

MANDATORY PROVIDENT FUND SCHEMES AUTHORITY

III.14 Guidelines on Default Investment Strategy

INTRODUCTION

The Mandatory Provident Fund Schemes Ordinance (the Ordinance) provides, among other things, for the establishment of and matters concerning a default investment strategy (DIS) in a registered scheme.

2. Part 4AA of, and Schedules 10 and 11 to, the Ordinance set out requirements for the DIS.

3. Section 6H of the Ordinance provides that the Mandatory Provident Fund Schemes Authority (the Authority) may issue guidelines for the guidance of approved trustees, service providers, participating employers and their employees, self-employed persons, regulated persons and other persons concerned with the Ordinance.

4. The Authority hereby issues guidelines to:

- (a) identify assets which are “higher risk assets” for the purposes of this definition set out in section 1 of Schedule 10 to the Ordinance;
- (b) provide guidance on general investment requirements and other related issues in relation to the DIS;
- (c) provide guidance on payment for services and out-of-pocket expenses in respect of the percentages specified for the purposes of section 34DD(4) set out in sections 1 and 2 of Schedule 11 to the Ordinance;
- (d) set out the manner and the time specified for approved trustees to

locate scheme members for the purposes of section 34DJ(2) of the Ordinance; and

- (e) set out the form of notice specified by the Authority for the purposes of Division 3 of Part 4AA of the Ordinance.

ASSETS IDENTIFIED AS “HIGHER RISK ASSETS”

5. Section 1 of Schedule 10 to the Ordinance defines “higher risk assets” to mean any assets identified as such in the guidelines for the purposes of that Schedule.

6. For the purposes of Schedule 10, the following assets are identified as “higher risk assets”:

- (a) shares;
- (b) warrants;
- (c) financial futures contracts and financial option contracts that are used other than for hedging purposes;
- (d) interests in an index-tracking collective investment scheme (ITCIS) that tracks an index comprised of equities or equities-like securities;
- (e) any investment approved by the Authority under section 8(1)(c) of Schedule 1 to the Mandatory Provident Fund Schemes (General) Regulation (the Regulation) and set out in paragraph 5 of Guidelines III.2 on Equities and other Securities (Guidelines III.2);
- (f) any investment approved by the Authority under section 8(2)(b) of Schedule 1 to the Regulation and set out in paragraph 8 of Guidelines III.2;
- (g) that part of any authorized unit trusts and mutual funds approved by the Authority under section 8(2)(c) of Schedule 1 to the Regulation and set out in paragraph 12(a)(i) to (v) of Guidelines III.2 which is invested in the assets set out in paragraphs (a) to (d) above of this

paragraph 6;

- (h) authorized unit trusts and mutual funds approved by the Authority under section 8(2)(c) of Schedule 1 to the Regulation and set out in paragraph 12(a)(vi) of Guidelines III.2; and
- (i) authorized unit trusts and mutual funds approved by the Authority under section 8(2)(c) of Schedule 1 to the Regulation and set out in paragraph 12(b) and (c) of Guidelines III.2.

7. For the avoidance of doubt, nothing in this guidance affects whether a particular investment is permissible in accordance with section 40 or other sections of the Regulation.

GENERAL INVESTMENT REQUIREMENTS AND OTHER RELATED ISSUES IN RELATION TO THE DIS

Investments in higher risk assets at any point in time

8. Section 34DB(1)(b) of the Ordinance provides that an approved trustee of a registered scheme must ensure that any investment related to the DIS accords with the requirements under Part 4AA of and Part 2 of Schedule 10 to the Ordinance. Section 2 of Schedule 10 to the Ordinance provides that the approved trustee of a registered scheme must make available in the scheme the following constituent funds for investment under the DIS of the scheme:

- (a) a constituent fund investing in a globally diversified manner that targets to invest 20% of the net asset value of the fund in higher risk assets, but the investment in those assets may vary from 15% to 25% of the net asset value of the fund at any point in time (Age 65 Plus Fund);
- (b) a constituent fund investing in a globally diversified manner that targets to invest 60% of the net asset value of the fund in higher risk assets, but the investment in those assets may vary from 55% to 65%

of the net asset value of the fund at any point in time (Core Accumulation Fund).

9. For compliance with the requirements under section 2 of Schedule 10 to the Ordinance, the approved trustee must ensure that, the investment in higher risk assets by the Core Accumulation Fund (CAF) and the Age 65 Plus Fund (A65F) does not, at any point in time, directly or indirectly, breach the percentages of the net asset value as set out in that section. Where the assets of the CAF or the A65F are invested in underlying approved pooled investment funds (APIFs) and ITCISs (other than an ITCIS referred to in paragraph 6(d) above), the approved trustee must determine the percentage of the constituent fund indirectly invested in higher risk assets held in the APIF or ITCIS and, where relevant, APIF or ITCIS invested into by such APIF or ITCIS. For the purposes of determining this, the approved trustee should obtain from the operators of such APIFs and/or ITCISs relevant information about their asset holdings to enable the approved trustee to make the necessary calculations. Trustees of APIFs should endeavour to provide the relevant information to the approved trustee or if relevant, operators of other APIFs that invest in that APIF as regularly as possible.

