PERIODIC REPORTING FOR RETAIL INVESTMENT FUNDS IN ASIA PACIFIC

An Investor's Perspective

CFA Institute

CFA Institute is the global association of investment professionals that sets the standard for professional excellence. We are a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community.

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Executive Summary

According to a global wealth report released by the Boston Consulting Group in May 2012, the Asia-Pacific region posted the biggest increase in millionaire households in 2011.[1] The report also highlighted that private wealth in the region (ex Japan) grew by 10.7% over the same period to US$23.7 trillion. This wealth creation has led to an increased demand for property investments, commodities (especially gold), traditional equities and fixed-income products, foreign exchange, and structured products. It has also led to a myriad of investment product offerings for the individual investor across Asia Pacific. This growing array of financial products has, at the same time, created a growing burden for investors as they decide how best to invest this new wealth.

Regulators in Asia Pacific have also kept pace with developments. They have commissioned studies and undertaken reforms to improve disclosures for financial products through product offering and sales documents by distributors and product manufacturers. Although much has been done in this area, the focus has been on information disclosure at the point of sale. But there are significant differences between pre- and post-sale disclosures that affect how investors monitor and evaluate the performance of their fund investments.

In light of these developments, in May 2012, CFA Institute initiated a study on existing regulations relating to disclosure and periodic reporting requirements for retail investment funds in six selected countries: Australia, China, Hong Kong, India, Japan, and Singapore. The aim of the study was to provide suggestions for improvements to periodic reports on the disclosure of relevant information regarding investment funds, particularly their performance. The project was completed with assistance and feedback from CFA societies in the six countries studied, along with comments received from those in the Philippines, Pakistan, New Zealand, and Sri Lanka (because the issues are similar throughout Asia Pacific). Five areas of disclosure are reviewed in this report:

- Frequency of disclosures
- Fund fees and charges
- Fund performance
- Fund holdings and asset allocation
- Conflicts of interest and management discussions

[1] Boston Consulting Group, "Global Wealth 2012: The Battle to Regain Strength" (May 2012).

Summary of Key Findings and Conclusion

Frequency of disclosures

At a minimum, collective investment schemes are required to produce for investors an annual report with detailed disclosure requirements. More jurisdictions now mandate semiannual reports, with Australia being a notable exception. Nonetheless, the trend seems to be moving to more regular reporting, such as quarterly and monthly reports.

The consensus from feedback on this issue is that annual reports should be audited and quarterly and monthly reports could contain less detail. Respondents noted that although more frequent reporting and disclosures would enhance transparency with respect to performance and management of funds, too-frequent reporting might lead to short-term investment strategies that are at odds with long-term investment objectives. At a minimum, there should be quarterly reporting of fund performance to investors.

Disclosure of fund fees and charges

The costs incurred by an investor in fund investments have a significant impact on returns over the long term. Adequate breakdowns and clear disclosures, which help the investor understand and compare fees and charges across funds, are important elements in decision making. Industry codes that promote best practices, such as the Asset Manager Code of Professional Conduct, require full and fair disclosure of management fees as well as other investment costs charged to investors.

In all the jurisdictions reviewed, all fees and charges are required to be itemised along with a total expense ratio (TER). Historical TERs are not required to be disclosed except in Singapore. Only four of the six jurisdictions require disclosure of transaction costs arising from asset trading.

All the respondents agreed that all fees and charges should be itemised and disclosed both in absolute amounts and in percentages. In addition, respondents believed TERs should be calculated and presented along with the itemised fees and charges. TERs that include standard items would enable fair and easy comparison among similar investment products. But TER calculations have to be harmonised for meaningful comparison within a jurisdiction and across borders. Some respondents requested the disclosure of historical fees and charges for a period of at least three years.

Disclosure of fund performance

The most pertinent disclosure for investors is the return on investment for the reporting period. There are various methods for calculating returns, and returns can be affected by the timing of cash flows and valuation methods, especially for illiquid assets. In the jurisdictions reviewed except for Australia, it is mandatory to disclose historical data on fund performance. Although not a requirement, periodic reports in Australia were found to include historical returns.

The responses revealed that in Asia Pacific, there is a lack of a consistent methodology for calculating returns. The comments stressed the need for the industry to prescribe a methodology to calculate total returns that is reasonable, comparable, and consistent. A global standard that is used by institutional investors for presenting past performance does exist. The Global Investment Performance Standards (GIPS®) require the use of time-weighted returns adjusted for external cash flows. The GIPS standards also require that firms use fair value principles in determining asset valuations because markets are not always liquid and that firms make their valuation policies available upon request.

Views about whether returns should be presented gross or net of fees or both were mixed. Another area in which there were inconsistencies was how historical performance should be presented. The respondents suggested that historical performance should be disclosed on both an annualised and a cumulative basis. The recommended periods were three months, six months, 1 year, 3 years, 5 years, 7 years, and 10 years since inception.

In comparison, the GIPS standards allow returns to be presented either gross or net of fees or both, but gross returns are preferred. Furthermore, the GIPS standards require 5 (growing to 10) years of annual performance to be disclosed and prohibit annualising returns of less than 12 months.

