The growth of the private wealth management industry in Singapore and Hong Kong

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Key points

- This article describes, from a legal and regulatory perspective, how Singapore and Hong Kong have developed themselves into leading centres for private wealth management in recent years.
- Asia's remarkable economic growth, led by China and India, and the recent financial crisis have provided a window of opportunity for Singapore and Hong Kong to capitalize on.
- The continuing growth of Singapore and Hong Kong's private wealth management industry has also been made possible by their respective government's approach in creating a facilitative legal and regulatory environment.

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1. Introduction

Much has been said in various quarters about how Switzerland may be losing its position as the traditionally dominant private banking and private wealth management hub of the world. In contrast, industry opinion suggests that private wealth management is experiencing a shift towards Asia, particularly in financial centres like Singapore and Hong Kong, where the rapid growth of the private banking industry and the rise of money managers looking to capitalize on a share of the swelling ranks of millionaires has been nothing short of impressive. This article seeks to explore some of the reasons for this phenomenon, and considers the extent to which legal and regulatory considerations may have played a part in this growth.

2. Switzerland: the tradition of private wealth management

Wealth management can be generally defined as a financial service provided by private banks and asset managers to private, corporate or institutional clients with a certain threshold of wealth, with varying degrees of customization and complexity involved depending on the volume of those assets.[1] This article will confine itself to the private wealth management industry, where the clients are private individuals with a large economic or financial net worth.

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1 The Swiss Bankers Association, *The Swiss Banking Sector Compendium 2010* (Basel 2010) 41.

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For over a hundred years, Switzerland has been the centre for wealth management and a safe haven for high-net-worth individuals (HNWIs) to park their money. This has been due in no small part to its strict laws on bank secrecy. Central to this concept is Article 47 of the Swiss Federal Banking Act of 8 November 1934, which considers a bank's (and its employees') duty of confidence as a professional duty which arises as a matter of course in the banker–client relationship, and for which violation thereof must be punished by criminal law either through imprisonment or a fine. Violation of this secrecy remains punishable even when the banker–client relationship or employment has terminated or the holder of the confidential information no longer works in the banking industry.

This notion of bank secrecy is further underpinned and complemented by Article 13 of the Federal Constitution of the Swiss Confederation, which states that everyone has the right to privacy in their private and family life, and in relation to their mail and telecommunications, as well as the right to be protected against the misuse of personal data.[2]

Against such a backdrop emphasizing the protection of personal information, Switzerland has seen its private wealth management industry flourish. In 2007, the nation accounted for 9.1 per cent of global assets under management (AUM), giving it a market-leading share of 27 per cent in offshore private banking.[3] At the end of 2007, AUM in Switzerland stood at 5.4 trillion Swiss Francs, which is more than 10 times Switzerland's gross domestic product.[4]

However, due to the global financial crisis from 2008 to 2009, Switzerland and its banks suffered from global developments, which looked to have somewhat derailed the country's continued growth as a wealth management centre. As at October 2008, total AUM in Switzerland had dropped to around 4.1 trillion Swiss Francs.[5] An important consequence of the credit crunch has been an increase in pressure for governments globally to find means to increase their fiscal budgets, and cross-border assets started to come under the spotlight. As one of the world's biggest offshore banking centres, Switzerland naturally became a specific target and, through a series of events, came to face global pressure as an alleged tax haven.

3. Asia: a viable alternative

Against this backdrop of uncertainty affecting Switzerland, Asia seems to have become the new economic *Zeitgeist* and focal point for the global private wealth industry. There are a few reasons for this growth.

First, the economic development of the People's Republic of China and of India in recent years has been nothing short of remarkable, resulting in a tidal effect that has had

2 The Federal Constitution of the Swiss Confederation 1999, art 13.

3 The Swiss Bankers Association, *Wealth Management in Switzerland January 2009* (Basel 2009) 4.

4 Ibid at 8.

5 Ibid.

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an uplifting impact on Asia in general. This sentiment can be gleaned from the increase in investment opportunities in Asia, rising affluence within the Asian population and the desire of global investors to have a more balanced portfolio.[6] This trend is forecasted to continue strongly as Asia, led by the People's Republic of China and India, is likely to be the powerhouse of HNWI growth in coming years,[7] with its economic expansion and growth likely to keep outpacing more developed economies.

In addition, Asia was comparatively unscathed by the sub-prime crisis due to: (i) its healthier macroeconomic fundamentals compared with the prior decade; (ii) improved corporate balance sheets; (iii) reformed banking systems; (iv) strong external positions and (v) relatively modest property price appreciation compared with the USA and Europe.[8]

The relative stability of the Asian economy against the US and European economies during the recent financial crisis has provided Asia with a window of opportunity to capitalize on. Within the private wealth management industry, portfolio allocations shifted towards Asia, private wealth managers sought to forge new relationships in Asia and private banks strengthened their presence in Asia to manage private wealth in an effort to tap the rising population of HNWIs.[9]

For many years, Singapore and Hong Kong have positioned themselves as being two of the region's leading financial centres and are two prime candidates to illustrate Asia's burgeoning private wealth management industry. Given the recent developments, these two traditional rivals look to ride the 'Asian Wave' to grow their reputations as centres for private banks and wealth managers to establish operations, so as to take advantage of the huge inflows of capital that have been making their way into the region from around the world. This article shall proceed, from a largely legal and regulatory perspective, to first consider the Singapore growth story and examine the probable reasons for such development before going on to look at Hong Kong's wealth management industry and the factors that have likely enabled its rise in fortunes.

4. Singapore: the cosmopolitan hub

Singapore has a sterling reputation as an investor- and business-friendly jurisdiction, as seen from the various accolades Singapore has earned itself: world's easiest place to do business;[10] ranked number two worldwide as the city with the best investment

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6 Arif Sharif, 'Gulf Investors to shift focus to Asia, Latin America, Credit Suisse says' *Bloomberg* (27 June 2010) <http://www.bloomberg.com/news/2010-06-27/gulf-investors-to-shift-focus-to-asia-latin-america-credit-suisse-says.html> accessed 6 July 2010.

7 Capgemini and Merrill Lynch Wealth Management *World Wealth Report* 2010, 8 <http://www.capgemini.com/insights-and-resources/by-publication/world-wealth-report-2010/> accessed 31 August 2010 (restricted content available upon registration).

8 Khor, Hoe Ee and Kee, Rui Xiong, 'Asia: A Perspective on the Subprime Crisis' *Finance and Development* (June 2008) <http://mpra.ub.uni-muenchen.de/9995/1/MPRA_paper_9995.pdf> accessed 6 July 2010.

9 Nisha Gopalan, 'Banks Rush to Tap Asia's Wealth' *Wall Street Journal* (22 March 2010) <http://online.wsj.com/article/SB10001424052748704841304575137400083836726.html> accessed 6 July 2010.

10 World Bank, *Doing Business 2010* (World Bank Publications 2010) <http://www.doingbusiness.org/documents/fullreport/2010/DB10-full-report.pdf> accessed 31 August 2010.

potential for 16 consecutive years;[11] ranked first for having the most open economy for international trade and investment[12] and cited as having the best business environment in Asia Pacific and worldwide.[13]

Since the 1970s, when Singapore was still largely a manufacturing-intensive economy, Singapore has successfully transformed itself into a service economy and over the past decade has steadily been building up its infrastructure and capability in the wealth management sphere. As at the end of 2009, AUM figures for financial institutions[14] with asset-management activities in Singapore stood at a new high of S$1.2 trillion, a 40 per cent increase over the S$864 billion at the end of 2008[15] and surpassing the previous high watermark of S$1.173 trillion set at the end of 2007.[16] This represents a 19 per cent per annum growth rate on a rolling 5-year-average basis[17] and underscores the sustained growth and dynamism of the wealth management industry in Singapore.

