

Guidelines On Hedge Funds Reporting Requirements

Introduction

The Securities and Futures Commission (the Commission) has published the Guidelines on Hedge Funds Reporting Requirements (the Guidelines). The Guidelines sets out the minimum amount of information that is required to be disclosed in regular reporting to holders.

1. Pursuant to Chapters 5.17 and 11.6 of the Code on Unit Trusts and Mutual Funds (the Code), authorized schemes are required to publish at least two reports in respect of each financial year, of which the annual report must be audited by the auditor for the scheme. Pursuant to Chapter 8.7(v) of the Code, authorized hedge funds are also required to publish quarterly reports for holders. The following scheme reports should be distributed to holders and filed with the Commission within the stipulated timeframe:

Nature of reports	<i>No. of reports for each scheme financial year</i>	<i>Timeframe for filing and distribution to holders</i>
Annual report	One	Within four months of the end of the relevant financial year, [except for fund of hedge funds (FoHFs) where the timeframe for filing and distribution to holders is within six months of the end of the relevant financial year].
Semi-annual report	One	Within two months of the end of the relevant period
Quarterly reports	Four	Within one month of the end of the relevant period

Note: Where the management company wishes to report to holders via monthly reports, there is no need to prepare quarterly reports provided that the same requirements for quarterly reports are complied with in the monthly reports.

2. These Guidelines aims to provide further guidance to management companies regarding the on-going reporting requirements of authorized hedge funds. *The Commission reserves the right to require additional disclosure to be made.*
3. For the ease of understanding by holders, where technical terms are used in the scheme reports, the management company should include a glossary to explain their meaning and their implications to investors.
4. Where the provisions refer to the scheme, this means the authorized hedge fund.

A. Contents of Financial Reports

Requirements Applicable to Both Annual and Semi-Annual Reports

5. [Annual and semi-annual reports of the scheme must be prepared in accordance with International Accounting Standards (IAS) as promulgated from time to time by the International Accounting Standards Board.

Note: Where the scheme is an existing fund that adopts a different accounting standard from IAS and the financial year end for its annual report (or the end of the reporting period for its semi-annual report, if more recent) falls on a date within four months from the effective date of these Guidelines, the scheme is not required to prepare such report in accordance with IAS until the next reporting period provided that it discloses and explains differences of accounting practice between IAS and the accounting standard adopted by the scheme, and include a statement of the financial effect of any such material differences.]

6. Annual and semi-annual reports of the scheme must contain the information as required by Appendix E of the Code, with the exceptions as provided in paragraph 7.
7. The Commission encourages full disclosure of individual holdings of the scheme. Where the management company is satisfied that full disclosure of such information may be unduly burdensome, it may adopt alternative disclosures in lieu of the disclosure as required in the Investment Portfolio subsection of Appendix E of the Code. In that case, the management company must choose the most appropriate and informative illustration of the scheme's holdings/exposures at the end of the relevant period, taking into account the objective and strategy of the scheme.

[Note: The following will be regarded as minimum disclosures acceptable to the Commission:

- (1) Exposures for the scheme (expressed in percentage terms of net asset value of the scheme) categorized by asset class, geographical region, industry, strategy, or some other basis that the management company considers the most appropriate, taking into account the objective and strategy of the scheme; and*
- (2) Top ten positions of the scheme in absolute terms (ie. counting both the long and short positions of the scheme).]*

Requirements Specific to Annual Reports

8. Annual reports of the scheme must contain the following information:
 - (a) Where the scheme appointed prime broker(s) during the financial year, the name(s) of the prime broker(s), the amount of the scheme's assets held with the prime broker(s) as at the end of the financial year, and their respective maximum levels during the financial year; and

- (b) Where performance fees were borne by the scheme during the financial year, the amount of such performance fees expressed as a percentage of average net asset value of the scheme payable at the scheme level as at the end of the financial year and the calculation basis.

Note: A nil statement is required if no performance fees were borne by the scheme during the financial year.

B. Quarterly Reports

Distribution of Quarterly Reports

9. Quarterly reports are required to be filed with the SFC and distributed to holders within the stipulated timeframe under paragraph 1 of these Guidelines.

Note: Given the newness of these Guidelines to the market, measures would be taken to familiarise the management company with the reporting requirements and the disclosure standard expected of these reports. The first quarterly report of each scheme must obtain a “no objection” letter from the Commission before it is issued to persons in Hong Kong.

10. Quarterly reports may not be distributed to non-holders unless accompanied by the offering document of the scheme.

Contents of Quarterly Reports

11. Quarterly reports must be provided in the English and Chinese languages, and should contain the following information regarding the scheme.

Management Commentary

- (a) Performance review

A commentary by the management company that describes and explains the key factors impacting upon the scheme’s financial performance during the reporting period.

Note: Where the scheme is a FoHFs, the management company is expected to explain what has driven performance in terms of different strategies.

- (b) Market outlook

A discussion of the management company’s expectation of the primary risk factors to which the scheme is exposed to, and the outlook of the development of these factors as they relate to the scheme.

(c) Changes in key investment personnel

A discussion on the changes in composition of the key investment personnel (if any) and their impact on the scheme's overall strategy, risk profile or future performance.

Portfolio Review

(a) Fund size and NAV per unit/share

The scheme's total net asset value, net asset value per unit/share as at the end of the reporting period, and the percentage change in net asset value per unit/share since the last reporting period.

