

MANDATORY PROVIDENT FUND SCHEMES AUTHORITY

III.11 Guidelines on Spread Requirements

INTRODUCTION

Section 2(1) of Schedule 1 to the Mandatory Provident Fund Schemes (General) Regulation (“the Regulation”) specifies that the total amount invested in securities and other permissible investments (excluding an investment permitted under section 11 of Schedule 1) issued by any one person must not exceed 10 per cent of the total funds of a constituent fund.

2. Section 2(1A) of Schedule 1 to the Regulation further specifies that for the purposes of section 2(1), where the funds of a constituent fund are invested in a relevant investment, the amount invested in the relevant investment is also to be taken into account in the manner specified by the Mandatory Provident Fund Schemes Authority (“the Authority”) for the purposes of section 2(1A) when ascertaining the total amount of the funds invested in the securities and other permissible investments issued by the person who issues the underlying investment of the relevant investment.

3. Section 2(7) of Schedule 1 to the Regulation defines:
- (a) “relevant investment” to mean a permissible investment –
 - (i) the value of which is determined by reference to the value of another investment; and
 - (ii) which is specified, or belongs to a class of investment specified, by the Authority as a relevant investment for the purposes of this definition; and

- (b) “underlying investment”, in relation to a relevant investment, to mean an investment –
 - (i) by reference to the value of which the value of the relevant investment is determined; and
 - (ii) which is specified, or belongs to a class of investment specified, by the Authority as an underlying investment for the purposes of this definition.

4. Section 6H of the Mandatory Provident Fund Schemes Ordinance (“the Ordinance”) provides that the Authority may issue guidelines for the guidance of approved trustees, service providers and other persons concerned with the Ordinance.

5. For the purposes of section 2(1A) of Schedule 1 to the Regulation, the Authority hereby issues guidelines to set out –

- (a) those permissible investments or a class of permissible investments that are “relevant investments”;
- (b) those investments or a class of investments that are “underlying investments”; and
- (c) the manner of taking an investment in a “relevant investment” into account when ascertaining the total amounts of the funds invested in the securities and other permissible investments issued by the person who issues the “underlying investment” of the “relevant investment” (“aggregation manner”).

RELEVANT INVESTMENT, UNDERLYING INVESTMENT AND AGGREGATION MANNER

6. The list of “relevant investment”, “underlying investment” and aggregation manner for the purposes of section 2(1A) of Schedule 1 to the

Regulation is set out in the Annex. For the avoidance of doubt, any investment having values ascertainable by reference to more than one security (such as index-tracking collective investment schemes, approved pooled investment funds, authorized unit trusts, financial futures and option contracts for indices, and any of the investments included in the Annex with more than one underlying security) is not a “relevant investment” for the purposes of section 2(1A).

7. Approved trustees and investment managers are reminded that inclusion of individual class of investments in the Guidelines does not imply permissibility for MPF investment purposes. Permissibility of individual investment depends on the specific investment and whether it fits the statutory definition and meets the relevant permissibility requirements.

EFFECTIVE DATE

8. These Guidelines shall become effective upon the expiry of six months from the date of commencement of the Mandatory Provident Fund Schemes (General) (Amendment) Regulation 2006.

DEFINITIONS OF TERMS

9. Except where otherwise specified in the Guidelines, the terms common to the Ordinance and the subsidiary legislation of the Ordinance carry the same meanings as defined in the Ordinance and the subsidiary legislation. References should be made to the Ordinance and the subsidiary legislation, where necessary.

“RELEVANT INVESTMENT”, “UNDERLYING INVESTMENT” AND AGGREGATION MANNER FOR THE PURPOSES OF SECTION 2(1A) OF SCHEDULE 1 TO THE REGULATION

Relevant Investment	Underlying Investment	Manner of Aggregating Exposure to the Issuer of the Underlying Securities	Illustrative Example¹ (<i>MV = market value</i>)
Equity linked instruments (ELI)	A share or DR, the price of which determines the value of the ELI	The amount invested in an ELI to be added to the amount of investments issued by the entity that issued the underlying investment	MV of ELI issued by B linked to price of shares of A = 100 MV of shares in A held = 200 <u>Total amount of investments:</u> In A = 100+200 = 300 In B = 100
Depository receipts (DR)	A share, the economic benefits of ownership of which the DR entitles the owner to (either directly or through another receipt or certificate)	The amount invested in a DR to be added to the amount of investments issued by the entity that issues the underlying investment	MV of DR over shares in A issued by B = 100 MV of shares in A held = 200 <u>Total amount of investments:</u> In A = 100+200 = 300 In B = 100
Third party convertible debts (TPCD)	A share or DR into which the TPDC may be converted	The amount invested in a TPCD to be added to the amount of investments issued by the entity that issues the underlying investment	MV of TPCD convertible to shares in A issued by B = 100 MV of shares in A held = 200 <u>Total amount of investments:</u> In A = 100+200 = 300 In B = 100
Derivative warrants, not being a covered put warrant (DW) ²	A share that the DW confers a right on the holder to subscribe for from the issuer of the DW	The amount invested in a DW to be added to the amount of investments issued by the entity that issues the underlying investment	MV of DW over shares in A issued by B = 100 MV of shares in A held = 200 <u>Total amount of investments:</u> In A = 100+200 = 300 In B = 100

¹ The illustrative examples are included solely for illustrative purposes and do not form part of the requirements under section 2(1A) of Schedule 1 to the Regulation. For the avoidance of doubt, it should be noted that investments in B in the illustrative examples are still required to comply with section 2(1) of Schedule 1 to the Regulation.

² For the avoidance of doubt, a covered put warrant, which can only be used for hedging purposes under the MPF legislation, needs not be aggregated for the purposes of section 2(1A) of Schedule 1 to the Regulation as it essentially creates a short position of the underlying investment for the fund.