As for the use of benchmarks, it would be an effective indicator of performance only if the selected benchmark reflects the same investment style, has the same specific investment strategy, and fits the same investment objectives.

Disclosure of portfolio holdings and asset allocation

Transparency in portfolio holdings would highlight the investment strategy a fund manager adopts, including whether fund specifications are being complied with. It would also make it easier to observe the amount of illiquid assets in the portfolio and the level of overlap in an investor's overall portfolio. Almost all the jurisdictions reviewed require full disclosure of portfolio holdings semiannually. Australia does not currently have a requirement for portfolio holdings to be disclosed, but plans for introducing this requirement and for public consultation are being developed.

In the feedback received, respondents called for annual and possibly semiannual reports to include full details about the assets in the portfolio, along with sector and geographic allocations. The portfolio disclosures in other periodic reports do not need to be as detailed, and lag periods for the disclosure of individual portfolio holdings of two to three months were acceptable. Disclosure of the maturity date, duration, and credit rating would enhance disclosure of fixed-income securities in portfolios.

Disclosure of conflicts of interest and management discussions

Investors are increasingly seeking nonfinancial information in reviewing fund performance. High turnover of fund managers and key personnel and conflicts of interest that include dealings with brokers and investing in companies within the same corporate organisation are risks that potentially impact the performance of the fund.

All conflicts that have the potential to affect the fund manager's ability to act in the best interest of investors should be disclosed. These conflicts include soft commissions and rebates, related-party transactions, and relationships with brokers. All the jurisdictions in our review require that conflicts of interest be disclosed. But one area of disclosure that is noticeably lacking is the disclosure of details about the portfolio managers, such as their names and tenures at the fund.

Respondents suggested that all disclosures in the periodic reports as well as on the firm's website about conflicts of interest should include when the conflicts occurred. Furthermore, annual and semiannual reports should contain an operations and performance review, whereas quarterly and monthly reports should contain only a performance review and any material operational issues. Disclosure of details about the fund manager should be in only the annual report, and if any changes occur during the year, information should be updated on the website.

Conclusion

In conclusion, from the investor's perspective, periodic fund reporting can be further enhanced in the following ways.

Performance presentation can be enhanced by requiring a common standard for calculating returns, presenting current and past performance, and selecting appropriate benchmarks. Currently, most jurisdictions require a total expense ratio and detailed disclosure of cost components. The presentation can be further improved with historical expense ratios to compare trends in the costs of managing the fund along with examples based on a defined account size to better illustrate the cost impact for an investor. TER calculations need to be harmonised for meaningful comparisons within a jurisdiction and across borders.

In addition, there should be greater disclosure of policies adopted by funds that affect the information provided in their reports. These disclosures should include information about policies on valuing securities and portfolios (especially illiquid assets), calculating returns, managing conflicts of interest, and voting by proxy. These practices are already required by industry best practice codes, such as the Asset Manager Code of Professional Conduct.

Finally, there is a need to harmonise regulations related to periodic fund reporting. This change should include standardising the disclosures of fund performance, fund fees and charges, portfolio holdings, management information, and conflicts of interest. With increasing cross-border selling of retail funds, standardising disclosures will improve investors' ability to compare and assess more accurately the spectrum of funds available and to make more informed decisions.

Some challenges exist because the level of development and sophistication of the mutual fund industry varies significantly across Asia. In some markets, there are open competition and easy access to global products offered to investors. Some markets have stricter controls on allowing foreign-domiciled funds to be sold to local investors. In addition, there are capital controls that limit foreign currency products sold to local investors. As markets develop and wealth grows, the challenge is to find the right balance between investor protection and free markets that allows investors to search for higher yields and greater diversification.

1. Introduction

Economic growth and wealth creation in Asian countries over the past decade have been credited as being the catalysts of the increase in financial product offerings targeted at individual investors. The vast array of financial products ranges from traditional fixed-income and equity funds to index funds, hybrid funds, exchange-traded funds, real estate investment trusts, investment life insurance products, and other structured products. Furthermore, hundreds of new investment products are being developed and promoted every year. Given the breadth and depth of financial product offerings, how do retail investors select the investments that will best meet their financial objectives?

In the wake of the 2008 financial crisis, investors began asking for more up-to-date information on the status of their investment portfolios. Asian regulators have responded by continually revisiting existing regulations on disclosures, and in recent years, periodic reporting requirements have become a focus of financial reforms. Periodic reporting is a key element in efforts to improve the transparency of financial products, which are aimed at enhancing investor protection.

Retail investors usually depend on two principal sources of information when making an investment decision—impersonal sources (such as product advertisements and published financial and fund information) and interpersonal sources (such as family, friends, and investment advisers). Interestingly, research has shown that impersonal sources have a greater influence on the decision-making process.[2] This finding implies that investors would benefit from more frequent information that allows them to review the performance of their investments, make comparisons with other investment products, and undertake informed decisions regarding the investments in their portfolios. Additionally, market commentators would benefit because more up-to-date data would facilitate more robust analysis of investment products.

