

GUIDANCE NOTE ON PRACTICES BY FUND MANAGEMENT COMPANIES IN RESPECT OF WHOLESALE FUNDS

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PART I

INTRODUCTION

- 1.1 The Securities Commission Malaysia (SC) has set out a number of core principles that a fund management company must ensure compliance with under the *Guidelines on Compliance Function for Fund Management Companies* (Compliance Guidelines).
- 1.2 This *Guidance Note on Practices by Fund Management Companies in respect of Wholesale Funds* (Guidance Note) seeks to provide clarification on some practices or aspects of fund management activities relating to wholesale funds¹ (WSF) that the SC may consider as non-compliant with one or more of the core principles set out under the Compliance Guidelines.
- 1.3 A fund management company who engages in such practices or aspects of fund management activities may reflect adversely on the fit and properness of the fund management company, and may result in the SC taking regulatory or other appropriate actions against it.
- 1.4 This Guidance Note should be read together with the relevant laws and regulations, and guidelines issued by the SC.
- 1.5 For the avoidance of doubt, this Guidance Note does not prevent the SC from exercising its powers under the securities laws or take any action should the need arise.

¹ As defined in the *Guidelines on Unlisted Capital Market Products under the Lodge and Launch Framework* (LOLA).

PART II

GUIDANCE NOTE ON PRACTICES RELATING TO WHOLESALF FUNDS

General

- 2.1 The SC may take into account the overall circumstances in assessing whether a practice or aspect of fund management activities may be considered as non-compliant with any core principles set out under the Compliance Guidelines.
- 2.2 The core principles referred to in this Guidance Note on the practices or aspects of fund management activities are not intended to be exhaustive.

Establishment of Wholesale Funds

- 3.1 A fund management company should not initiate or facilitate the establishment of a WSF for the primary purpose of or consisting only a particular investor and persons associated² to that particular investor, when it is more appropriate that the fund management activities to be by way of portfolio management to prevent or address potential issue of conflicts and/or the use of the WSF as a structure to circumvent any of the requirements as described in paragraph 4.1 and 4.2 below.
- 3.2 The SC is likely to consider the facts including characteristics, practices of and assessments undertaken in respect of the WSF set out in paragraph 3.1 above in assessing and determining the non-compliance with the core principles of integrity and business conduct.

Investment Practices

- 4.1 In selecting the investment for WSF, fund management company should exercise professional scepticism and place greater scrutiny before any decision is being made particularly where it is a recommendation by the investor for the WSF to invest in or purchase such specific securities, which may or may not be connected to the investor or persons associated to the investor.
- 4.2 Where a WSF makes any investment that would result in the circumvention of the requirements of any laws, rules, regulations, guidelines or other requirements governing the investor and/or its investment in the capital market products or any other investment products, the SC is likely to consider such practice as non-compliant with the core principles of integrity, skill, care and diligence or business conduct.

² As defined in section 3 of the *Capital Markets and Services Act 2007*.

Example for paragraphs 4.1 and 4.2

A fund, based on an investor's recommendation, makes an investment in bond or sukuk issued by that investor's related company which if the investor had invested directly would have triggered the required cancellation of the bond or sukuk as stipulated in the Principal Terms and Condition (PTC) for the bond or sukuk.

- 4.3 There could be a concern of potential derogation of the fund management company's independence and objectivity in managing the WSF which may arise in circumstances where the WSF is having or being dependent on a single or significant investor (whether individual or a company or its group of companies) giving rise to the investor having or perceived to have influence over the WSF. Where a WSF is managed to the effect that any investment-related decisions or any operation of the WSF would be under the influence, whether directly or indirectly, of a third party or any particular investor, the SC is likely to consider such practice as non-compliant with the core principles of integrity, acting in clients' interests, skill, care and diligence or business conduct.

Example for paragraph 4.3

A fund is established and structured with a condition or an understanding with the client that would result in the investors for the fund to consist solely of a client and its group of companies. Such arrangement may include a restriction that no other investor may invest in the fund without the client's approval.