10. There may be occasions where the asset allocation of the CAF and A65F in the DIS may be outside the targeted limit as set out in section 2 of Schedule 10 to the Ordinance, as a result of market fluctuation. In general, when such a situation is identified, trustees should take steps to remedy the situation as soon as practicable having regard to the interests of scheme members.

De-risking of investment in DIS

11. Section 34DB(1)(c) of the Ordinance provides that, an approved trustee must invest the accrued benefits (which include contributions and transfers) of a scheme member of the scheme according to the DIS, subject to

certain exceptions as specified in sections 34DB(2), 34DB(3), 34DB(4) and 34DC.

12. A key feature of the DIS is the de-risking of investment for scheme members as their age increases. The de-risking provisions, which are set out in section 4 of Schedule 10 to the Ordinance, apply to investments for scheme members who are 50 years of age or above but are below 65 years of age. An approved trustee must invest the accrued benefits in the member's account according to the age of the member in column 1 of the Table in section 4(3) of Schedule 10 in the CAF and A65F in the proportions as set out in the Table.

13. The annual de-risking for a member according to the Table in section 4(3) of Schedule 10 should be undertaken on a date, determined by the trustee of the relevant scheme, that is within a period of 60 days commencing on the birthday of that member.

14. Section 4(2)(d) of Schedule 10 prescribes how a trustee must invest accrued benefits in the member's account in a particular year that "have not been invested". This provision relates to accrued benefits, such as contributions and transfers which have not yet been invested after receipt. The trustee should allocate these benefits between the CAF and the A65F in accordance with the Table as specified in section 4(3) of Schedule 10 according to the age of the member.

De-risking for scheme member who does not have the full date of birth

15. There may be some individual cases where the trustee is not aware of the month and/or day of birth of a scheme member. In such cases, having made reasonable steps to ascertain such information, in the absence of any other evidence, where the trustee is only aware of the year and month of birth (i.e. not

the day of birth), the trustee should use the last day of the month as the birthday of the member, and where the trustee is only aware of the year of birth (and neither the month nor day of birth), the trustee should use the last day of the year as the birthday of the scheme member.

16. Section 6 of Schedule 10 to the Ordinance provides that if the approved trustee is not aware of the age of the member, the trustee must invest the accrued benefits of the member solely in the A65F. A trustee is considered to be aware of the age of the member if the year of birth of the member is known to the trustee, regardless of whether the month or day of birth is also known.

Reference portfolios

17. A reference portfolio for each of the constituent funds under the DIS has been developed by the industry, to which recognition has been given by the Authority for the purpose of the Code on Disclosure for MPF Investment Funds (recognized reference portfolios). The main purpose of the recognized reference portfolios is to provide a common reference point for the approved trustees to report to members about the performance of the CAF and the A65F respectively. The Code on Disclosure for MPF Investment Funds sets out the disclosure requirements relating to the performance measurement that is required to be made against the recognized reference portfolios.

Investment choice

18. Section 34DB(1)(d) of the Ordinance provides that, an approved trustee of a registered scheme must ensure that the DIS is available for selection by scheme members. Section 27(2A) of the Ordinance provides that an approved trustee of a registered scheme must invest the accrued benefits of a scheme member according to the member's selection as permitted under the governing rules. To facilitate trustees in discharging their duty under sections

34DB(1)(d) and 27(2A) of the Ordinance, trustees should ensure that the relevant forms or facilities offering investment choice clearly explain the following issues in a fair and prominent manner:

- (a) scheme members who do not wish to choose an investment option do not have to do so. If they do not make any choice, their accrued benefits (including contributions) will be invested in accordance with the DIS;
- (b) scheme members are free to choose to invest according to the DIS should they agree with and find it suitable for their personal preference. For this purpose, the DIS as a choice should be set out above individual constituent fund choices in relevant choice forms;
- (c) whether there are any limitations on choice combinations as between the DIS and constituent funds of the scheme; and
- (d) where a scheme member has chosen the CAF or A65F as a constituent fund choice, rather than as part of the DIS, an explanation that the automatic de-risking features of the DIS does not apply to such investment.

CONTROL OF PAYMENT FOR SERVICES AND OUT-OF-POCKET EXPENSES RELATING TO DIS

19. Section 34DD of the Ordinance sets out the framework for regulating certain types of fees, expenses and charges relating to the DIS. Section 34DD(1) sets out a general prohibition in relation to charging payments for services to a DIS constituent fund or a scheme member who invests in such fund. Subsection (3) provides exceptions for those payments which are for services that are calculated as a percentage of the net asset value of the fund, certain types of payments to custodians, payments relating to establishment or winding up of a fund and member charges for obtaining certain types of documents.

20. Section 34DD(4) sets out a regime for the control of the amounts and types of items that can be charged to or imposed on a DIS constituent fund or a scheme member who invests in such fund. Section 34DD(4)(a) imposes a daily limit on payments for services permissible under section 34DD(3) and similar amounts chargeable to underlying investment funds. Subsection (4)(b) imposes a separate, yearly limit on the amount of certain types of out-of-pocket expenses that are charged to or imposed on a DIS constituent fund or a scheme member who invests in such funds.