Furthermore, advances in information technology have significantly improved the timeliness of access to information. As a result, robust reporting has become a necessary component of sound investment decision making. Increased transparency of client reporting as well as more frequent communication regarding investment risks and returns will help investors distinguish between different investment product offerings and allow them to make more informed decisions. It has been suggested that such developments may motivate investment funds to act transparently, to improve performance and service, and to control investors' costs.

[2]N. Finch, "The Trouble with MER: The Disclosure of Fees and Charges in Australian Superannuation and Investment Funds," *Journal of Law and Financial Management*, vol. 4, no. 1 (June 2005):32–51.

1.1. Objective of Report

In May 2012, CFA Institute launched a study of existing regulations relating to disclosure and periodic reporting requirements for retail investment funds in six countries: Australia, China, Hong Kong, India, Japan, and Singapore. The purpose of this study was to obtain comments and suggestions from members and industry participants on existing regulatory requirements and practices with regard to periodic disclosures for investment funds targeted at retail investors and to improve these periodic reports for better disclosure of relevant information and performance of funds.

The five areas of disclosure that were identified for discussion in this report are

- frequency of disclosures,
- fund fees and charges,
- fund performance,
- fund holdings and asset allocation, and
- conflicts of interest and management discussions.

The consultation paper, which is posted on the CFA Institute website, was developed with assistance and feedback from CFA societies in the six countries. Feedback on the consultation paper was received from respondents in Australia, China, India, Japan, New Zealand, Pakistan, the Philippines, and Sri Lanka.[3] Conference calls were also held with leaders from CFA societies to gather responses and feedback. Although the questions offered were intended to guide the discussion, respondents were encouraged to suggest other areas in which disclosure could assist in elevating retail investors' understanding of their investments.

1.2. Scope of Report

In this report, retail investment funds refer to collective investment schemes that are not part of a superannuation or retirement plan. The reporting requirements for superannuation or retirement funds tend to be more onerous because of the nature and purpose of such investments, and those funds are usually under a separate set of regulations.

In this report, periodic reporting refers to disclosures that do not constitute a prospectus or sales document. The prospectus is a legal document that provides investors with material information about the fund that investors need before making an investment decision, whereas periodic disclosures are the primary conduit for the investment fund to communicate with investors post-sale. The content in periodic reports typically includes details of an investment fund's operations and performance for the period under review.

[3] A summary of the questions presented in the consultation paper is in Appendix 1.

1.3. Organisation of Report

The format in each of the following sections consists of an examination of the relevant issues with comparative tables. The comparative tables in each section are mainly based on regulatory requirements in the countries selected for this study (i.e., Australia, China, Hong Kong, India, Japan, and Singapore). The examination is followed by a summary of the responses received on the issues highlighted in the consultation paper.

2. Frequency of Disclosures

Current requirements generally specify reporting disclosures once a year at a minimum, although semiannual reports are becoming increasingly common. These reports are normally provided in written form, but the use of information technology, with up-to-date disclosures posted on a fund's website, provides more timely access that is more cost effective.

The breadth and depth of the content in each type of periodic report (annual, semiannual, quarterly, or monthly) differ on the basis of investors' needs. But Westpac New Zealand indicated in a report to the New Zealand Ministry of Economic Development that in Australia, higher levels of disclosure did not necessarily result in higher levels of retail investor understanding.[4] Instead, the Australian experience suggests that retail investors might have disengaged further because of the high volume of information that was potentially difficult to understand.

To ensure reliability of the information provided, the Organisation for Economic Co-Operation and Development (OECD) recommended that for collective investment schemes, at least one report a year must include financial statements certified by an independent auditor.[5]

Exhibit 1 shows the required frequency of reporting in the countries studied.

Exhibit 1. Frequency of Periodic Reporting

Frequency	Australia	China	Hong Kong	India	Japan	Singapore
Annually	✓[a]	✓	✓	✓	✓	✓
Semiannually		✓	✓	✓	✓	✓
Quarterly		✓			✓	
Monthly		✓		✓	✓	

[a]At least one periodic statement a year is required.

All investment funds in the jurisdictions reviewed are required to provide an audited annual report that highlights the funds' operations and performance. Most countries have increased this reporting requirement to at least twice a year. Only China, India, and Japan have more frequent reporting requirements.

[4]Westpac New Zealand's submission to the Ministry of Economic Development on "Periodic Reporting Regulations for Retail KiwiSaver Schemes—Discussion Paper," 18 March 2011.
[5]Organisation for Economic Co-Operation and Development, "White Paper on Governance of Collective Investment Schemes," *Financial Market Trends*, no. 88 (March 2005):137–167.

Q1 *What would be the appropriate frequency for periodic disclosures? What are the pros and cons for more frequent disclosures?*

The respondents agreed that, at a minimum, reporting should be annual and should contain more details regarding the financial statements, operations, and performance of the fund. Some of the respondents were partial toward semiannual reporting, but the responses regarding quarterly and monthly reporting were mixed. All respondents agreed that the information in the periodic reports, with the exception of the annual report, could be less detailed.