(b) Leverage

The amount of leverage at the scheme level and a summary of its calculation basis as at the end of the reporting period.

Note: The management company is expected to choose the most appropriate and informative illustration of the scheme's leverage at the end of the relevant period, taking into account the objective and strategy of the scheme.

(c) Performance and risk measures

[Disclosure of performance and risk measures of the scheme in tabular form. A sample format with the required parameters and time frames is set out in the **Appendix** to these Guidelines.]

The management company is encouraged to disclose other appropriate performance and risk measures, taking into account the objective and strategy of the scheme (eg. value-at-risk (VaR), % of down months, % of up months etc.).

(d) Amount of seed money

Disclosure of the amount of seed money contributed by the management company or its connected persons as at the end of the reporting period.

(e) Illiquid holdings

Disclosure of any scheme holdings as at the end of the reporting period for which there is no readily available market value, how the value of these holdings are ascertained, and by whom.

Note: For the purposes of presentation, such illiquid holdings should be classified into different categories, eg. securities and derivatives.

(f) Concentrated exposures

Exposures for the scheme (expressed in percentage terms of net asset value of the

scheme) categorized by asset class, geographical region, industry, strategy, or some other basis that the management company considers the most appropriate and informative, taking into account the objective and strategy of the scheme, and the top five positions of the scheme in absolute terms (ie. counting both long and short positions of the scheme).

Note: The Commission reserves the right to require disclosure of the full position of the scheme for the purposes of carrying out its regulatory functions. Such disclosures to the Commission will be subject to the Commission’s preservation of secrecy provisions.

(g) Additional disclosures for FoHFs

Where the scheme is a FoHFs, the management company should include:

- (i) A liquidity profile of the holdings of the FoHFs as at the end of the reporting period. A sample format with the required parameters is set out as follows;

Liquidity Profile of Holdings of [the FoHFs] as at [date]	%
Holdings with less than 30 days to cash	[]
Holdings with 30 to 59 days to cash	[]
Holdings with 60 to 89 days to cash	[]
Holdings with 90 to 179 days to cash	[]
Holdings with 180 or more days to cash	[]
Total scheme net asset value	100%

- (ii) A “percentage closed” figure for the FoHFs (defined as the percentage of the FoHFs’ capital dollars invested in underlying funds that would be closed to further subscriptions by the FoHFs as at the end of the reporting period divided by total capital dollars across all underlying funds); and

Note: “Percentage closed” gives an indication of the FoHFs’ investment in underlying funds that have reached their full capacity with reference to the FoHFs, and whether new subscriptions into the FoHFs are likely to face diluted allocations. It is recognized that funds closed may re-open in future and vice versa, and thus the figure is disclosed as an indication only.

- (iii) The number of underlying funds and number of underlying fund managers included in the FoHFs as at the end of the reporting period.

C. Recommended Practices

12. In addition to the minimum disclosure requirements, the Commission encourages inclusion of the following voluntary disclosures in the scheme’s reports:

(a) Information on inflows and outflows of money

Disclosure of total subscriptions and redemptions of the scheme during the relevant period.

(b) Information on intraperiod holdings

Disclosure of intraperiod investment activities in terms of the highest, median and lowest holdings of the portfolio categorized by asset classes, geographical region, industry, strategy, or some other basis that the management company considers the most appropriate, taking into account the objective and strategy of the scheme.

(c) Information on intraperiod risk measures

Risk measures, including its definition adopted by the management company in preparing the scheme report, of the relevant portfolio in terms of the highest, median and lowest values over the reporting interval and at period end.

Appendix

Information to be Disclosed under Section B.11(f) of the Guidelines on Hedge Funds Reporting Requirements

Actual Monthly Returns in the Last Three Calendar Years (net of all fees and charges)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD Actual
Year (T-2)													
Year (T-1)													
Year T													

Summary Data

	Year T	Year (T -1)	Year (T - 2)	Since Launch ⁴ [specify launch date]
Performance Statistics				
Annual Return				
Annualized Standard Deviation ⁵				
Sharpe Ratio ⁶				
Fund Statistics				
Highest NAV per unit/share				
Lowest NAV per unit/share				
Maximum Drawdown ⁷				

[Display prominent warning statements to the effect that: **“Investment involves risk, please see the offering document for further details. Past performance figures shown are not indicative of future performance.”**]

Notes:

- (1) Calculations must be net of all fees and charges borne by the scheme, with the calculation basis clearly stated.
- (2) “Year T” denotes the current calendar year.
- (3) As per paragraph 3 of the Guidelines, the management company should include a glossary of technical terms to explain their meaning and implications to investors (e.g. the higher the number, the riskier the scheme etc.).
- (4) Statistics since launch can only be shown if the scheme has been in existence for one year or longer.
- (5) “Annualized standard deviation” is defined as the square root of the squared deviations of the actual returns from the simple average return based on the dealing days of the scheme, divided by the number of observations, shown on an annualised basis.
- (6) “Sharpe ratio” is defined as annual return divided by the annualised standard deviation.
NB: For the sake of simplicity, a zero risk free rate is adopted in the calculation for “Sharpe Ratio”
- (7) “Maximum drawdown” is the maximum amount of loss from an equity high until a new equity high, expressed as a percentage of the previous equity high.