A critical component of this growth has primarily come from the development of the private wealth management sector, with an increasing number of Swiss and international private banks and wealth managers setting up shop in Singapore. Amongst a host of others, top Swiss private banking outfits like the Julius Baer Group and Lombard Odier Darier Hentsch & Cie established operations in Singapore in 2006 and 2008, respectively, with the Singapore office of Julius Baer being the regional centre[18] for the Swiss private banking conglomerate, ramping up operations in the span of 4 years to employ ~360 employees as of May 2010.[19] Other international and Swiss full service banks have long established a private banking presence in the country, with the likes of Citibank, Morgan Stanley, UBS and Credit Suisse being leading industry players. Even local banks like OCBC are increasing their stake in the private banking business, with the October 2009 acquisition of ING's Asian private banking division to form the Bank of Singapore.[20]

As a follow-on to the heightened activity of private banks, there has been a sizeable increase in the incidence of trust[21] and family-wealth-succession planning structures. Popular amongst such structures is the use of a private trust company (PTC)—whereby a

11 *BERI Report 2010* (Business Environment Risk Intelligence, Washington State, USA April 2010).

12 Robert Z Lawrence, Margareta Drzeniek Hanouz and John Moavenzadeh, *The Global Enabling Trade Report 2010* (World Economic Forum 2010) <http://www.weforum.org/pdf/GETR10/Global-Enabling-Trade-Report-2010.pdf> accessed 31 August 2010.

13 Economist Intelligence Unit, 'Economist Intelligence Unit: Country Forecast' *The Economist* (December 2009).

14 Including banks, finance and treasury centres, capital markets services licensees, financial advisers, operational headquarters and exempt entities.

15 Monetary Authority of Singapore, *2009 Singapore Asset Management Industry Survey* (Singapore 2009) <http://www.mas.gov.sg/resource/eco_research/surveys/AssetMgmt09.pdf> accessed 13 July 2010.

16 Monetary Authority of Singapore, *2007 Singapore Asset Management Industry Survey* (Singapore 2007) <http://www.mas.gov.sg/resource/eco_research/surveys/AssetMgmt07.pdf> accessed 15 May 2010.

17 MAS (n 15).

18 Saeed Azhar, 'Julius Baer seeks expansion in Southeast Asia' *Reuters* (29 June 2007) <http://www.reuters.com/article/idUSSIN23513820070629> accessed 23 May 2010.

19 Maryam Omidi, 'Julius Baer adds 11 in Singapore' *Financial News* (14 May 2010) <http://www.efinancialnews.com/story/2010-05-14/julius-baer-hires-eleven-asia> accessed 6 June 2010.

20 'OCBC Bank Acquires ING Asia Private Bank' *Banking Business Review* (29 January 2010) <http://retailbanking.banking-business-review.com/news/ocbc_bank_acquires_ing_asia_private_bank_100129/> accessed 23 May 2010.

21 'Explanatory Brief: Trust Companies Bill 2005' (Press Release 25 January 2005) <http://www.mas.gov.sg/news_room/press_releases/2005/Explantory_Brief_Trust_Companies_Bill.html> accessed 23 May 2010.

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PTC acts as the trustee for family trusts—as the trust mechanism of choice to plan for the future ownership of family business interests. Its popularity is due to the fact that unlike a traditional trust arrangement whereby an external trust company is appointed as trustee to manage trust assets, a PTC structure allows the settlor to retain control in the management of underlying investments through direct ownership of shares in the PTC itself or by sitting on the board of directors of the PTC.[22] Furthermore, as will be discussed in greater detail below, Singapore has encouraged the development of such PTC arrangements through a favourable regulatory and taxation regime. In addition, private banks themselves favour the use of such PTC structures as those that have trust business functions would much rather that their trust companies not hold direct stakes as a trustee in any investments by a trust in the nature of operating businesses and listed companies, which would consequently attract a fair amount of fiduciary risk and responsibility.[23]

Reasons for growth

While the growth and development of Asia has no doubt contributed largely to the rise of the private wealth management industry in Singapore, Singapore's sound legal and regulatory framework coupled with a pro-business and tax-friendly environment for wealth managers, private banks and HNWIs have acted as a catalyst that allowed Singapore to take advantage of this window of opportunity. At the same time, Singapore is also cognizant of the need to maintain its status and reputation as a trusted and responsible business and financial hub committed to international efforts to combat cross-border tax evasion[24] through the adherence to international standards and rules regarding the exchange of information.

Regulatory regime governing wealth management

In Singapore, the wealth management industry is regulated by various laws and regulations depending on the type of arrangement contemplated. The Singapore government and its *de facto* central bank, the Monetary Authority of Singapore (MAS), takes a proactive approach in weaving a facilitative regulatory framework to accommodate and promote the growth of private wealth management in Singapore. Three areas worth mentioning are the regulatory regimes governing private banks, fund managers and private trusts, which are respectively governed by the Banking Act, Chapter 19 of Singapore (Banking Act), the Securities and Futures Act, Chapter 289 of Singapore (SFA) and the Trust Companies Act, Chapter 336 of Singapore (Trust Companies Act).

The MAS issues three types of banking licences: full bank licences, wholesale bank licences and offshore bank licences. A holder of a full bank licence can engage in the full range of 'banking business' as defined in the Banking Act,[25] while a holder of a wholesale

22 Ashley Crossley, 'Offshore Planning: Trends and Developments' (2006) 13 JTCP 123, 128.

23 Christian Stewart, 'Private Trust Company Structures: a Hong Kong Perspective' (June 2008) Offshore Investment Magazine 187.

24 Second Reading Speech by Minister for Finance, 'Income Tax (Amendment) (Exchange of Information) Bill 2009'.

25 Banking Act, Chapter 19 of Singapore s 2.

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bank licence or offshore bank licence can carry on 'banking business', but subject to certain restrictions on Singapore dollar business. In particular, an offshore bank licence holder cannot operate Singapore dollar-denominated savings accounts and fixed deposits for Singapore residents,[26] while a wholesale bank licence holder can operate Singapore dollar-denominated savings accounts, subject to MAS approval, and may accept fixed deposits, which shall not be less than S$250,000 at all times for Singapore dollar-denominated fixed deposits except on termination of the account or the withdrawal of all deposits standing to the credit of the depositor.[27]

There is also the alternative of applying to the MAS for approval as a merchant bank. A merchant bank can operate an Asian Currency Unit (ACU) if it obtains permission from the MAS to do so. An ACU is permitted to, *inter alia*, accept non-Singapore dollar-denominated time and demand deposits (including savings and checking accounts).[28] In effect, a merchant bank that has approval to operate an ACU can conduct non-Singapore dollar-denominated banking business.

Many private banks in Singapore are either licensed as wholesale banks, or have obtained approval from the MAS to operate as merchant banks, largely owing to the foreign nature and large amounts of funds contributed by the HNWIs investing with such banks, which enable these private banks to adhere to the restrictions and conditions attaching to them as wholesale banks or merchant banks.

'Fund management'[29] is a regulated activity in Singapore and, generally, financial institutions that engage in the business of fund management in Singapore would be required to apply for a Capital Markets Services Licence (CMSL), or rely on an exemption from such licensing. One such exemption relates to licensed banks whereby a bank which holds any one of the banking licences mentioned above, or is approved as a merchant bank, is authorized to carry out the regulated activity of fund management without needing to hold or apply for a CMSL for fund management.

Fund-management houses that do not conduct banking business would need to apply for a CMSL or rely on an exemption from such licensing too. An exemption is available where the fund manager provides its services to no more than 30 'qualified investors',[30] which includes, *inter alia*, certain categories of 'accredited investors', as well as funds

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26 Monetary Authority of Singapore, *Guidelines for Operation of Offshore Banks* (Singapore 31 July 2008) <http://www.mas.gov.sg/resource/legislation_guidelines/banks/guidelines/Offshore%20Banks%20Guidelines%20-%208%20Jul%2008.pdf> accessed 8 July 2010.