Respondents acknowledged that more frequent disclosures are desirable and would enhance transparency with respect to the management and performance of a fund. Investors would have more up-to-date information and would thus be better informed. Financial service providers would also be able to analyse the updates to better advise their clients.

The respondents from India and Pakistan, however, remarked that frequent reporting could also lead investors to focus on short-term performance and thereby force the fund managers to look at short-term asset allocations rather than build more robust long-term portfolios. Investors could also be overwhelmed with too much information that they neither understand nor use.

Some respondents also noted that more reporting could add to the operational costs, which would then be passed back to the investors. Nonetheless, with technology, internet-based dissemination of these reports is more cost effective than conventional printed copies.

Q2 *Should semiannual and quarterly reports be audited?*

All the respondents agreed that annual reports should be audited. But the responses about whether semiannual and quarterly reports should be audited were mixed. Increasing the frequency of audits not only would increase the operational costs but also could delay the dissemination of the information, thereby making it less relevant. Although audited reports would instil greater investor confidence in the data presented, the added costs and untimeliness of reporting might not justify such a measure.

3. Fund Fees and Charges

Prior to investing, investors can usually find a comprehensive list of fees and expenses, except transaction costs, in the prospectus. The disclosure of fund expenses is usually in a ratio format, so investors can estimate the impact of expenses on fund performance. Subsequent to investing, investors are provided with information on funds' actual costs to assess whether such costs are reasonable.

In our study of the jurisdictions, fund fees and charges are classified in a variety of ways. An example of the classification is as follows:

- one-time costs associated with the buying or selling of the fund;
- costs of servicing investor-specific decisions, such as switching fees; or
- costs of investing in the fund, such as management fees, performance fees, and transaction costs.

Under the GIPS standards, fees and charges are classified as:

- administrative fees, which could include accounting fees, consulting fees, legal fees, performance measurement fees, and other related fees;
- investment management fees; and
- trading expenses, which can be direct (brokerage commissions and stamp duty) or indirect (bid–ask spread).

The average retail investor is not likely to be able to determine whether the fees charged are reasonable, how the fees compare with those of other funds, and whether the additional services offered really justify higher fees. Fees and charges ultimately affect the returns to investors. Hence, efforts should be taken to ensure full and transparent disclosures so that competitive pressures can moderate the level of fees and charges. **Exhibit 2** shows the level of fee disclosure in each country studied.

Exhibit 2. Disclosure of Fund Fees and Charges

Items Disclosed	Australia	China	Hong Kong	India	Japan	Singapore
Itemised fees and charges	✓	✓	✓	✓	✓	✓
Single-figure fee for comparison[a]	✓[b]	✓[b]	✓[b]	✓	✓[b]	✓[c]
Transaction costs	✓	✓	✓		✓	

[a]The figure is generally based on IOSCO's TER model.
[b]Firms are not required to show history of TER.
[c]Expense ratios are required for the period under review and the previous year.

Fees and charges are itemised in all the jurisdictions reviewed. Single-figure expense ratios are also provided for ease of comparison. But expense ratios for past years, which allow investors to determine whether costs have increased, are not disclosed with the current expense ratio. The determination of the expense ratios is generally based on the International Organization of Securities Commissions' (IOSCO) definition of a total expense ratio (TER), which is the ratio of the fund's total operating costs to its average net assets. The ratio is calculated once a year and includes all recurring and nonrecurring costs, except transaction costs of asset purchases and sales.

Transaction costs allow investors to assess the impact of asset-trading costs on their return on investment. They also allow investors to determine the style of the fund—active versus passive. Nonetheless, investors can determine whether the fund meets their investment preference on the basis of information about the nature of the fund disclosed in the prospectus. In some countries, proxies for the cost of trading assets, such as turnover ratio, are provided. For example, Singapore requires turnover ratios to be disclosed for the period under review and the previous year.

In India, there is a cap on the investment management fee as well as the total expense ratio. Similarly, in Pakistan, only fees that have been listed can be charged to investors (for example, the management fee, front-end load, and back-end load). Furthermore, there are only a few expenses that can be charged to the fund (for example, the auditor fee, the trustee fee, the regulator fee, any legal fees and charges, and any direct taxes on the fund).[6] Any other expenses have to be absorbed by the management company.

Q3 *Should fees and charges be itemised? If yes, should all fees and charges be disclosed or just selected ones? If selected, which fees and charges should be disclosed? Should the data be in absolute amounts or in percentages or both?*

Most respondents were in agreement that fees and charges should be itemised and disclosed both in absolute amounts and in percentages. The reason is that percentages allow for easier peer-to-peer comparison, whereas absolute amounts allow investors to understand the effects of economies of scale. Nonetheless, the respondents from China believed that only absolute amounts need to be disclosed because the ratios or percentages can be determined from the data presented.

In terms of presentation, some respondents suggested that fees and charges be separated into fees due to the management company (e.g., administration, investment, advisory, and performance) and fees due to third-party service providers (e.g., trustees, custodians, brokers, lawyers, and research analysts). Alternatively, itemisation of fees and charges could be based on materiality. For example, expense items that are more than 5% of total expenses would be itemised, whereas those that are less than 5% would be combined and shown as miscellaneous fees. Abnormal or one-off expense items should also be disclosed.

