nine Mainland cities in the GBA who meet the requirements set out by the Mainland regulatory authorities. They will only be able to invest in their personal capacity, but not as joint-name or corporate customers, and may not authorise a third party to operate the account nor be assessed as a “vulnerable customer”, i.e. customer who has limited ability to understand associated risks of the investment and withstand potential investment losses. If, however, an existing customer becomes a vulnerable customer due to a change in personal circumstances, the Hong Kong bank can continue to provide WMC services to the customer whilst providing enhanced investor protection measures to that customer.

Account opening arrangements

Regardless of whether an investor already has an account with the Hong Kong bank, a separate investment account and a related settlement account will need to be opened with a Hong Kong bank as the dedicated investment account, and a remittance account should either be newly opened or designated from an existing account maintained with the same Mainland partner bank as the dedicated remittance account for Southbound Scheme investments. This is to enable effective monitoring of funds remittances and transfers conducted through dedicated accounts and implementation of the close-looped funds flow management.

In opening the dedicated investment account for Mainland investors, Hong Kong banks must conduct customer due diligence, vulnerable customer assessment and risk profiling assessment. Taking into account the barriers to travel caused by the Covid-19 pandemic, Mainland investors can open such a dedicated investment account either remotely by attestation, i.e. the verification of client identity, sighting of identification documents and signing of client agreement to be certified by the Mainland partner bank, or in person with the relevant Hong Kong bank in the normal way.

Whilst a Hong Kong bank can partner with more than one Mainland partner bank, each eligible investor can only have one dedicated investment account with the Hong Kong bank and one dedicated remittance account with the Mainland partner bank at all times. The dedicated investment account will only be able to be used for investment purposes under the Southbound Scheme and should not be used for the provision of any other services of the Hong Kong bank.

Cross-boundary remittance

The WMC operates a closed-loop funds flow channel established between the banking systems of the two jurisdictions. This means that a dedicated investment account must always be paired with a dedicated remittance account for the purpose of transferring or receiving funds. Under this closed-loop, funds in the investment accounts can only be used for the purchase of eligible wealth management products and they must be remitted to the investor’s dedicated remittance account only. Investors are not allowed to withdraw cash from their investment accounts and the funds cannot be used for security or guarantee purposes.

In addition, cross-boundary remittance must be conducted in Renminbi (RMB). Save for exotic foreign currency deposits (exotic foreign currency means currency other than RMB, Hong Kong dollars, United States dollars, Euros, British Pounds Sterling, Australian dollars, New Zealand dollars, Canadian dollars, Swiss Francs, Japanese Yen and Singapore dollars), there is no restriction on the settlement currencies of the wealth management products being invested and Hong Kong banks can provide foreign exchange services to enable investors to invest in eligible products denominated in foreign currencies. Nevertheless, funds must be converted back into RMB when investors exit their investments and be remitted back to their remittance accounts through the Cross-border Interbank Payment System.

Aggregate and individual quota

The aggregate quota for the Southbound Scheme is initially set at RMB150 billion which is calculated on a net basis by reference to remittances from the Mainland to Hong Kong and Macao minus cumulative remittances from Hong Kong and Macao back to the Mainland. Hong Kong banks and the Mainland partner banks will need to check the usage of the aggregate quota, which is to be updated each trading day on the websites of the PBoC Guangzhou Branch and PBoC Shenzhen Central Sub-branch.

Individual investments are subject to an individual investor quota of RMB1 million, which is also calculated on a net basis. For example, if an investor remits RMB800,000 from the Mainland to Hong Kong to purchase investment products and later sells some of the products for RMB200,000 and remits that money back, then he or she will have used RMB600,000 of the quota. Once the RMB1 million quota is reached, the investment account is suspended and the individual cannot invest more.