21. Both sections 34DD(1) and 34DD(4) refer to amounts charged to or imposed on a scheme member. This would cover different types of charging mechanisms such as direct billing/payment or deductions made directly from the member's account.

Underlying investment fund fee

22. Section 34DD(4)(a)(ii) of the Ordinance includes in the calculation, payments for services chargeable at the underlying investment fund level. It requires the total amount of “proportionate underlying investment fund fees” chargeable to any underlying investment fund of a DIS constituent fund to be aggregated with certain types of payments for services (PFS) at the constituent fund level (the Aggregate PFS) for the purpose of determining whether the percentage in section 1 of Schedule 11 to the Ordinance is exceeded. The term “proportionate underlying investment fund fee” is defined in section 34DD(5), by reference to the term “**underlying investment fund fee**”. This term is defined in section 34DD(5) to mean any amount payable for the services provided in relation to an underlying investment fund by a “specified person”, but does not include the payment for the services similar to those referred to in sections 34DD(3)(b) and (c) in relation to a DIS constituent fund.

23. The term “specified person” is defined in section 34DD(5) to mean:
- (a) a person (first mentioned person) whose role in relation to an underlying investment fund is similar to that of any of the following persons who provide services in relation to a DIS constituent fund:
 - (i) an approved trustee of a registered scheme;
 - (ii) a specified service provider;
 - (iii) a person named as the sponsor or promoter in the governing rules of the scheme; or
 - (b) a person who provides services that are identical or similar to the services provided by the first mentioned person.

24. At the underlying investment fund level, fee structures may not directly match those at the constituent fund level. Some ITCISs, for example, might not have a party explicitly known as a trustee. In determining what fees or payments to be included as “underlying investment fund fee”, the approved trustees should have regard to the types of functions performed by the various parties. Typically, this would mean that underlying investment fund fees shall include, for example, the ongoing management fees chargeable to the fund for services of a trustee (for trust funds), fund provider (or issuer or management company), investment manager (including performance fee, if any), administrator, distributor, custodian (only those customarily calculated as a percentage of net asset value of the fund). Trustees can ascertain what is “chargeable” for these purposes by reference to the disclosures made by or on behalf of the underlying investment fund or by direct enquiry with the entity that operates the underlying investment fund. If the trustee is unable to ascertain such information, the trustee should use the latest available aggregated data about total expenses (such as a published expense or fee ratio however described).

Determination of Aggregate PFS of a DIS constituent fund

25. The term “proportionate underlying investment fund fee” is defined in section 34DD(5) of the Ordinance, in relation to an underlying investment fund, to mean an amount that is the product of A and B where **A** is the underlying investment fund fee and being calculated as a percentage of the net asset value of the underlying investment fund, and **B** is the proportion of the assets of the DIS constituent fund that is invested in the underlying investment fund. The total amount of the proportionate underlying investment fund fees for a DIS constituent fund shall be the sum of the respective products of A and B for each underlying investment fund of the constituent fund.

26. For the purpose of determining the Aggregate PFS of a DIS constituent fund on a relevant day, the approved trustee has to secure the following information about the constituent fund and those of the underlying investment funds into which the constituent fund invests into, directly or indirectly on the relevant day:

- (a) respective PFS of the DIS constituent fund and underlying investment fund fees of each of its underlying investment funds, expressed as a percentage of the net asset value of the fund (net of any management fee rebate from any constituent fund and underlying investment funds if relevant); and
- (b) asset allocation of the DIS constituent fund in percentage of the net asset value of the fund into each of the underlying investment funds at the cut off time for pricing and valuation of the DIS constituent fund for the relevant day.

27. For a direct underlying investment fund of a DIS constituent fund, **B** is the percentage proportion of the assets of the constituent fund that is invested in the fund on a relevant day. For an indirect underlying investment fund of a

DIS constituent fund (i.e. the constituent fund invests into the fund via one or more upper layers of other investment funds), B is the ultimate proportionate exposure of the assets of the constituent fund into the said underlying investment fund. For example, a DIS constituent fund invests 40% of its assets into an underlying investment fund X, fund X invests 40% of its assets into another underlying investment fund Y and fund Y further invests 60% of its assets into another underlying investment fund Z. The proportionate exposures of the constituent fund's assets (i.e. B) into these funds are respectively: 40% for fund X, (40% x 40%) for fund Y, and (40% x 40% x 60%) for fund Z. Further illustrations on the calculation of B for a DIS constituent fund under different investment structures are provided at Annex A.

Percentage specified for the purpose of section 34DD(4)(a) in section 1 of Schedule 11

28. For compliance with the requirements under section 34DD(4)(a) of the Ordinance, the approved trustee of a registered scheme must ensure that the Aggregate PFS of a DIS constituent fund does not, in a single day, exceed the maximum daily rate specified in section 1 of Schedule 11 to the Ordinance. Whilst this is an ongoing, daily requirement, the frequency of calculation would be a matter for the approved trustee to determine having regard to how close the total aggregate percentage is to the percentage specified in section 1 of Schedule 11, how static allocations to underlying investment funds are and the volatility of other variables that may affect the calculated result. Approved trustees should maintain records of their periodic calculations and the methodology adopted for the frequency of the calculation for consideration and inspection by the auditor of the scheme and the Authority as required.