[6]The regulator fee would be for the Securities and Exchange Commission of Pakistan (SECP).

In the case of performance fees, respondents from New Zealand suggested including examples of the application of the performance fee by using a benchmark that reflects the investment strategy of the fund or a fee (in per cent) based on a standard size investment. The examples would help investors understand how performance fees are charged as well as assess the performance of the fund manager.

Q4 *Should fees and charges be disclosed as a single percentage figure that represents all costs? What are the likely costs and benefits of requiring a TER calculation? What types of costs should be included or should not be included in the calculation of the TER?*

A TER should be calculated and presented along with the itemisation of all fees and costs. A TER that covers standard items (which need to be defined) would enable fair and easy comparison between investment products. If the methodology is aligned with international standards, international comparisons would be possible.

Respondents from Australia stressed that a single TER percentage figure should be based on a "standard" calculation methodology and be auditable. All costs should be included in the TER because excluding any fees/costs would interfere with a fair comparison. The TER should be broken down into standard ongoing fees and abnormal fees. The New Zealand respondents' suggestions for what items should be included in the calculation of the TER were investment management fees, submanagers' fees, performance fees, consultant fees, member fees, and administrative and operating expenses. But transaction costs, interest, brokerage fees, and fees for servicing (for example, withdrawal and switching fees) should not be included. Categorising the TER into ongoing costs and fees for specific services would be helpful.

There was also a suggestion that a TER be calculated for a defined account size (for example, $100,000) to standardise comparisons, especially when tiered fees are involved. All in all, the consensus was that a best practice framework for fees and charges should be developed for the industry.

A respondent from Japan highlighted the need for special disclosure requirements for fund-of-funds products. Because of the fund structure, some of the disclosure issues discussed would present some challenges. For example, itemising the fees and charges, determining a synthetic TER that incorporates underlying costs, and disclosing portfolio holdings were some of the issues raised.

Q5 *Should transaction costs be disclosed? What would be the arguments for or against the disclosure of transaction costs? If transaction costs need to be disclosed, in what form should the disclosure be:*

- *numeric value?*
- *portfolio turnover ratio?*
- *trading expense ratio (i.e., total commissions incurred divided by the total assets)?*

In principle, transaction costs should be disclosed because they affect an investor's return. In practice, it might be difficult to obtain accurate transaction data. Nonetheless, such costs will be reflected in the investor's return and will thus provide an incentive for fund managers to minimise transaction costs.

The argument for disclosure of transaction costs is that it could be an indicator of the investment ability and investment style of the fund manager. A fund manager who churned less would have a lower cost. The effectiveness of a fund manager's ability to negotiate brokerage fees could also be ascertained from the disclosure of transaction costs.

The argument against the disclosure of transaction costs is that it is already accounted for in the calculation of returns. Furthermore, the trading frequency is different for different types of strategies. Hence, it would not be very useful to compare the transaction costs for different strategies. The disclosure of transaction costs could also be misleading in the case of lumpiness and lags related to structured deals and private equity transactions. Nonetheless, such disclosures could give some indication of how active a fund is and how much the activity is costing in terms of performance.

Respondents noted that disclosures should be in the form of a portfolio turnover ratio and a trading expense ratio. Ideally, transaction costs should be broken down into various categories (for example, brokerage and buy–sell spread), but that might not be possible. At a minimum, a total transaction cost figure should be reported.

Q6 *Should disclosure include historical fees and charges? How many years of historical disclosure would be recommended?*

The comments were mixed. Some agreed that historical fees and charges should be disclosed, whereas others said that only current data would be sufficient.

If historical disclosure was recommended, the respondents from India and Japan suggested a minimum reporting period of three years for all types of funds to enable investors to detect patterns and changes. Alternatively, the period of historical disclosure could be aligned with the period of historical performance disclosure. Nonetheless, the current practice is to disclose the fees and charges for the financial reporting period and the previous period for comparison purposes.

4. Fund Performance

Information about investment returns is used by investors for a number of purposes. The main ones are

- to evaluate the performance of a fund and the fund manager and
- to monitor the fund's progress toward fulfilling its financial objectives.

But it should be noted that any investment has two dimensions—risk and return. By itself, information on returns is not sufficient to make an investment decision. Investors need to use information about returns in conjunction with information about the risk of the investment. As a rule, higher expected returns are associated with higher risk.

Hence, the OECD recommended in its "White Paper on Governance of Collective Investment Schemes" that the kind and degree of risk that a fund would assume must also be explained. For example, the basic risks associated with an asset class and any further risks that the fund manager intends to assume as part of the investment style need to be specified. And such risks should be explained in language that the retail investor can understand.

The Global Investment Performance Standards (GIPS) require firms to disclose the presence, use, and extent of leverage, derivatives, and short positions if they are material, including a description of the frequency of use and characteristics of the instruments sufficient to identify risks. For composite funds, firms are required to disclose sufficient information to allow a current and prospective client to understand the relevant risks of the composite strategy. **Exhibit 3** shows the level of fund performance disclosure in the countries studied.