Eligible wealth management products

Wealth management products which are eligible include the following:

- investment products (excluding products listed and traded on The Stock Exchange of Hong Kong (SEHK), the Hong Kong Futures Exchange Limited and the London Metal Exchange);
- products that are assessed as “low” risk to “medium” risk and “non-complex” by the Hong Kong banks distributing such products. This will include (i) funds domiciled in Hong Kong which are authorised by the SFC for retail distribution in Hong Kong and (ii) bonds. Complex products or derivative funds, regardless of whether they are SFC authorised or not, will not be eligible;
- deposits in RMB, the Hong Kong dollars and foreign currencies; and
- approved pooled investment funds (being SFC authorised funds approved by the Mandatory Provident Fund Schemes Authority) and unlisted units/class of exchange traded funds which are domiciled in Hong Kong, authorised by the SFC and listed on the SEHK and are assessed as “low” risk to “medium” risk and “non-complex” by the Hong Kong banks distributing such products.

Hong Kong banks must conduct pre-sale and ongoing product due diligence to ensure the risks and complexity of investment products distributed remain within the eligible scope.

In determining the risk rating of the products, Hong Kong banks should consider factors such as the nature and risks of the investment product, market and industry risks, economic and political environment, regulatory restrictions and any other factors which impose direct/indirect impact on the risk return and growth prospect of the relevant investment.

Therefore an equity fund does not automatically be classified as a product with higher than “medium” risk. The categorisation really depends on the market or industry the equity fund invests in, the volatility of investment returns and other relevant factors. However, if an equity fund focuses its investment on market or industry with high volatility, it might be considered as high risks and therefore is not eligible wealth management product.

Promotion and sale

With regard to cross-border marketing to the Mainland public without a dedicated investment account and/or a dedicated remittance account, cross-border marketing activities are limited to providing general information about the WMC, the factual representation that the bank provides Southbound Scheme services and displaying only a broad generic description of the scope and categories of wealth management products being offered. Hong Kong banks are not permitted to proactively market their Southbound Scheme services to the Mainland public.

Transactions in wealth management products under the Southbound Scheme conducted by Hong Kong banks may only be carried out on an “execution-only” basis. This means that an investor will initiate and directly issue investment instructions, and the Hong Kong bank will execute such instructions and respond to the investor’s enquiries upon request. Any contents of promotional materials provided to investors should not involve any form of solicitation or recommendation, should not constitute an offer to the Mainland public in relation to investment in individual products and should not constitute active marketing of the Hong Kong bank’s cross-boundary WMC services to the Mainland public.

The Northbound Scheme

Sets out below are the arrangements and regulatory requirements provided for in the Circular that Hong Kong banks are expected to comply with when participating in the Northbound Scheme, whereby eligible Hong Kong investors invest in eligible wealth management products offered by eligible banks in the Mainland via designated channels.

Eligible investors

All Hong Kong residents who hold a Hong Kong identity card, including permanent and non-permanent residents, who are assessed by Hong Kong banks as not being a vulnerable customer can participate in the Northbound Scheme. Similar to requirements under the Southbound Scheme, eligible investors will only be able to invest in their personal capacity, and not as joint-name or corporate customers and may not authorise a third party to operate the account.

Account opening arrangements

Regardless of whether an investor already has an account with the Hong Kong bank, he or she should open a dedicated remittance account in one of the Hong Kong banks, and an investment account should either be newly opened or designated from an existing account maintained with the same Mainland partner bank as the dedicated investment account to form a closed-looped funds flow. Unlike the Southbound Scheme in which Mainland investors have the option to open a remittance account with a Hong Kong bank by attestation, Hong Kong investors can only open a RMB remittance account in person with the Mainland partner bank following prevailing rules and regulations at the time of the launch. The HKMA has indicated that it is “exploring” with Mainland regulatory authorities arrangements for account opening by attestation under the Northbound Scheme similar to the Southbound Scheme.

Cross-boundary remittance

As with the Southbound Scheme, cross-boundary remittance is subject to closed-loop management and is conducted in RMB only. Nevertheless, RMB remittance to the Mainland under the Northbound Scheme is not subject to the daily maximum remittance limit of RMB80,000 per person for individual Hong Kong and Macao residents' inward remittance to bank accounts under the same name in the Mainland.

Aggregate and individual quota

Like the Southbound Scheme, the aggregate quota is initially set at RMB150 billion which is calculated on a net basis by reference to cumulative remittances from Hong Kong and Macao to the Mainland minimum cumulative remittances from the Mainland back to Hong Kong and Macao. Each investor is also subject to an individual investor quota which is set at RMB1 million calculated on a net basis, similar to the Southbound Scheme.