Illustrations of Aggregate PFS calculations and comparison with percentage specified in section 1 of Schedule 11

29. Annex A sets out some illustrative examples of the calculation of the daily aggregated percentage of PFS for a DIS constituent fund under different investment structures and the comparison against the percentage specified in section 1 of Schedule 11.

Percentage specified for the purpose of section 34DD(4)(b) in section 2 of Schedule 11

30. The term “out-of-pocket expenses” (OPE) is defined in section 34DA of the Ordinance to mean “auditor’s fee for annual audit, printing expenses and postage, fund price publication expenses, bank charges, governmental fees and charges (including but not limited to stamp duty and licence fee), other charges and expenses properly incurred and permitted under this Ordinance, the regulations and the governing rules”. Section 34DD(4)(b) sets out a calculation requirement in relation to certain types of OPE. To comply with that section, the approved trustee will need to identify those OPE items that meet the following statutory criteria:

- (a) the item is charged to or imposed on the DIS constituent fund, or a scheme member who invests in such fund;
- (b) the item is incurred by the approved trustee;
- (c) the item is incurred on a recurrent basis; and
- (d) the item is incurred by the approved trustee in the discharge of the approved trustee’s duties to provide services in relation to the fund.

31. An item would be incurred on a recurrent basis if the item is incurred repeatedly or periodically. Repetition rather than the frequency should be considered, such that an item which is incurred infrequently, e.g. once per year, but on a repeated basis, would be considered to be recurrent. Accordingly,

expenses relating to an annual audit process would be recurrent, however, an audit, independent review or accounting expense related to a one-off issue e.g. scheme merger or a change of trustee or scheme administrator, would not be recurrent. Similarly, investment expenses charged to or imposed on a DIS constituent fund for acquisition or disposal of investments would be recurrent, however, such expenses incurred during a one-off restructuring would not be recurrent. The criteria above would include various types of OPE including, for example, annual audit expenses, printing or postage expenses relating to recurrent activities (such as issuing annual benefit statements), recurrent legal expenses, transaction costs incurred by a DIS constituent fund in recurrent acquisition of investments for the fund (including, for example, costs incurred in acquiring “underlying investment funds” (as defined) or in acquiring securities where relevant) and annual statutory expenses (such as compensation fund levy where relevant).

32. The approved trustee must ensure that the total amount of all payments that are charged to or imposed in a year on a DIS constituent fund, or a scheme member who invests in the fund, for OPE incurred by the approved trustee, when expressed as a percentage of the net asset value of the fund does not exceed the percentage specified in section 2 of Schedule 11 to the Ordinance. The net asset value that should be used for calculating the percentage of OPE is the sum of the net asset value of the relevant DIS constituent fund as at the last dealing day of each month of the relevant year divided by 12. A “year” for this purpose should commence on the start of the financial period of the relevant scheme.

33. For the purpose of determining compliance under section 34DD(4)(b) with the percentage specified in section 2 of Schedule 11, if a scheme has a financial period that commences on a date other than 1 April 2017¹, the approved

¹ The date of commencement of operation of Part 4AA of, and Schedules 10 and 11 to, the Ordinance.

trustee should, for the period preceding the start of the next financial period, pro rate the percentage in section 2 of Schedule 11 accordingly. Pro ratings may also be necessary where a scheme changes its financial period after 1 April 2017.

LOCATING SCHEME MEMBERS

34. Section 34DJ(1) of the Ordinance sets out that that section applies if:

- (a) it comes to the knowledge of an approved trustee of a registered scheme that a specified notice given to an existing member under section 34DI(1) of the Ordinance is not taken to have been given under section 206(1A) or (2) of the Regulation. The specified notice was “not taken to have been given under section 206(1A) or (2)”, for example, when the trustee receives a specified notice returned as undelivered; or
- (b) the trustee is not aware of any contact details of an existing member that enable the trustee to give a specified notice to the member under section 34DI(1).

35. Section 34DJ(2) of the Ordinance provides that the trustee must proceed to locate the member in the manner, and within the time limit, specified in the guidelines for the purposes of that section.

Steps to be taken to locate scheme members

36. For the purposes of section 34DJ(2) of the Ordinance, the specified manner and the time limits for approved trustees to locate scheme members are set out below.

37. Where an approved trustee has complied with section 34DI(1) and, on or before the expiry day of the reply period, has knowledge that the specified notice was “not taken to have been given under section 206(1A) or (2) of the

Regulation”, such that section 34DJ(1)(a) of the Ordinance applies, the trustee must proceed to locate the member in the manner set out in paragraph 39 below within the time limit of 60 days after the trustee has knowledge that the specified notice was not taken to have been given under section 206(1A) or (2) of the Regulation.

38. Where an approved trustee is unable to comply with section 34DI(1) because it is not aware of any contact details of an existing member such that section 34DJ(1)(b) applies, the trustee must proceed to locate the member in the manner set out in paragraph 39 below within the time limit of 6 months after 1 April 2017.