Exhibit 3. Disclosure of Fund Performance

	Australia	China	Hong Kong	India	Japan	Singapore
Return on investment	✓[a]	✓	✓	✓[b]	✓	✓
Historical data	[c]	✓[d]	✓[e]	✓	✓	✓[f]

[a]Returns are reported either gross or net of taxes.

[b]Returns are reported in terms of compound annual growth rates and absolute amounts.

[c]Although Section 1017D of the Corporations Act 2001 does not require disclosure of historical investment return data, such information can be found in the periodic statements.

[d]Comparative figures are required for the corresponding period and year.

[e]Disclosures include

- a comparative table covering the last 3 financial years and
- a performance record for the past 10 financial years that shows the highest issue price and lowest redemption price for each year.

[f]Performance of the scheme against the benchmark covering the following periods of time: three months, six months, 1 year, 3 years, 5 years, 10 years, and since inception.

In general, the return on investment for a fund is determined from the ratio of the initial value to the redeemable value at the end of the period, expressed as a percentage.

Returns may be calculated net or gross of fees and may be presented on a before-tax or after-tax basis. The performance of the fund can be measured through benchmarking. Benchmarking provides a means of evaluating the quality of the fund manager's decisions. Funds can be required to benchmark performance against the objectives of the fund or against other similar funds. In some jurisdictions, funds are required to benchmark against securities indices. But this method may not always be an accurate or valuable way of benchmarking performance because the securities indices may not correctly reflect the strategy of the fund.

Q7 *What are the key issues around the calculation of total returns for a fund? Is there a need to prescribe methodologies? If so, why? If not, why not?*

The key issues highlighted by respondents were the reliability of asset valuation and consistency in the methodology for calculating total return. For example, such issues as valuation (especially of illiquid assets); the use of bid, ask, or mid prices; accruals of dividends; the treatment of cash flows; and the use of time-weighted versus money-weighted methodologies could have an effect on the calculated returns and need to be standardised.

The comments from respondents stressed the need for the industry to prescribe a methodology to calculate total returns that is reasonable, comparable, and consistent. They noted that there is a global standard that is used by institutional investors for presenting past performance. The GIPS standards require the use of time-weighted returns adjusted for external cash flows. The GIPS standards also require that firms use fair value principles in determining asset valuations because markets are not always liquid and that firms make their valuation policies available upon request.

Q8 *Should returns be presented gross or net of fees or both?*

The views were mixed. The rationale for disclosing returns both gross and net of fees was that it illustrates the extent to which returns are eroded by fees. It would also allow for better comparability with other funds as well as increase the transparency of fund information.

Proponents for presenting returns net of fees, however, argued that this is information that the investor receives. They rationalised that it would facilitate comparison among funds because fees vary among funds. They also noted that returns net of fees should exclude entry and exit loads because different investors might pay different loads.

Q9 *Should returns be disclosed before or after tax?*

Income and capital gains generated from investment funds in Asia are generally taxed before dividends are distributed to investors. The tax rates and taxation rules vary across jurisdictions, and in China, there is currently a 20% withholding tax on dividends paid.

Respondents recommended disclosing returns before tax and after tax at the fund level. Some did suggest that disclosing after-tax returns at the investor level would benefit investors, but there are practical issues of scaled tax rates. Some funds disclose tax-equivalent yields based on an assumed individual tax rate for informational purposes.

Q10 *Would the disclosure of past performance provide value to investors? If so, why? If not, why not? If historical performance is to be presented,*

- *should it be on a cumulative or annualised basis?*
- *how many calendar years of historical performance would be recommended?*

Past performance, although not an indicator of future performance, would give investors a sense of how well a fund manager had performed over various periods of time—that is, an indication of the track record and competence of the fund manager. It would also provide signals to current and potential investors regarding the volatility of the fund. Disclosures of past performance would help investors compare funds with similar strategies.

Past performance should be disclosed on both an annualised and a cumulative basis. Historical performance annualised over three months, six months, 1 year, 3 years, 5 years, 7 years, and 10 years since inception should be shown. Cumulative performance versus a benchmark over those periods would be best presented in a graphical format.

Q11 *Would benchmarking be an effective indicator of performance? If so, why and what type of benchmark would provide a useful comparison? If not, why not?*

The respondents agreed that the effectiveness of benchmarks in measuring performance depends on the choice of an appropriate proxy. The right benchmark could be used to assess more than just the performance of the fund. Because investment strategies for different funds would not likely be the same, it would not be meaningful for the investor to simply compare the absolute returns of each fund. A better measure would be to compare a particular fund's performance with that of other comparable funds.

Hence, an effective benchmark should reflect the same investment style and specific investment strategy and fit the same investment objectives. A respondent from New Zealand acknowledged that the task of identifying a suitable benchmark might be challenging, especially if the fund is one that has adopted "exotic" strategies. And a respondent from China suggested that in the selection of an appropriate benchmark, it would be useful to consider the following factors:

- Components of the benchmark
- Weight of the components
- Rebalancing frequency

- Tracking error
- Availability of the benchmark

In addition, the benchmark chosen should be a total return benchmark. The reason is that comparing the total returns of a fund or portfolio with a price-only benchmark would be inherently incomparable.