Eligible wealth management products

Eligible wealth management products mainly include products distributed by Mainland banks that are of “low” risk to “medium” risk and are relatively simple. They include public fixed income wealth management products issued by Mainland wealth management firms and being assessed by the issuers as products with risk rating of “R1” to “R3” (excluding wealth management products for the purpose of cash management) and public securities investment funds (excluding listed funds) being assessed by Mainland public fund managers and Mainland banks as products with risk rating of “R1” to “R3”.

By way of background, product risk ratings in the Mainland range from R1 to R5 with R1 being of the lowest risk.

Promotion and sale

Hong Kong banks may through media, communication channels and briefings organised in Hong Kong, introduce the fact that the bank provides WMC services in a fair and factual manner to the Hong Kong general public. As with the Southbound Scheme, the “execution-only” model is adopted and no promotional materials should be seen as any form of solicitation or recommendation, constituted as an offer to the Hong Kong public in relation to investment in individual products or amount to active marketing of the Mainland partner bank's WMC services to the Hong Kong public. Given that the eligible wealth management products under the Northbound Scheme are not authorised by the SFC for offer to the public in Hong Kong, Hong Kong banks should be mindful of the selling restrictions under the SFO and the Companies (Winding Up and Miscellaneous Provisions) Ordinance. Separately, Mainland banks are not permitted to proactively market their Northbound Scheme services to the Hong Kong public (unless the required licences/registrations have been obtained).

Regulatory supervisions

The Southbound and Northbound Schemes offer the first mutual market access mechanism that facilitates cross-border investments for individual investors. As a novel mechanism, sufficient controls and supervision will need to be in place to ensure statutory and regulatory compliance by Hong Kong banks. The HKMA is to be responsible for such supervision, and it will conduct on-site examinations as well as off-site surveillance of Hong Kong banks' Southbound Scheme and Northbound Scheme business. Where there is non-compliance or breaches, the HKMA and the PBoC will consider suspension of the relevant bank's eligibility to engage in WMC activities. They may also take supervisory and/or enforcement actions against the relevant Hong Kong banks and/or their relevant personnel in respect of the non-compliance or breaches. It is important to note that the Circular does not revise the SFO.

In terms of investor protection, the relevant Mainland and Hong Kong regulatory authorities will supervise the banks' activities according to the laws, regulations and regulatory regimes of the jurisdiction in which the transactions take place. In Hong Kong, the relevant statute, the SFO, as well as other ordinances will apply. Hong Kong banks will handle complaints involving cross-boundary funds remittances under the Northbound Scheme and those relating to the sale of wealth management products under the Southbound Scheme in accordance with the HKMA's SPM module IC-4 "Complaint Handling Procedure. Other cross-boundary complaints will be referred to the Mainland partner bank for follow-up with the assistance of the Hong Kong bank.

Conclusion

The launch of the WMC will further deepen the financial connectivity between Mainland China and Hong Kong and expand cross-boundary investment channel and asset allocation choices for residents in the GBA. For managers of the Hong Kong domiciled funds authorised by the SFC, this in particular presents significant business opportunities as it opens up a potential retail investor base of close to 70 million people in the GBA. Although the current scope of eligible wealth management products under the Northbound Scheme and Southbound Scheme is relatively limited at this initial stage, it is expected that the category of eligible products will expand and the investment quotas will increase as WMC matures. It is anticipated that more international financial institutions will consider using Hong Kong to capitalise on the opportunities offered by WMC to access the GBA market.

Whilst earlier Stock Connect and Bond Connect are primarily driven by professional institutional investors, WMC is the first mutual market access mechanism that allows individual investors to participate directly in both Northbound and Southbound investments. WMC is a huge milestone for the financial industry in Hong Kong as it should facilitate cross-boundary investment, diversify investment portfolios and is a step towards further liberalising Mainland China's financial markets. Under WMC, Hong Kong banks and the fund management industry in particular, can hopefully monetise the investment potential of the Mainland.

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