39. Within the time limits specified in paragraphs 37 and 38 above, the approved trustee must attempt to locate the scheme member in the following manner:

- (a) contact the current employer concerned, if any, to obtain any contact information of the scheme member unless the member has been located before the trustee contacts the employer;
- (b) after the trustee has complied with paragraph (a) above, the trustee must make a first attempt to contact the member based on the contact information provided by the current employer in paragraph (a) above or, if none, any other contact information known to the trustee, unless the member has been located before the trustee makes the first attempt. Where the trustee has already sent a specified notice under section 34DI(1), the trustee should use contact information which is different from the contact information used by the trustee for sending that notice if such information is available;
- (c) if the member cannot be located after the first attempt, the trustee must make a second attempt to contact the member, at a time and

date different from those of the first attempt. The trustee should use contact information which is different from the contact information used by the trustee for sending the specified notice under section 34DI(1) (if applicable) and in the first attempt, if such information is available and the trustee is satisfied that the contact information used in the first attempt cannot locate the member;

- (d) if the member cannot be located after the second attempt, the trustee must make a third and final attempt to locate the member, at a time and date different from those of the first and second attempts. The trustee should use contact information which is different from the contact information used by the trustee for sending the specified notice under section 34DI(1) (if applicable) and in the first and second attempts, if such information is available and the trustee is satisfied that the contact information used in the first and second attempts cannot locate the member.

40. If, after section 34DJ(2) has been complied with, a scheme member cannot be located before the expiry of the time limit, the approved trustee must comply with section 34DJ(3).

41. If a scheme member in relation to whom section 34DJ(2) applies is located before the expiry of the time limit, the approved trustee must comply with section 34DJ(4), regardless of whether the member is located as a result of the trustee's attempts to locate the member as set out above.

FORM OF SPECIFIED NOTICE

42. As set out in section 34DF of the Ordinance, "specified notice" means a notice that is approved, or in the form specified, by the Authority for the purposes of Division 3 of Part 4AA of the Ordinance. Section 34DI(1) of the

Ordinance requires that the approved trustee must within 6 months after the commencement date:

- (a) give a specified notice to each existing member in respect of (each of, if applicable) the member's default investment arrangement account (DIA account); and
- (b) in the specified notice, inform the member of the requirements under section 34DI(2) to invest those benefits in the DIA account according to the DIS of the scheme.

43. The form of the notice specified by the Authority for the purposes of Division 3 of Part 4AA of the Ordinance is set out at Annex B.

DEFINITION OF TERMS

44. Where a term used in the Guidelines is defined in the Ordinance or the subsidiary legislation then, except where specified in the Guidelines, that term carries the meaning as defined in the Ordinance or the subsidiary legislation.

ILLUSTRATIONS FOR CALCULATING DAILY AGGREGATE PAYMENT FOR SERVICES FOR A DIS CONSTITUENT FUND

For the purposes of section 34DD(4)(a) of and section 1 of Schedule 11 to the Ordinance, examples are set out below to illustrate how to calculate the daily aggregate payment for services (“PFS”) for a DIS constituent fund (“DIS CF”) under four different investment structures and scenarios. They are provided to assist approved trustees in understanding the relevant calculation and in comparing it against the daily percentage rate set out in section 1 of Schedule 11 to the Ordinance.

Formula for calculating Aggregate PFS of a DIS CF for the purposes of section 34DD(4)(a) of and section 1 of Schedule 11 to the Ordinance

Aggregate PFS (%)

= the total amount of all PFS specified in section 34DD(2) that are charged to or imposed on the fund, or a scheme member who invests in the fund and calculated as a percentage of the net asset value of the fund (%)

+

the total amount of any proportionate underlying investment fund fees chargeable to any underlying investment fund of the fund (%)

where

proportionate underlying investment fund fee = A x B;

and where

A = the underlying investment fund fee (“UIFF”) being calculated as a percentage of the net asset value (“NAV”) of the underlying investment fund;

B = the proportion of the assets of the DIS CF that is invested in the underlying investment fund

Scenario 1: The DIS CF makes direct investment**Assumptions:**

1. PFS of DIS CF = 0.70% p.a. of the CF's NAV

$$\boxed{\text{CF}} \quad 0.70\%$$

Step 1: Calculate the total PFS at CF level and the total proportionate UIFF at underlying investment fund level:

- (a) Total amount of all PFS at CF level = 0.70%
- (b) Total amount of all proportionate UIFF (A x B) = 0%

Step 2: Calculate Aggregate PFS for the DIS CF:

$$\text{Aggregate PFS} = (a) + (b) = 0.70\% + 0\% = 0.70\%$$

Step 3: Compare daily Aggregate PFS with daily rate specified in section 1 of Schedule 11 to the Ordinance:

$$\frac{0.70\%}{N} < \frac{0.75\%}{N}$$

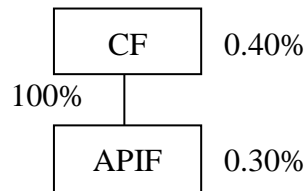
where N is the number of days in the year

Since the daily Aggregate PFS does not exceed the daily rate specified in section 1 of Schedule 11 to the Ordinance, it complies with section 34DD(4)(a) of the Ordinance.