Although benchmarks are important, some respondents mentioned that retail investors tend to look at absolute returns and compare them with fixed deposit rates as reference points.

5. Fund Holdings and Asset Allocation

Transparency in portfolio holdings allows investors to understand what the fund invests in and to assess the risks. It also allows the investor to gauge whether the fund's investments are consistent with its investment philosophy and style. **Exhibit 4** indicates the level of disclosure of fund holdings in the countries studied.

Exhibit 4. Disclosure of Fund Holdings and Asset Allocation

	Australia	China	Hong Kong	India	Japan	Singapore
Disclosure of portfolio holdings[a]		✓	✓[b]	✓[c]	✓	✓[d]

[a]Defined as full disclosure of portfolio holdings semiannually.

[b]Disclosures include

- quantity of each holding with description and market value by category,
- total cost of investment,
- value of each holding as a percentage of NAV, and
- statement of movements in portfolio holdings since the end of the preceding accounting period.

[c]In India, semiannual portfolio disclosures (to be disclosed within one month of the end of the half year) include such details as the following:

- Equities (listed or unlisted, quantity, market value, industry, and percentage of net assets)
- Portfolio turnover ratio
- Data on derivatives positions
- Average maturity of the portfolio for debt schemes and ratings of debt securities
- Details on foreign securities to be disclosed separately
- Separate portfolio format prescribed for closed-end debt schemes, which must be disclosed on a monthly basis
- Disclosure of the top 10 holdings of each scheme on a monthly basis (Data related to performance are also computed and disclosed. This disclosure is released around the 10th of the next month.)

[d]Disclosures include

- investments at market value and as a percentage of NAV by country, industry, asset class, and credit rating and
- top 10 holdings at market value and as a percentage of NAV for the current and preceding periods.

One major issue with the disclosure of portfolio holdings is the extent of disclosure. An option may be for providers to disclose all the assets of the fund or, alternatively, the top 25 or top 10 assets. When only the top portfolio holdings are disclosed, the composition of the fund in terms of asset class could also be disclosed. This disclosure would give investors the asset allocation in the portfolio. In China, fund managers usually disclose the top 20 holdings in the fund.

Another issue is the frequency of disclosure of portfolio holdings. In our review, all the countries with the exception of Australia require portfolio holdings to be disclosed twice a year.

Q12 *To what extent should portfolio holdings be disclosed?*

At one end of the spectrum, some respondents suggested that annual reports (and possibly semiannual reports) should include disclosures of the full portfolio, along with sector and geographic allocations. At the other end of the spectrum, respondents called for the disclosure of the top 10 holdings by size—that is, by net asset value (NAV). And in between, suggestions included listing holdings that represent 50% or 75% of the assets, the top 20 holdings by size, or the top 10 or 20 holdings in each of the major asset classes.

Although some suggested that holdings in subfunds should also be disclosed, it might be difficult to obtain such information for a fund of funds.

Sector and geographic allocations would be best presented in a graphical format. Classification of the holdings into their respective sectors should be standardised for accuracy and ease of comparison. One such classification system that could be used is the Global Industry Classification Standard (GICS).[7] Respondents suggested that using Level 2 of the GICS sector classification might be sufficient.

Unlike equities, fixed-income securities require more information than just the name of the issuer. Some suggested including information on maturity date, duration, and credit ratings and an adequate description of the fixed-income security.

Q13 *Should the disclosure of individual holdings in the portfolio be on a lagged basis? If yes, what is the recommended time frame?*

Disclosing details of individual holdings in the portfolio on a lagged basis would help to protect the intellectual property (i.e., investment strategies) of the fund manager. The uniqueness of the investment strategy would be a key differentiating factor for a fund. Nonetheless, too long of a lag period would reduce the relevance of such disclosures.

A number of respondents noted that for audited reports, there is a natural built-in lag period dictated by the time taken to conduct the audit. For unaudited reports, the suggested lag periods were two to three months. And for monthly reports, a respondent from Australia remarked that the lag period should not be more than two weeks.

[7]GICS is a standardised classification system for equities developed jointly by Morgan Stanley Capital International and Standard & Poor's. The GICS hierarchy has four levels and begins with 10 sectors followed by 24 industry groups, 67 industries, and 147 subindustries. Each stock that is classified has a coding at all four of these levels. The main goal of GICS is to allow all market participants to classify stocks by standardised industry definitions. GICS is used to make portfolio diversification and overall asset allocation decisions from within a common framework.

6. Other Disclosures

In addition to informing investors about the basic characteristics of the fund prior to the investment, the manager should, after the investment, provide information to investors regarding any material changes in the fund, such as changes in investment policy, investment restrictions, or investment manager, as well as significant pending lawsuits. Currently, periodic reports include a brief summary of the factors that influenced fund performance during the period under review. Some reports also include forward-looking statements regarding the fund. **Exhibit 5** shows which other relevant disclosures are required in the six countries.