27 Monetary Authority of Singapore, *Guidelines for Operation of Wholesale Banks* (Singapore 31 July 2008) <http://www.mas.gov.sg/resource/legislation_guidelines/banks/guidelines/Wholesale%20Banks%20Guidelines.pdf> accessed 8 July 2010.

28 Monetary Authority of Singapore, *Asian Currency Units Terms and Conditions of Operation* (Singapore 31 July 2008) <http://www.mas.gov.sg/resource/legislation_guidelines/banks/guidelines/ACU%20Terms%20and%20Conditions.pdf> accessed 8 July 2010.

29 Fund management means undertaking on behalf of a customer (whether on a discretionary authority granted by the customer or otherwise): (i) the management of a portfolio of securities or futures contracts; or (ii) foreign exchange trading or leveraged foreign exchange trading for the purpose of managing the customer's funds, but does not include real estate investment trust management.

30 As defined in the Securities and Futures (Licensing and Conduct of Business) Regulations.

offered solely to 'accredited investors' or investors of an equivalent class in a foreign jurisdiction (the '30 QI Exemption'). 'Accredited Investors' are defined to include, *inter alia*, individuals with net personal assets exceeding S$2 million or whose income in the preceding 12 months is not less than S$300,000.

Singapore's well-structured and comprehensive regulatory framework provides fund managers and private banks who confine their clientele to only sophisticated HNWIs, and in the case of the 30 QI Exemption to a limited number of such sophisticated investors, the ability to choose a licensing or regulatory regime more appropriate to their needs, instead of having to apply for the full bank licence or CMSL. This favourable environment in turn has attracted growth and encouraged development of the wealth management industry.

However, in keeping with the regulatory reforms currently taking place in Europe and North America with regard to the fund-management industry, the MAS has in April 2010 issued a consultation paper seeking views from the public on proposed changes to the regulatory regime for fund management companies (FMCs). The consultation paper proposes that the current fund-management-licensing framework be streamlined and a new, tiered licensing and regulatory framework be introduced, the first category of which requires FMCs with AUM of not more than S$250 million, and who serve not more than 30 'qualified investors' (of which not more than 15 are funds), to notify the MAS in the prescribed manner. The second category requires FMCs who serve only 'accredited investors' and/or 'institutional investors' (as defined in the SFA) to apply for a CMSL in fund management. The third category requires FMCs who serve retail investors to apply for a full CMSL in fund management. On 28 September 2010, the MAS issued its response to public feedback which it received on the consultation paper and stated that it will consult the industry on draft legislative amendments in the coming months to implement the proposals outlined in the consultation paper possibly in 2011. While the proposals represent an overall tightening of the regulatory requirements, many industry watchers laude the fact that the MAS does attempt to take a pragmatic approach and keeps an active dialogue with the various industry players. This is ultimately in line with the MAS objective of developing the wealth management industry, and also illustrates a desire to strike a balance so that any regulatory enhancements do not unduly deter the growth pattern that Singapore has witnessed thus far.

In terms of the regulatory requirements for private trust structures, while the carrying on of 'trust business'[31] by a company will require such company to hold a

31 Trust business comprises of the following:

(i) the provision of services with respect to the creation of an express trust;
(ii) acting as trustee in relation to an express trust;
(iii) arranging for any person to act as trustee in respect of an express trust; and
(iv) the provision of trust administration services in relation to an express trust.

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trust business licence,[32] there is an exemption for any PTC, so long as the PTC engages a licensed trust company to carry out trust-administration services for the purposes of conducting the necessary checks to comply with anti-money laundering and countering the financing of terrorism (AML/CFT) notices, guidelines and directions issued by the MAS.[33] A PTC is defined as a corporation, the purpose of which is solely to provide trust business services in respect of a specific trust or of specific trusts, where each settlor of such trust is a connected person[34] in relation to any other settlor of any other trust to which the corporation provides trust business services, and each beneficiary of such a trust is a connected person in relation to the settlor of that trust or a charity,[35] and that does not solicit trust business from, or provide trust business services to, the public. Even as compliance with the conditions to rely on the tax exemption schemes and PTC-licensing exemption are arguably not too difficult and serve as an incentive to grow the sector, the fact that the administrative functions are to be outsourced to a licensed trust company should add credibility and engender regulatory oversight of the industry.

Being sophisticated investors, HNWIs looking to set up private family-trust structures will usually want a say in the management and supervision of their assets and be reluctant to hand over trusteeship wholesale to an external trust company, regardless of whether it is licensed or not. As such, HNWIs setting up a private family trust may wish to be involved in the trusteeship through direct ownership of shares in the PTC itself or by sitting on the board of directors of the PTC. Accordingly, the abovementioned exemption spares such settlors from the process of having to apply for and obtain a trust business licence for the PTC, and at the same time allows them to benefit from the provision of trust administrative services by professional licensed trust companies; moreover, such settlors can still maintain for themselves a degree of ownership and control by being on the board of directors or shareholders of the PTC.

Tax incentives

Singapore has a competitive tax regime, with one of the lowest personal and corporate tax rates in Asia and no estate duty.[36] Singapore income tax is generally imposed on the income of any person accruing in or derived from Singapore or foreign-sourced income received in Singapore from outside Singapore. The income tax rate for Singapore resident individuals is tiered, subject to a maximum of 20 per cent. For non-resident individuals, except for employment income which is taxed at the higher rate of 15 per cent or resident

32 Trust Companies Act, Chapter 336 of Singapore, s 3.

33 Trust Companies (Exemption) Regulations reg 4.

34 'Connected person', in relation to an individual, includes, *inter alia,* that individual's spouse, the descendants of the individual and their spouses, parents, grandparents, siblings and in-laws.

35 A charity, in this context, is defined as 'any trust, foundation, company or other body established solely for a purpose recognised as charitable by the governing law of the trust in respect of which the private trust company provides trust business services'.

36 Singapore estate duty has been abolished with respect to deaths occurring on or after 15 February 2008.

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rates, all other income (including director's fees and consultation fees) will be taxed at 20 per cent. The prevailing Singapore corporate tax rate is 17 per cent.

Gains which are considered capital in nature (ie gains which are considered non-income in nature) are not taxable but Singapore income tax will be imposed on gains of a revenue nature. It should be appreciated that although there are no specific laws or regulations which deal with the characterisation of whether a gain is revenue or capital in nature, gains derived from investments made by a foreign investor investing in Singapore as part of its trade or business carried out in Singapore may be subject to tax. On the other hand, where investments are acquired other than as part of a trade or business carried on by the foreign investor in Singapore, any gains made from such investments are more likely to be viewed as capital in nature, and accordingly, not subject to Singapore tax. However, the question of whether a gain is income or capital in nature would remain a matter of fact depending on the foreign investors' personal circumstances.

There are also numerous tax incentives that are applicable to the private wealth management industry that would benefit various investment structures such as trusts and private investment funds.

In terms of taxation regarding private family-trust structures mentioned above which utilize PTC arrangements for generational wealth planning, there are a number of tax exemption schemes available in Singapore to complement the regulatory treatment of PTC structures. Under Section 13Q of the Income Tax Act, Chapter 134 of Singapore (Income Tax Act), there is an exemption from Singapore income tax on all 'relevant income'[37] of such 'locally administered trust' and a holding company established for the purposes of such trust; and the share of such relevant income to which any beneficiary of the trust is entitled is also tax-exempt.[38]

A trust will qualify as a 'locally administered trust' for the purposes of the Income Tax Act[39] and relevant regulations[40] if certain conditions are fulfilled, including, *inter alia*, where every settlor of the trust is an individual, every beneficiary of the trust is an individual or a charitable institution, trust or body of persons established for charitable purposes only, at least one of the beneficiaries of the trust is not a settlor of the trust, the trust is created in writing and the trust is 'administered by a trustee company'[41] in Singapore.