Scenario 2: The DIS CF invests solely in an approved pooled investment fund (“APIF”) which makes direct investment

Assumptions:

1. PFS of DIS CF = 0.40% p. a. of the CF’s NAV
2. For the APIF, A= 0.30% p.a. of the APIF’s NAV, B =100%



Step 1: Calculate the total PFS at CF level and the total proportionate UIFF at underlying investment fund level:

- (a) Total amount of all PFS at CF level = 0.40%
- (b) Total amount of all proportionate UIFF (A x B) = 0.30% x 100% = 0.30%

Step 2: Calculate the Aggregate PFS for the DIS CF:

$$\text{Aggregate PFS} = (a) + (b) = 0.40\% + 0.30\% = 0.70\%$$

Step 3: Compare daily Aggregate PFS with the daily rate specified in section 1 of Schedule 11 to the Ordinance:

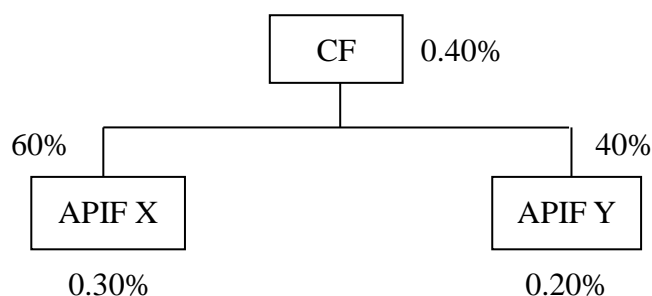
$$\frac{0.70\%}{N} < \frac{0.75\%}{N}$$

where N is the number of days in the year

Since the daily Aggregate PFS does not exceed the daily rate specified in section 1 of Schedule 11 to the Ordinance, it complies with section 34DD(4)(a) of the Ordinance.

Scenario 3: The DIS CF invests into two APIFs which make direct investment**Assumptions:**

1. PFS of DIS CF = 0.40% p. a. of the CF's NAV
2. APIF X and APIF Y make direct investment
3. For APIF X, A = 0.30% p. a. of APIF X's NAV, B = 60%
4. For APIF Y, A = 0.20% p. a. of APIF Y's NAV, B = 40%

**Step 1: Calculate the total PFS at CF level and the total proportionate UIFF at underlying investment fund level:**

- (a) Total amount of all PFS at CF level = 0.40%
- (b) Total amount of all proportionate UIFF (A x B) = 0.30% x 60% + 0.20% x 40%
= 0.26%

Step 2: Calculate the Aggregate PFS for the DIS CF:

$$\text{Aggregate PFS} = (a) + (b) = 0.40\% + 0.26\% = 0.66\%$$

Step 3: Compare daily Aggregate PFS with the daily rate specified in section 1 of Schedule 11 to the Ordinance:

$$\frac{0.66\%}{N} < \frac{0.75\%}{N}$$

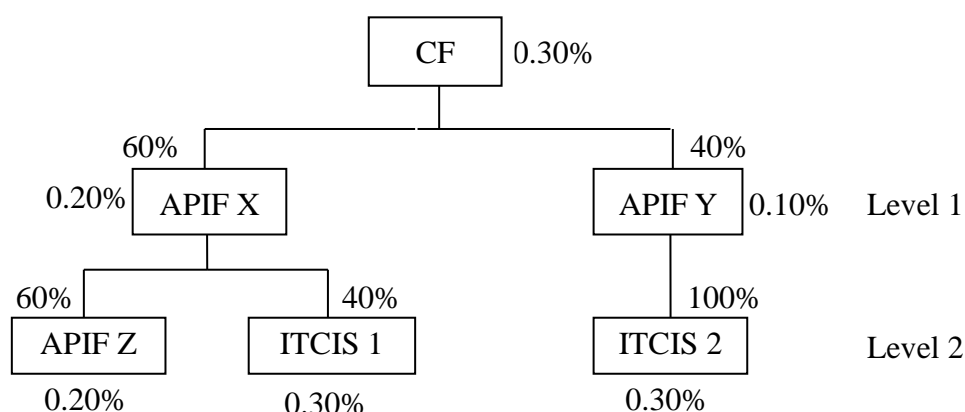
where N is the number of days in the year

Since the daily Aggregate PFS does not exceed the daily rate specified in section 1 of Schedule 11 to the Ordinance, it complies with section 34DD(4)(a) of the Ordinance.