Exhibit 5. Other Relevant Disclosures

Disclosure	Australia	China	Hong Kong	India	Japan	Singapore
Soft-dollar arrangements	✓		✓			✓
Related-party transactions		✓[a]	✓	✓		✓
Management discussion of changes that affected the investment	✓	✓		✓	✓	✓

[a]Firms must disclose no less than two years of data on related-party transactions.

All the countries in our review require that conflicts of interest be disclosed. But one area of disclosure that was noticeably lacking was the disclosure of the names and tenures of the portfolio managers. The rationale behind this disclosure is that turnover in the ranks of portfolio managers may signal stability issues in the organisation. The departure of a decision maker also brings into doubt the relevance of the performance track record.

Another area for disclosure is the management's commentary on the operations of the fund, particularly whether there were any significant changes in the fund over the period under review and the reasons for the changes. In our review, we found that with the exception of Hong Kong, it is a regulatory requirement to include management discussion in periodic reports.

Q14 *What types of conflicts of interest should be disclosed? How should these conflicts be disclosed?*

As an overall guide, all conflicts that have the potential to affect the fund manager's ability to act in the best interests of investors should be disclosed in the periodic reports, particularly in the annual and semiannual reports. Some respondents suggested that all conflicts of interest as outlined in the CFA Institute Standards of Practice Handbook and Asset Manager Code of Professional Conduct be noted, along with when the conflicts occurred, in the periodic statements until such time as the conflicts are no longer relevant to the short- or long-term performance of the fund.

Examples of key conflicts that respondents provided were related-party transactions, trade allocation, front running, and soft commissions. Disclosure should be published in the form of the manager's policies on such matters, and an annual statement should be published noting the extent to which the policies have been complied with.

Q15 *Should all periodic disclosures include a section on the management's discussion of the fund's operations and performance?*

Ideally, periodic reports should include a discussion of the fund's operations and performance. Nevertheless, respondents suggested that such discussions should not be mandatory in the interest of timely reporting, although any material matters during the period under review should be disclosed. For the purpose of practicality, they suggested that annual and semiannual reports should contain both an operations and a performance review, whereas quarterly and monthly reports should contain only a performance review unless any material operational matters exist.

As for the contents of the management review, respondents suggested including an overall market commentary, fund performance, and an investment outlook for the period under review. In addition, specific sectors or other factors that could enhance or deteriorate fund performance should also be discussed. In addition, there were suggestions to include fund liquidity; turnover of fund managers, directors, and key management staff; and disclosure of proxy-voting policies as well as information on voting actions taken by fund managers.

Q16 *Should periodic disclosures include details about the fund manager?*

A majority of respondents noted that it would be more appropriate to disclose details about the fund manager in the annual report. For the other reporting periods, disclosure would be necessary only if there were any material changes. Disclosing personnel data would help investors better understand the personalities of those responsible for running and maintaining the performance of the fund.

Some respondents suggested that disclosures should include all key personnel—for example, portfolio managers, research analysts, risk managers, compliance managers, investment committee members, and any other relevant decision makers. Details to include would be their names, educational backgrounds, past working experience, number of years in the financial industry, and start date of managing the fund.

Appendix 1

Summary of Questions

A. Frequency of Disclosures

Q1 What would be the appropriate frequency for periodic disclosures? What are the pros and cons for more frequent disclosures?

Q2 Should semiannual and quarterly reports be audited?

B. Fund Fees and Charges

Q3 Should fees and charges be itemised? If yes, should all fees and charges be disclosed or just selected ones? If selected, which fees and charges should be disclosed? Should the data be in absolute amounts or in percentages or both?

Q4 Should fees and charges be disclosed as a single percentage figure that represents all costs? What are the likely costs and benefits of requiring a TER calculation? What types of costs should be included or should not be included in the calculation of the TER?

Q5 Should transaction costs be disclosed? What would be the arguments for or against the disclosure of transaction costs? If transaction costs need to be disclosed, in what form should the disclosure be:

- numeric value?
- portfolio turnover ratio?
- trading expense ratio (i.e., total commissions incurred divided by the total assets)?

Q6 Should disclosure include historical fees and charges? How many years of historical disclosure would be recommended?

C. Fund Performance

Q7 What are the key issues around the calculation of total returns for a fund? Is there a need to prescribe methodologies? If so, why? If not, why not?

Q8 Should returns be presented gross or net of fees or both?

Q9 Should returns be disclosed before or after tax?

Q10 Would the disclosure of past performance provide value to investors? If so, why? If not, why not? If historical performance is to be presented,

- should it be on a cumulative or annualised basis?
- how many calendar years of historical performance would be recommended?

Q11 Would benchmarking be an effective indicator of performance? If so, why and what type of benchmark would provide a useful comparison? If not, why not?

D. Fund Holdings and Asset Allocation

Q12 To what extent should portfolio holdings be disclosed?

Q13 Should the disclosure of individual holdings in the portfolio be on a lagged basis? If yes, what is the recommended time frame?

E. Other Disclosures

Q14 What types of conflicts of interest should be disclosed? How should these conflicts be disclosed?

Q15 Should all periodic disclosures include a section on the management's discussion of the fund's operations and performance?

Q16 Should periodic disclosures include details about the fund manager?

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