A trust is considered to be 'administered by a trustee company' if, (i) the trustee company provides services to the trust in its capacity as trustee of the trust, including providing services as manager or administrator of a holding company of that trust, or

37 'Relevant income' is defined to include, *inter alia*, interest from deposits of monies with an approved bank or a finance company licensed under the Finance Companies Act, Chapter 108 of Singapore, interest from debt securities, income from certain annuities, income from life insurance policies, distributions by authorised collective investment schemes constituted as unit trusts and offered to the public for subscription and distributions from real estate investment trusts.

38 Income Tax Act, s 13Q.

39 Ibid s 13Q(3).

40 Income Tax (Exemption of Income of Locally Administered Trust) Regulations 2007 (Income Tax Regulations) reg 2(1).

41 A 'trustee company' is defined as a company that is a licensed trust company within the meaning of the Trust Companies Act or that is exempted from holding a trust business licence within the meaning of the Trust Companies Act.

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(ii) the trustee company provides services to a trustee of the trust under a contract for services with that trustee, such services being the establishing of the trust or a holding company of the trust, and/or the administration or management of the trust or a holding company of the trust.[42]

There is also a corresponding tax exemption scheme available for foreign trusts under Section 13G of the Income Tax Act that is broadly similar to Section 13Q, whereby a 'foreign trust' is one where the beneficiaries are persons who are neither citizens nor residents of Singapore.

These two tax exemption schemes have been helpful to encourage the proliferation of family wealth-planning trust structures in Singapore. In addition, for families who prefer not to use a trust structure but family investment holding companies, the new Tax Exemption Scheme for Family-Owned Investment Holding Companies (FIHC) was introduced in 2008. Under the FIHC Tax Exemption Scheme, subject to certain prescribed conditions, tax exemptions previously only available to individuals are now extended to individuals investing through a qualifying FIHC, which is incorporated before 1 April 2013. Specifically, a qualifying FIHC is exempted from tax on certain income (i.e. similar to those exempted under Section 13Q of the Income Tax Act), to the extent that such income would have been exempted from tax if derived or received directly by an individual.

In order to promote Singapore as a hub for fund-management activities, there have been several incentives introduced for the fund management industry. Of particular note is the Enhanced-Tier Fund Tax Incentive Scheme (Enhanced-Tier Fund Scheme)[43] which was introduced in 2009.[44]

A fund which qualifies under the Enhanced-Tier Fund Scheme will be exempted from tax on a broad list of 'specified income' from 'designated investments' for the life of the fund, provided it meets certain prescribed conditions which include, *inter alia*, a minimum fund size of S$50 million; is managed by a Singapore fund manager; incurs at least S$200,000 local business spending annually and uses a Singapore-based administrator.[45]

At the fund-manager level, there is the Financial Sector Incentive (Fund Management) Award which allows a Singapore fund-management company, which is granted the award, to be taxed at a concessionary rate of 10 per cent, as opposed to the usual 17 per cent corporate tax rate, on income from providing fund management or investment advisory services to a fund that falls within one of the tax incentive schemes in Singapore (including the Enhanced-Tier Fund Scheme).

42 Income Tax Regulations (n 40) reg 2(2).

43 Families interested in the Enhanced-Tier Fund Scheme should seek advice as to whether their proposed fund structure would be able to benefit from the said Scheme, in view of the purpose and objective of their fund structure.

44 Income Tax Act, s 13X.

45 The condition of using a Singapore-based administrator is applicable to funds in the form of companies incorporated in Singapore.

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Banking secrecy and confidentiality

Like any other developed financial hub, Singapore has adopted a strict bank secrecy regime which is governed by the Banking Act. Under Section 47 of the Banking Act, a blanket prohibition exists against disclosure of 'customer information' by a bank[46] or any of its officers to any other person except as expressly provided in the Banking Act.

In addition to bank secrecy, there are also similar confidentiality provisions under the Trust Companies Act, which prohibits disclosure of information regarding a 'protected party' (which is defined as, in relation to a trust company, a trust for which the trust company provides trust business services and includes the settlor and beneficiary under the trust) by a licensed trust company or any of its officers, to any other person except as expressly provided in the Trust Companies Act[47].

By enacting secrecy and confidentiality provisions to the Banking Act and the Trust Companies Act, Singapore offers protection to the personal information of banking clients and settlors and beneficiaries of trusts. Nonetheless, recent developments with regards to the Organisation for Economic Co-operation and Development (OECD) has illustrated Singapore's willingness and desire to co-operate with other countries within the global financial community.

OECD: shift to greater compliance

Singapore's push in recent times towards a greater commitment to international standards relating to exchange of information has helped to further position itself as a reputable centre for financial dealings and enhance its standing as a legitimate economic hub, which in turn provides another level of assurance to private banking clients looking to find a jurisdiction to invest in.

The economic boom of 2006–2007 led to a marked increase in private banking activity and an increasing concern amongst the international community about Singapore possibly becoming a 'tax haven' or being viewed as such. Unlike Switzerland, who signed up as a 'third country', Singapore was not a signatory to the European Union (EU) Savings Directive, which attempts to reduce the proliferation of cross-border tax evasion through the exchange of information with EU member states about foreign-resident individuals receiving savings income outside their resident state, or the levying of a withholding tax as a substitute for exchanging information.[48] This potentially exacerbated the effect of driving capital from the EU to other offshore financial centres, including Singapore.[49] The fact that the EU in 2007 refused to enter into trade talks with the Association of South East Asian Nations (ASEAN) unless they were less opaque in

46 'Bank' means a bank incorporated in Singapore or the branches and offices located within Singapore of a bank incorporated outside Singapore.

47 Trust Companies Act (n 32) s 49.

48 Crossley (n 22) 123.

49 David Maude, *Global Private Banking and Wealth Management: The New Realities* (John Wiley & Sons Ltd, Hoboken NJ 2006) 249.

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their financial dealings[50] reflected the increasing global concerns about the growth of private wealth inflows accompanied by a lack of transparency within the South-East Asian economies generally and of countries like Singapore that was gaining popularity as an offshore financial centre.

This increasing concern within the international community, that Singapore could potentially become a tax haven and money-laundering jurisdiction,[51] culminated in Singapore being on the OECD's grey list for non-compliance with the internationally agreed standard developed in the OECD's Global Forum on Taxation and endorsed by G20 Finance Ministers and the UN Committee of Experts on International Co-operation in Tax Matters; the agreed standard requires exchange of information on request in all tax matters for the administration and enforcement of domestic tax law notwithstanding domestic tax laws and banking secrecy requirements.[52]

However, recognizing the importance of being removed from the grey list, Singapore took prompt action by renegotiating its tax treaties with at least 12 other countries to implement the international standard for exchange of information and successfully removed itself from the OECD grey list.[53] This swift turnaround had the beneficial effect of enhancing Singapore's credibility as an open and well-regulated economy, removes the concerns of the international community, while also negating the threat of international sanctions by the G20.[54] This in turn promotes confidence and encourages investments and inflows from private banking clients.

Even with Singapore's implementation of the international standard for exchange of information via the passing and bringing into force of the Income Tax (Amendment) (Exchange of Information) Act (Exchange of Information Act),[55] there are still appropriate safeguards in place to ensure that Singapore's bank secrecy and confidentiality provisions are not overly eroded and that banking and trust clients are still afforded adequate protection against disclosure of their private information.

Under the Exchange of Information Act, a foreign tax authority making the request for information must provide relevant details in relation to the request, including, *inter alia*, the purpose of the request, the identity of the person regarding whom information is requested, the nature and relevance of the information requested, the reasons for believing that the information requested is in the possession or control of a person in Singapore, a statement that the request is in conformity with the law and administrative practices of that foreign tax authority and a statement that the

50 'Singapore bank secrecy threatens EU trade talks' *Reuters* (2 October 2007) <http://www.reuters.com/article/idUSSIN14706320071002> accessed 27 May 2010.