Scenario 4: The DIS CF invests into two APIFs which invest further into approved index-tracking collective investment schemes (“ITCIS”) and/or APIF

Assumptions:

1. PFS of DIS CF = 0.30% p. a. of the CF’s NAV
2. APIF X invests 60% into APIF Z and 40% into ITCIS 1
3. APIF Y invests solely into ITCIS 2
4. APIF Z, ITCIS 1 and ITCIS 2 make direct investments
5. For APIF X, A = 0.20% p. a. of APIF X’s NAV, B = 60%
6. For APIF Y, A = 0.10% p. a. of APIF Y’s NAV, B = 40%
7. For APIF Z, A = 0.20% p. a. of APIF Z’s NAV, B = 60% x 60%
8. For ITCIS 1, A = 0.30% p. a. of ITCIS 1’s NAV, B = 60% x 40%
9. For ITCIS 2, A = 0.30% p. a. of ITCIS 2’s NAV, B = 40% x 100%



Step 1: Calculate the total PFS at CF level and the total proportionate UIFF at underlying investment fund levels:

- (a) Total amount of all PFS at CF level = 0.30%
- (b) Total amount of all proportionate UIFF (A x B) = [(0.20% x 60%) + (0.10% x 40%)] + [(0.20% x 60% x 60%) + (0.30% x 60% x 40%) + (0.30% x 40% x 100%)]
= 0.424%

Step 2: Calculate the Aggregate PFS for the DIS CF:

$$\text{Aggregate PFS} = (a) + (b) = 0.30\% + 0.424\% = 0.724\%$$

Step 3: Compare daily Aggregate PFS with the daily rate specified in section 1 of Schedule 11 to the Ordinance:

$$\frac{0.724\%}{N} < \frac{0.75\%}{N}$$

where N is the number of days in the year

Since the daily Aggregate PFS does not exceed the daily rate specified in section 1 of Schedule 11 to the Ordinance, it complies with section 34DD(4)(a) of the Ordinance.

DIS RE-INVESTMENT NOTICE
MANDATORY PROVIDENT FUND SCHEMES ORDINANCE

This DIS Re-investment Notice (“the Notice”) is important as it deals with how your Mandatory Provident Fund (“MPF”) benefits may be affected by the Default Investment Strategy as set out in the Mandatory Provident Fund Schemes Ordinance (“the Ordinance”). You should read it carefully, and in particular note the impact explained in paragraph 4 about what happens if no action is taken by you within 42 days. You are also reminded to consider it in conjunction with the [Offering Document]¹ of the MPF Scheme mentioned below.

This Notice is sent to you by us, the approved trustee of your MPF Scheme, in relation to your MPF account listed below, under sections 34DI and 34DJ of the Ordinance because:

- (a) as at 1 April 2017, all of the accrued benefits in your account listed below were invested according to the Default Investment Arrangement of the Scheme and have since remained so invested;**
- (b) we have not received any investment instructions from you to invest the accrued benefits in the account in constituent funds according to your selection as permitted under the governing rules; and**
- (c) you were under 60 years of age or became 60 years of age on 1 April 2017, or your birthday is unknown to us².**

Your MPF Account Details

Name of scheme member: [xxxxxx]

Account number of scheme member: [xxxxxx]

Date of birth (dd/mm/yyyy): [xxxxxx]³

Name of scheme: [xxxxxx] (“the Scheme”)

Name of approved trustee: [xxxxxx]

Default Investment Arrangement details: [Insert brief details about holdings, e.g. “All benefits in the account are held in units of the ABC Fund and the DEF Fund as of [xx-xx-2017]”⁴]

¹ Note for trustees: Substitute other terms as appropriate for the scheme in describing the offering document throughout the Notice.

² Note for trustees: Include only the relevant option.

³ Note for trustees: Insert “Unknown” if the date of birth is unknown.

⁴ Note for trustees: Insert table as necessary if current holdings are split between various prior default funds.

Why you are getting this Notice

1. Amendments to the Ordinance in 2016 provide for the establishment of a new investment arrangement called the Default Investment Strategy (“the DIS”) in all MPF schemes. In essence, the DIS has been designed as a standardized investment arrangement that applies to accrued benefits in accounts where the scheme member has not given any investment instructions.
2. Details of the DIS, including its automatic de-risking characteristics and fee controls, were sent to scheme members in the notice in [relevant months] setting out changes to the governing rules and [offering document] of the Scheme (“Amendment Notice”). If you do not have a copy of the Amendment Notice, a copy of it and the [offering document] is available on our website at [trustees’ website address] or [set out details about how the member could obtain another copy of the Amendment Notice].
3. Under the Ordinance, as the approved trustee of the Scheme, we must, by 3 October 2017 give you this Notice so that you can understand the impact of this change on your account.

The impact on your account

4. **If, by [yy-yy-2017], i.e. 42 days after the date of this Notice, we have not received any specific investment instructions from you for the accrued benefits in your account and all of the accrued benefits in your account continue to be invested according to the Default Investment Arrangement of the Scheme set out under “Your MPF Account Details” above, we must, by [zz-zz-2017], i.e. 14 days after [yy-yy-2017], invest those benefits according to the DIS.** We are required to invest those benefits according to the DIS and any investment instruction received by us after [yy-yy-2017] can only be carried out after the benefits have been first invested according to the DIS, providing that such investment instruction is still a valid instruction. There is potential investment gain or loss since the processes of investing according to the DIS will involve selling units from the existing Default Investment Arrangement fund(s) then purchasing units in the DIS funds at prevailing prices.
5. Further, if accrued benefits referred to in paragraph 4 are invested according to the DIS, this will also affect how future contributions or accrued benefits transferred from another scheme are invested. Contributions received or accrued benefits transferred from another scheme into the account after the date on which the accrued benefits

referred to in paragraph 4 are invested according to the DIS will also be invested according to the DIS unless we receive specific investment instructions from you to invest them in some other way. [You should note that special rules apply in some cases where benefits are transferred between accounts (e.g. between a contribution account and a personal account) within the 42-day period. If this applies to you, we will advise you accordingly.]⁵

6. [Note⁶] The accrued benefits in your account are partly/fully invested in a guaranteed fund. According to the Ordinance, we will not invest those benefits according to the DIS, if, on [yy-yy-2017] the market value of those benefits is less than the value guaranteed by the fund to be paid to you on that day. In that case, those benefits will stay in the guaranteed fund unless or until you give investment instructions to invest them in some other way.