51 Edward Taylor and Cris Prystay, 'Swiss Fight against Tax Cheats' (Article on Global Policy Forum website) <http://www.globalpolicy.org/component/content/article/172/30120.html> accessed 26 May 2010.

52 'Following G20 OECD delivers on tax pledge' (Press Release 2 April 2009) <http://www.oecd.org/document/57/0,3343,en_2649_34487_42496569_1_1_1_1,00.html> accessed 13 June 2010.

53 'Singapore signs its 12th tax agreement meeting the OECD standard' (Press Release 13 November 2009) <http://www.oecd.org/document/0/0,3343,en_2649_33767_44062080_1_1_1_37427,00.html> accessed 15 June 2010.

54 Richard Standing, 'All for the common good' *Business Times* (Singapore 13 January 2010) <http://www.businesstimes.com.sg/sub/supplement/story/0,4574,367706,00.html> accessed 5 June 2010.

55 Income Tax (Amendment)(Exchange of Information) Act 2009 s 105B.

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requesting country has pursued all means available in its own territory to obtain the information.[56]

Additionally, if the information requested is information that is protected from unauthorized disclosure under the Banking Act and the Trust Companies Act ('Protected Information'), then the Inland Revenue Authority of Singapore (IRAS) must, subject to certain exceptions, serve notice of the request on the person identified to be in possession or control of the Protected Information,[57] and must apply to the Singapore High Court for an order for the provision of the Protected Information.[58] The High Court has to be satisfied that the making of the order would be justified in the circumstances of the case and that provision of the Protected Information would not be contrary to the public interest.[59] If an order for the provision of the Protected Information is made by the High Court, either the person to whom the Protected Information relates or the person who is in possession or control of it may apply to the High Court to have the order discharged or varied within 7 days from the date the order is served on the person in possession or control of the Protected Information.[60]

The requirements to be met for an exchange of information request to be successful seek to ensure that foreign authorities are prevented from engaging in 'fishing expeditions'[61] where the information is requested for without a valid basis with the hope that the request would unearth some form of tax evasion information in the process; the requests for information will only be granted where there are specified, well-founded cases which are in-line with the OECD international standard.[62]

Singapore's actions towards greater international co-operation for the exchange of information with other countries should further enhance its status globally as a well-governed and transparent financial centre, while still affording a high degree of confidentiality to investors. This balance has to be well-struck and maintained to attract private wealth investment and HNWIs to Singapore.

A city to live, work and play

Singapore also recognizes the importance of human capital and understands that having a facilitative tax and regulatory environment is not all that is required. In addition to enhancing its reputation as one of the best places in Asia to live, work and play,[63] Singapore is also said to have amongst the least restrictive immigration laws in Asia for

56 Ibid Eight Schedule.

57 Ibid s 105E.

58 Ibid s 105J(1).

59 Ibid s 105J(2)–(3).

60 Ibid s 105J(4).

61 Edmund Leow and Simon Michaels, 'Has Banking Secrecy Come to an End in Singapore' *Business Times* (Singapore 8 June 2010).

62 'Singapore set to be removed from OECD's grey list' *Channel News Asia* (Singapore 11 November 2009) <http://www.channelnewsasia.com/stories/singaporebusinessnews/view/1017554/1/.html> accessed 12 May 2010.

63 Mercer, 'Quality of Living Worldwide City Rankings 2010 – Mercer Survey' <http://www.mercer.com/qualityoflivingpr> accessed 7 July 2010.

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foreign talent.[64] There are also schemes such as the Global Investor Programme and the Financial Investor Scheme whereby HNWI and entrepreneurs interested in investing or doing business in Singapore can be afforded residency status for themselves and their families.

In summary, Singapore's private banking and wealth management market has grown into a considerable hub in Asia in no small part due to its efforts to promote the sector through favourable and attractive yet internationally compliant regulatory and tax regimes. In applying a balanced and circumspect approach, Singapore looks set to promote the continued prosperity of its wealth management industry.

5. Hong Kong: the gateway to China

In contrast with the proactive strategy adopted by Singapore, the development of the private wealth management industry in Hong Kong can be said to be largely market driven. The Hong Kong government has taken a relatively *laissez-faire* approach, leaving the growth of the industry to market forces and the efforts of market participants. Despite this, the rise of the private wealth management industry in Hong Kong has been no less impressive.

As at the end of 2008, the value of assets under management by Hong Kong's combined fund-management business[65] amounted to HK$5,850 billion.[66] Although this represents a drop of 39.3 per cent from the previous year, the figures remain in an uptrend, standing at HK$7,212 billion on a trailing 3-year-average basis.[67] Furthermore, the international nature of Hong Kong's combined fund management industry appears to have been unaffected by the financial turmoil: the proportion of funds sourced from non-Hong Kong investors remained steady at 64.2 per cent,[68] in line with previous years.

Despite the setbacks suffered as a result of the credit crisis, Hong Kong remains well positioned to serve as a wealth management hub for the region, particularly the mainland Chinese market. As one of the two special administrative regions of the People's Republic of China, it is one of the world's leading international financial centres with a highly developed capitalist economy that has been ranked the freest in the world for 16 consecutive years[69] by the Index of Economic Freedom published by the Heritage Foundation. Its strengths include its competitive tax regime, respect for the rule of law supported by an efficient and independent judiciary, and the absence of exchange controls or restrictions on capital inflows and outflows. Also central to Hong Kong's success are its stable regulatory environment, bank secrecy rules, extensive network of financial services groups and access to HNWIs. The liberalization of Renminbi (RMB) settlement

64 *IMD World Competitiveness Yearbook 2009* (Institute for Management Development, Lausanne 2009).

65 Comprising SFC-authorized real estate investment trusts management business, asset management, fund advisory business and other private banking business.

66 The Securities and Futures Commission, *Fund Management Activities Survey* (Hong Kong 2008) <http://www.sfc.hk/sfc/doc/EN/speeches/public/surveys/09/fmas_090728.pdf> accessed 6 July 2010.

67 Ibid.

68 Ibid.

69 During the period from 1995 to 2010.

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regulations is also expected to attract more HNWIs from the mainland into Hong Kong's private wealth management industry. These factors will be discussed further below.

Concentration of financial professionals and HNWIs

Hong Kong has one of the highest concentrations of international banks in the world. As at the end of May 2010, there were a total of 146 licensed banks, 24 restricted licence banks and 27 deposit-taking companies in Hong Kong, together with 70 local representative offices of overseas banking institutions.[70] In the wealth management arena, established Swiss players such as UBS and Credit Suisse, as well as international firms like Standard Chartered Bank and HSBC, have a long history in Hong Kong. This year alone has seen a number of key Swiss players establish operations in Hong Kong, including the opening by Bank Sarasin & Cie of a full-service branch in Hong Kong, its first international branch outside of Switzerland.[71] Bank Cantonale de Genève, a cantonal bank majority-owned by the Swiss government, has also launched a representative office in Hong Kong to access rising regional demand for wealth management services.[72]

Factors that attract financial institutions to Hong Kong include its sound regulatory environment, low tax rates and clear tax regime, strong talent base and the quality of its communications and supporting infrastructure. This favourable environment has resulted in the growth of an integrated network of institutions and markets which provide a wide range of products and services to local and international customers, including retail and institutional banking business such as deposit-taking, trade financing, corporate finance, treasury activities, precious metal trading and securities broking. Multidisciplinary houses with a regional investment banking presence are well placed to expand into related businesses and markets, including the private wealth management arena, fuelled by the demand for their products and services from HNWIs both in Hong Kong and around the region.