What you need to do – your options

Option 1 – Take no action and be invested in DIS

7. You are not required to do anything, however, if you do not take any action, then as set out in paragraphs 4 and 5 above, the accrued benefits in your account will be automatically re-invested according to the DIS [except for that part invested in a guaranteed fund, if, on [yy-yy-2017] the market value of those benefits is less than the value guaranteed by the fund to be paid to you on that day⁷] and future contributions and transfers will also be invested according to the DIS⁸.

Option 2 – Stay invested in the existing constituent funds

8. If you want the accrued benefits in your account and/or⁹ future contributions and transfers to stay invested in the existing constituent funds, as set out under “Your MPF Account Details” above, then you need to complete and return the attached **Option 2 Form** to us by [yy-yy-2017]. This Form can be returned by post to the address indicated on the form [or by (insert return options, e.g. through our website, other electronic options), if relevant]. This Form can only be acted on by us if it is received by us by [yy-yy-2017]. Accordingly, if you are replying by post, please allow

⁵ Note for trustees: Sentence may be deleted if not applicable to scheme.

⁶ Note for trustees: Paragraph to be included only if relevant to scheme.

⁷ Note for trustees: Text to be included only if relevant to scheme.

⁸ Note for trustees: The words “and future contributions and transfers will also be invested according to the DIS” should be deleted in the rare case where a recipient of the Notice has already given specific investment instructions for such benefits.

⁹ Note for trustees: Whether this is “and” or “and/or” is subject to scheme rules. Select as appropriate and amend Option 2 Form accordingly.

adequate time and affix sufficient postage for postal delivery so that it will be received by us by [yy-yy-2017]. If you want to invest in the existing constituent funds after your accrued benefits and/or contributions and transfers have been invested according to the DIS, you are free to do so at any time by giving us an investment instruction.

9. You are reminded that if you want to re-invest the accrued benefits in your account into some other constituent funds, you are free to give us investment instructions to do so at any time, whether before or after [yy-yy-2017], by [set out brief details about how to do so]. Please note, however, as set out in paragraph 4 above, any investment instructions in relation to existing benefits received by us after [yy-yy-2017] can only be carried out after those benefits have been first invested according to the DIS.
10. As always, when making decisions about how to invest the accrued benefits in your MPF account, you should obtain the necessary information from the [offering document] of the Scheme and consider whether you need to obtain independent advice. Please note that the DIS does not provide any guarantee on the capital or return and investments in the DIS are subject to risks that are different from the risks of other investment strategies and constituent funds (including, for example, the impacts of the de-risking process and a different risk profile from the previous Default Investment Arrangement). These risks are set out more fully in the scheme [offering document] and in paragraph 4 above.
11. If you have any enquiries about what is set out in this Notice, please contact us by [set out details about how/where a member may make enquiries].

[date of Notice “xx-xx-2017”]

DIS Re-investment Notice**Option 2 Form**

Note: You only need to complete and send this Form to us if you wish to stay invested in the existing constituent funds, i.e. proceed with Option 2 as described in paragraph 8 of the DIS Re-investment Notice

To : [Name of approved trustee], [Name of scheme]
 Address : [Address of trustee]
 Email : xxxxx@trustee.com.hk
 Fax No. : xxxx xxxx

MPF Account Details

Name of scheme member: [xxxxx]
 Account number of scheme member: [xxxxxx]
 Date of birth (dd/mm/yyyy): [xxxxxx]
 Name of scheme: [xxxxxx] (“the Scheme”)
 Name of approved trustee: [xxxxxx]
 Default Investment Arrangement details: [Insert brief details about holdings, e.g. “All benefits in the account are held in units of the ABC Fund and the DEF Fund as of [xx-xx-2017]”]

[Note for Trustees: The above box repeats information from the 1st page of the Notice.]

I have read and understood the DIS Re-investment Notice dated [xx-xx-2017].

In respect of the existing accrued benefits in my account, the details of which are set out under “MPF Account Details” above, I hereby instruct you that these benefits are to stay invested in the existing constituent funds of the Default Investment Arrangement as set out above.

I note that this instruction also applies to future contributions and accrued benefits transferred from another scheme into the account. This instruction stays in force unless, or until, I make some other investment instructions in the manner set out in paragraph [9] of the DIS Re-investment Notice¹⁰.

 Signature of the Scheme Member

 Date

¹⁰ Note for trustees: Include Personal Information Collection Statement of the approved trustee in the Form.