HNWIs are in turn attracted to Hong Kong by the range of investment products and expertise available, its competitive tax regime and the absence of any exchange controls or restrictions on capital flows into and out of Hong Kong. The introduction of the Capital Investment Entrant Scheme in 2003 to facilitate the entry of foreign nationals into Hong Kong for residence through capital investment of at least HK$6.5 million into permissible assets, may also have played a part in attracting HNWIs into the city, having brought in more than HK$50 billion of capital into Hong Kong since its inception.[73]

This convergence of investors and financial professionals puts Hong Kong in a good position to develop into the wealth management hub for mainland China and, indeed, the rest of Asia.

70 Hong Kong Monetary Authority, 'Monthly Statistical Bulletin' (July 2010, Issue No 191) <http://www.info.gov.hk/hkma/eng/statistics/msb/index.htm> accessed 5 July 2010.

71 Leigh Powell, 'Sarasin unveils "historic" HK branch' *Asiamoney* (18 March 2010) <http://www.asiamoney.com/Article/2447996/Sarasin-unveils-historic-HK-branch.html?> accessed 22 June 2010.

72 Leigh Powell, 'Swiss state bank embarks on Hong Kong build-out' *Asiamoney* (23 March 2010) <http://www.asiamoney.com/Article/2450450/Search/Results/Swiss-state-bank-embarks-on-Hong-Kong-build-out.html?> accessed 22 June 2010.

73 Enoch Yiu, 'Rich Migrants Have Best of Both Worlds' *South China Morning Post* (Hong Kong 14 June 2010) Business B1.

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Regulatory framework

Hong Kong's legal and regulatory framework for the financial sector is transparent and efficient, and adheres to international standards of financial regulation. There are no specific barriers to entry by foreign firms. The principal regulators for the private banking industry are the Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC) and, to a lesser extent, the Insurance Authority, who are responsible for oversight of the banking industry, securities and futures and insurance industries, respectively.

Private banks wishing to set up in Hong Kong are required to obtain authorization from the HKMA if they wish to take deposits and/or carry on banking business. There are three categories of authorization:

- Licensed banks may operate current and savings accounts, and accept deposits of any size and maturity from the public and pay or collect cheques drawn by or paid in by customers.
- Restricted licence banks may take deposits of any maturity of HK$500,000 and above.
- Deposit-taking companies are restricted to taking deposits of HK$100,000 or above with an original term to maturity of at least 3 months. These companies generally engage in a range of specialized activities, including consumer finance, trade finance and securities business.

Apart from the above categories of authorized institutions that are permitted to take deposits in Hong Kong, overseas banks may also establish local representative offices. However, these offices are not permitted to engage in banking business and their role is confined mainly to liaison work between the bank and its Hong Kong-based customers.

A separate licensing regime, administered by the SFC, applies to firms wishing to engage in securities- or futures-related businesses or asset management (although institutions already authorized by the HKMA continue to liaise through the HKMA in this regard). The category of licence(s) required depends on the types of services provided, and may include, for example, 'dealing in securities', 'advising on securities', 'dealing in futures contracts', 'advising on futures contract', 'leveraged foreign exchange trading' and 'asset management'.

The Hong Kong regulators' priorities are to maintain financial stability and investor confidence through regulation, while at the same time remaining wary of undermining the growth of the industry through excessive intervention. An example of this approach can be seen in the concessions granted to SFC-licensed firms when dealing with 'professional investors' (such as HNWIs with a net worth of HK$8 million or above), which include relaxations from the rules which otherwise require firms to comply with trade reporting requirements and to ensure product suitability when making recommendations. Introduction of new regulations and policy changes are usually preceded by public consultation, which also serves as a forum where regulators can maintain an ongoing dialogue with industry practitioners.

Overall, Hong Kong's financial system has performed better than most in the midst of the global financial turmoil, and banks remain well capitalized. Unlike in a number of jurisdictions around the world, none of Hong Kong's locally incorporated licensed banks

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have required any capital injections from the government, although measures were announced by the government to provide such support if necessary.[74]

Banking secrecy

Hong Kong has strict bank secrecy laws, but unlike Switzerland and Singapore, these are embedded in the common law rather than in statute. Nevertheless, they are still strongly entrenched principles and, in practice, arguably no weaker than those in jurisdictions with a statutory right to secrecy (particularly given recent events in Switzerland). These common law principles are supplemented by data privacy legislation and non-mandatory codes of conduct which together provide a framework in which customer information is afforded protection.

Hong Kong common law imposes a duty of confidentiality arising as an implied term of the contract between a bank and its customer. This duty of confidentiality extends to all information that a bank may have concerning its customers, and extends to all banks (whether local or foreign) in Hong Kong and their customers where the relationship is governed by Hong Kong law. The right to confidentiality belongs to the customer, not the bank, and may be waived only by the customer. It is subject only to four exceptions, namely, where disclosure is required under compulsion of law, where there is a duty to the public to disclose, where the interests of the bank require disclosure and where the customer has (expressly or impliedly) consented to such disclosure. The duty is a legal one (not merely a moral duty), breach of which gives rise to a right to claim for damages. A breach of this duty may also be restrained by an injunction, subject to the usual discretion of the rules of equity.

Separately, the Personal Data (Privacy) Ordinance (Cap. 486) (PDPO) seeks to protect the privacy interests of living individuals in relation to their personal data. Personal data are data that directly or indirectly relate to a living individual, from which the identity of the individual may be ascertained and which are in a form in which access or processing is practicable. Any person who controls the collection, holding, processing or use of personal data is required, amongst other things, to maintain appropriate security measures to such data. This duty will thus extend to banks in the holding of customer information.

The Code of Banking Practice reiterates the principles of confidentiality under the common law and the PDPO in the context of the banker–customer relationship. It provides that institutions should treat their customers' (and former customers') banking affairs as private and confidential, and requires institutions to comply with the PDPO in the collection, use and holding of customer information. Although the Code does not have the force of law, it has been endorsed by the HKMA and all banks in Hong Kong are expected to comply with the Code. The HKMA monitors compliance with the Code as part of its regular supervision, and breaches of the Code (or indeed the PDPO or common law duty of confidentiality) may lead the HKMA to consider whether an

74 Alfred Liu and Benjamin Scent, 'You Can Bank on it' *The Standard* (Hong Kong 15 October 2008) <http://www.thestandard.com.hk/news_detail.asp?pp_cat=30&art_id=72879&sid=21002985&con_type=3> accessed 22 June 2010.

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institution is fit and proper to continue to remain licensed. Indeed, the HKMA has in the past been quick to investigate reports of leaks by banks of confidential customer information, and have issued a number of guidelines to banks underlining the importance of maintaining confidentiality.[75]

Family trust laws

Hong Kong's trust laws are currently going through a process of modernization, driven by the government's acknowledged objective to promote the wealth management business in Hong Kong and enhance its position as an international financial centre. In April 2010, the government published its consultation conclusions on the review of the Trustee Ordinance with the aim of introducing amendments into the legislation in 2011. The proposed reforms are intended to modernize Hong Kong trust law and provide greater clarity and certainty in trust arrangements in order to meet evolving market needs. The proposed changes include:

- introducing a statutory duty of care for trustees;
- providing for remuneration of professional trustees;
- empowering trustees to appoint agents, nominees and custodians;
- introducing wider powers for trustees to insure trust property and
- repealing complex and outdated rules against perpetuities and excessive accumulation of income.

As the Trustee Ordinance is primarily a default statute, its provisions as to trustees' powers generally only apply insofar as a contrary intention is not expressed in the trust instrument. Thus there is still scope for parties to agree contrary arrangements notwithstanding the changes. Overall, the proposed amendments are regarded as a welcome step in providing a favourable environment for the development of trust services and the wider private wealth management industry in Hong Kong.

Relaxation of Renminbi settlement regulations

The private wealth management industry in China is not well developed and consequently many HNWIs there choose to have their wealth managed by private banks in Hong Kong. A further draw has been the relaxation of RMB settlement regulations in the mainland which has led to a growing availability of RMB-denominated products available in Hong Kong and an opportunity for PRC investors to invest in their home currency (through offshore vehicles).

Landmark RMB issues in Hong Kong include the RMB5 billion launch of RMB bonds by China Development Bank in July 2007,[76] the first offshore RMB bond issue, and the RMB6 billion launch by the PRC government of fixed rate bonds for sale to retail and institutional investors in Hong Kong, marking the first sovereign RMB bond issue

75 Hong Kong Monetary Authority, 'Customer Data Protection' <http://www.info.gov.hk/hkma/eng/guide/circu_date/20080710e1.htm> accessed 6 July 2010; Hong Kong Monetary Authority, 'Examinations on Controls over Customer Data Protection' <http://www.info.gov.hk/hkma/eng/guide/circu_date/20061129e1.htm> accessed 6 July 2010.

76 'China's first RMB bond in Hong Kong hugely oversubscribed' *People's Daily Online* (PRC 10 July 2007) <http://english.peopledaily.com.cn/90001/90778/6211496.html> accessed 13 July 2010; Hong Kong Trade Development Council, 'Debt Market' <http://www.hktdc.com/info/vp/a/bkfin/en/1/4/1/1X003UPT/Banking—Finance/Debt-Market.htm> accessed 13 July 2010.

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outside of mainland China.[77] In July 2010, Hopewell Highway Infrastructure Limited closed a RMB1.38 billion offering, representing the first time a non-PRC issuer has issued a RMB-denominated bond.[78] The range of RMB-denominated products available in Hong Kong has further expanded to include RMB-denominated life policies, mutual fund, certificates of deposits, structured deposits and other equity and currency-linked structured products. A number of regulatory changes and policy statements have been made by the PRC and Hong Kong regulators to facilitate the growth of the offshore RMB market in Hong Kong. For instance, offshore corporations may now open RMB accounts and there is no limit on the exchange of RMB into a foreign currency by corporations subject only to the overall liquidity of the market. Many foreign investors have been receiving dividends from their onshore direct investment projects in RMB outside of China. The amount of RMB deposits in Hong Kong has also significantly increased since July primarily due to the increase in RMB trade settlement activities after the regulatory changes.

Currently, however, the exchange of RMB for Hong Kong dollars (or vice versa) by individuals is subject to a daily cap of RMB20,000.[79] This limit constrains the ability of PRC-based investors to acquire investments in Hong Kong. Many hope that once these limits are relaxed, this will allow the movement of further funds from mainland HNWIs into the Hong Kong banking sector, benefiting the growth of its private wealth management industry.

Tax regime

As indicated previously, the private wealth management industry in Hong Kong has been encouraged by the competitive tax regime. General features of the Hong Kong tax regime which would be relevant in this regard include a competitive corporate tax rate of 16.5 per cent, which will be applicable to wealth managers' own profits, coupled with a competitive personal income tax system, which imposes a maximum effective tax rate of 15 per cent on employment income. Consequently it is fairly easy to attract expatriate finance professionals to Hong Kong. Additionally, there is no value-added tax (VAT) or other forms of sales tax, which means that there is less tax administration for wealth managers than in other jurisdictions where such taxes are imposed on their fee income, as well as no issue of irrecoverable VAT costs triggered by the provision of services not subject to VAT. The absence of withholding taxes on dividends or interest, Hong Kong's

77 Bob Chen, 'China to Sell 6 Billion Yuan of Bonds in Hong Kong' *Bloomberg* (8 September 2009) <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a8dRCe61kx6w> accessed 13 July 2010; Hong Kong Monetary Authority, 'Renminbi Business in Hong Kong' <http://www.info.gov.hk/hkma/eng/renminbi/> accessed 13 July 2010; Hong Kong Trade Development Council, 'Debt Market' <http://www.hktdc.com/info/vp/a/bkfin/en/1/4/1/1X003UPT/Banking—Finance/Debt-Market.htm> accessed 13 July 2010.

78 Rachel Evans, 'Hopewell: How RMB Bonds Went International' *International Financial Law Review* (13 July 2010) <http://www.iflr.com/Article/2629741/Channel-Sector-News-and-deals/Hopewell-How-renminbi-bonds-went-international.html> accessed 14 July 2010.

79 Hong Kong Monetary Authority, 'Renminbi Business in Hong Kong' <http://www.info.gov.hk/hkma/eng/renminbi/> accessed 13 July 2010; Tony Liaw, Derek Yiu and Beth Ye, 'Companies to Get Free Rein on Yuan Exchange' *The Standard* (Hong Kong, 14 July 2008) <http://www.thestandard.com.hk/news_detail.asp?pp_cat=30&art_id=100522&sid=28887570&con_type=1> accessed 14 July 2010.

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general exemption of dividend income from taxation,[80] as well as the lack of any estate duty or inheritance tax in Hong Kong are additional factors which serve to make Hong Kong an attractive destination for wealth managers and HNWIs alike.

The targeted scope and territorial basis of taxation by Hong Kong's tax authorities is also another reason that makes Hong Kong appealing to wealth managers, as only profits arising in or derived from the conduct of a trade, profession or business in Hong Kong are subject to Hong Kong profits tax.[81] Hong Kong profits tax does not apply on a catch-all basis to any and all income. Furthermore, the Inland Revenue Department (IRD) publicly takes the position that profits from the purchase and sale of listed shares and other listed securities on an exchange should generally be treated as sourced where the exchange is located on which the shares or securities are traded (the analysis may be different for over-the-counter trades).[82] Thus wealth managers in Hong Kong may be reasonably confident that profits from trading overseas securities on behalf of their clients should not be taxable in Hong Kong.

The exemption from taxation of gains derived from the sale of capital assets is yet another factor contributing to the conducive tax environment for the wealth management industry.[83] As in Singapore, there can be debate regarding where the line is drawn between capital assets and trading assets. However, the investment objectives of some HNWIs, being focused on the long-term accumulation of wealth, should place them on the exempt, capital side of the line. Also, there is an unwritten practice of the IRD that in general they do not treat individuals as traders in securities, except where the individuals work in or own securities firms. This, however, does not apply if the individuals use a company to transact in securities.

There is no specific tax exemption for trust vehicles in Hong Kong. However, like Singapore, Hong Kong has a number of specific exemptions relevant to the wealth management sector, which may be applicable to trusts. Where these exemptions are not applicable, the tax treatment of a trust may be subject to some uncertainty in Hong Kong, as the general taxing provision in the Inland Revenue Ordinance (IRO) focuses on the trustee of a trust estate[84] without making clear what profits may be taxable in the hands of the trustee. Case law has also been contradictory on this point,[85] so clarification of the law in this area would be beneficial for the trust sector in Hong Kong.

Section 26A(1A) of the IRO provides an exemption from profits tax for profits received by or accrued to 'specified investment schemes'. These include mutual funds, unit trusts and similar investment schemes which are authorized under the Securities and

80 Section 26(a), Inland Revenue Ordinance (Cap 112) (the IRO).

81 In accordance with s 14, IRO.

82 Paragraph 45, Departmental Interpretation and Practice Notes (DIPN) No 21 (Revised December 2009).

83 Section 14, IRO excludes 'profits arising from the sale of capital assets' from the scope of assessable profits.

84 The definition of 'person' used in s 14 of the IRO, which is found in s 2(1) of the IRO, includes 'a corporation, partnership, trustee, whether incorporated or unincorporated, or body of persons'; no reference is made to trusts themselves being taxable entities. As s 14 provides that a person is subject to profits tax in respect of 'his assessable profits', it is therefore uncertain whether trustees are subject to tax in respect of trust income.

85 For discussion of the relevant principles, please refer *inter alia* to the Inland Revenue Board of Review decision in case D37/93 IRBRD Vol 8, 304 and the decision of the High Court in *Hong Wah Investment Co Ltd v CIR* [1990] (1 HKRC 90-041).

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Futures Ordinance (SFO), and other investment schemes where the Commissioner of Inland Revenue ('Commissioner') is satisfied that they are bona fide widely held[86] and comply with the requirements of 'a supervisory authority within an acceptable regime'.[87] The exemption applies equally to resident and non-resident funds meeting the conditions. Mutual funds, unit trusts and other similar investment schemes, including offshore funds, which are neither authorized nor 'bona fide widely held and supervised' do not qualify for the tax exemption under Section 26A(1A).

Private equity funds, hedge funds and other private wealth vehicles will by definition fall outside the scope of the Section 26A(1A) exemption. Such entities may instead benefit from Hong Kong's so-called 'Offshore Fund Exemption', introduced in 2006.[88] In fact, notwithstanding the name, the exemptions available under the 'Offshore Fund Exemption' apply generally to non-resident persons, but were introduced for the specific purpose of enhancing Hong Kong's competitiveness in the asset management industry by protecting offshore funds against the risk of Hong Kong taxation being triggered as a result of investment activities being carried on in Hong Kong on their behalf. In overview, three conditions must be met for a fund to benefit from exemption: (i) the fund must be regarded as a 'non-resident'; (ii) its activities in Hong Kong must be limited to 'specified transactions'[89] and transactions incidental thereto and (iii) those transactions must be carried out through, or arranged by, a 'specified person'.[90]

In relation to any year of assessment, a corporation, a partnership or a trustee of a trust estate is regarded as a non-resident person if the central management and control of the corporation, partnership or trust estate is not exercised in Hong Kong in that year of assessment. The concept of central management and control is commonly used in a corporate context and is taken to refer to the highest level of control of a company. This concept can also be readily applied to a partnership. However, there is no guidance

86 Section 26A(1A)(a)(ii), IRO—the IRD has stated at para 20, DIPN No 20 (Revised June 1998), that it may be presumed that the 'bona fide widely held' requirement is satisfied 'if, during the year of assessment in question, at no time did fewer than 50 persons hold (or have the right to become the holders of) all of the units or shares in the scheme and at no time during the year did fewer than 21 persons hold (or have the right to become the holders of) units or shares that entitled the holders, directly or indirectly, to 75 per cent, or more, of the income or property of the scheme'. Even where these tests are not met, 'it will still be accepted in practice that the requirement has been satisfied if it is clear from the constitutive documents of the scheme and other relevant material that it was established with a view to wide public participation and that genuine efforts are being taken with the aim of achieving that objective'.

87 There is no statutory definition of an 'acceptable regulatory regime'. However, the IRD states at para 22, DIPN No 20, that 'it will be accepted, unless there is evidence to the contrary, that a scheme qualifies in this respect if it is a scheme of a kind listed in Appendix A1 (Recognised Jurisdiction Schemes) of the Securities and Futures Commission (SFC) Code on Unit Trusts and Mutual Funds and has received recognition of such status from the supervisory authority corresponding to the SFC in the jurisdiction concerned'. Other regimes may be considered acceptable on application if they 'lay down standards for collective investment schemes which are comparable to those detailed in the SFC Code' and actively promote compliance.

88 Enacted by the Revenue (Profits Tax Exemption for Offshore Funds) Ordinance 2006, which introduced ss 20AB, 20AC, 20AD and 20AE to the IRO.

89 'Specified transactions' are defined in Schedule 16 of the IRO and include transactions in securities; transactions in futures contracts; transactions in foreign exchange contracts; transactions consisting in the making of a deposit other than by way of a money-lending business; transactions in foreign currencies; and transactions in exchange-traded commodities. 'Securities' do not include shares in a Hong Kong private company for this purpose.

90 'Specified persons' are defined in s 20AC(6)(b) IRO to mean in relation to a transaction carried out on or after 1 April 2003 'a corporation licensed under Part V of the Securities and Futures Ordinance (Cap. 571) to carry on, or an authorised financial institution registered under that Part for carrying on, a business in any regulated activity within the meaning of Part 1 of Schedule 5 to that Ordinance'.

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available on how it should be interpreted in the context of a trust estate, which creates some uncertainty for trust vehicles as regards the application of the 'Offshore Fund Exemption'.

The exemption also covers profits derived from the incidental transactions provided that the trading receipts from the incidental transactions do not exceed 5 per cent of the total trading receipts from both the specified transactions and the incidental transactions. If the 5 per cent threshold is exceeded, the trading receipts from all the incidental transactions will be chargeable to profits tax.[91] However, profits from the specified transactions will remain fully exempt. In contrast, if the non-resident carries out just one transaction in Hong Kong other than specified transactions, or transactions incidental to specified transactions, they will lose their exemption on all transactions for the year of assessment in question.[92] Operating within the parameters of the defined 'specified transactions' is therefore crucial for funds seeking to rely on the 'Offshore Fund Exemption'. It is also important to note that the exemption is targeted at non-residents. Accordingly, there are provisions to prevent Hong Kong residents from benefiting by investing in a non-resident vehicle.[93] Essentially, these apply where a Hong Kong resident, together with associates, holds directly or indirectly more than a 30 per cent interest in a non-resident which benefits from the exemptions, unless the vehicle is 'bona fide widely held'.[94]

It will be appreciated from the above that the tax exemptions available for funds in Hong Kong are selective, and will not cover every type of entity established for wealth management purposes. Nonetheless, many funds and vehicles are able to benefit from the protection of these exemptions, as well as benefiting from the benign, general, Hong Kong taxing provisions discussed earlier.

Hong Kong has also been active in responding to the OECD's initiatives on tax avoidance. By virtue of China's status in the G20, the Special Administrative Regions of Hong Kong and Macau were not included on the OECD's so-called grey list of non-compliant jurisdictions in April 2009, on the basis that they had committed to sign at least 12 agreements with other jurisdictions implementing the internationally agreed tax standard on exchange of information. In 2010, Hong Kong passed legislation to enable it to adopt the OECD's current model exchange of information article, and at the time of writing Hong Kong has fourteen double tax agreements signed which comply with the required standard, and a number of others in the pipeline. Previously, Hong Kong tax law did not permit the IRD to collect tax information in which it had no domestic tax interest, nor to exchange such information with another jurisdiction, which contributed to perceptions that Hong Kong was complicit in tax evasion. The actions taken over the last year should counter such perceptions and the associated risk of adverse treatment by OECD countries of enterprises or persons using Hong Kong to do

91 Section 20AC(1)(b)/(4) IRO.

92 Section 20AC(3) IRO.

93 Section 20AE IRO.

94 The same definition of 'bona fide widely held' applies as under s 26A(1A)—see n 86.

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business. At the same time, the Hong Kong authorities have ensured safeguards for taxpayers with regard to the exchange of information under double-tax agreements. In particular, Hong Kong's policy on the exchange of information is to restrict it to exchange in response to specific and bona fide requests received from the competent authority of a treaty partner in justifiable cases. Information exchanged under double taxation agreements will also be subject to strict confidentiality rules. The IRD has issued guidance to explain the safeguards to protect taxpayers' confidentiality and privacy rights, and its administrative practice in relation to exchange of information with treaty partners.[95]

6. Conclusion

This article has sought to describe, from a legal and regulatory perspective, how Singapore and Hong Kong, being beneficiaries of Asia's remarkable growth in recent years, have developed an accommodative environment to capitalize and take advantage of the opportunities arising from the 'Asian Wave'. The authors acknowledge that 'the whole is more than the sum of its parts' and an attempt to highlight merely the legal and regulatory factors that contributed to the growth of the private wealth management industry in Singapore and Hong Kong would not suffice. Nonetheless, the authors hope that this article will be illustrative of the facilitative role regulators and governments can play in such development.

95 DIPN No 47 (Issued June 2010).

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