

Content

Title :	Directions for Use by Securities Investment Trust Enterprises of Securities Investment Trust Funds for Trading of Securities-Related Products
Date :	2014.07.08
Legislative :	<ol style="list-style-type: none"><li>1. 12 points promulgated in full on 18 November 2004 per Public Announcement No. Financial-Supervisory-Securities-IV-0930005610 of the Financial Supervisory Commission, Executive Yuan</li><li>2. 11 points promulgated in full on 10 May 2005 per Public Announcement No. Financial-Supervisory-Securities-IV-0940002000 of the Financial Supervisory Commission, Executive Yuan</li><li>3. Points 2 to 8 amended and promulgated 22 January 2007 per Public Announcement No. Financial-Supervisory-Securities-IV-0950160701 of the Financial Supervisory Commission, Executive Yuan</li><li>4. 10 points amended in full and promulgated 18 February 2008 per Public Announcement No. Financial-Supervisory-Securities-IV-0970006673 of the Financial Supervisory Commission, Executive Yuan; effective immediately</li><li>5. Articles 2, 3, and 5 to 7 amended per 30 June 2011 Public Announcement No. Financial-Supervisory-Securities-SITC-1000016377 of the Financial Supervisory Commission, Executive Yuan; for immediate implementation</li><li>6. Full text of 10 points amended per 21 October 2013 Public Announcement No. Financial-Supervisory-Securities-SITC-1020042222 of the Financial Supervisory Commission; for immediate implementation</li><li>7. Full text of 10 points amended per 8 July 2014 Public Announcement No. Financial-Supervisory-Securities-SITC-1030023448 of the Financial Supervisory Commission; for immediate implementation</li></ol>
Content :	<p>Article 1</p> <p>These Directions are adopted pursuant to Article 9, paragraph 3 of the Regulations Governing Securities Investment Trust Funds ("the Fund Regulations").</p> <p>Article 2</p> <p>The following terms as used in these Directions are defined as follows:</p> <ol style="list-style-type: none"><li>1."Futures" or "options": Means securities-related futures contracts, options contracts, or futures options contracts that the Financial Supervisory Commission ("FSC") has announced, in accordance with Article 5 of the Futures Trading Act, may be accepted by futures commission merchants for brokerage trading, and to securities-related futures contracts, options contracts, or futures options contracts that may be traded, as approved by the FSC on a special case-by-case basis, in accordance with Article 9, paragraph 2 of the Fund Regulations.</li><li>2."Interest rate swap": Means an agreement with a trading counterparty for periodic cash settlements of the difference between an agreed level of interest and the actual levels of an interest rate benchmark at specified future intervals according to differing interest rate calculations, pursuant to the terms and conditions stipulated by the agreement.</li><li>3."Total (notional) value": In the context of equity option contracts, it means the total of the strike price multiplied by the contract multiplier or the contract unit; in the context of equity option contracts traded on the Taiwan Futures Exchange (TAIFEX), it means the total of the strike price multiplied by the theoretical hedge ratio (the delta) and multiplied</li></ol>

by the contract multiplier or the contract unit; in the context of interest rate option contracts and interest rate swap contracts, it means the total notional amount; and in the context of forward rate transactions (including non-deliverable forwards) and currency swap contracts, it means the total notional amount.

### Article 3

As required to hedge against risk or to increase investment efficiency, a securities investment trust enterprise (SITE) may utilize securities investment trust funds to engage in trading of securities-related products, in accordance with the following provisions:

1. A fund engaging, in the capacity of a trader, in the trading of securities-related products, shall take into consideration the fund's type, attributes, and the securities held by the fund, and shall limit the trading to the following:

A. futures or options derived from currencies, securities, interest rates, or indices;

B. interest rate swaps, or off-exchange trading in currency-derived, securities-derived, interest-rate derived, or index derived futures, options, or other financial instruments as approved by the FSC on a special case-by-case basis.

2. Whether an individual securities investment trust fund may engage in trading of securities-related products shall be as stipulated in the trust agreement of each securities investment trust fund. Securities investment trust enterprises shall appoint an individual possessing relevant trading knowledge or experience to be specifically in charge of determining and executing trading policy. The fund manager shall in addition receive six hours or more of pre-service and on-the-job training courses in legal and practice issues as they related to futures and options.

3. A SITE that utilizes securities investment trust funds to engage in trading of securities-related products shall, in its internal control system, prescribe control measures and accounting procedures for employment of the funds in the aforementioned trading, and have them approved by the board of directors. The same procedure shall apply to any amendments thereto.

4. The internal auditors of a SITE shall at definite intervals determine the suitability of the internal controls on trading of securities-related products and conduct monthly audits of the trading department's procedural compliance in its use of securities investment trust funds to engage in related trading, and prepare audit reports to be placed on file for possible inspection.

5. A SITE utilizing securities investment trust funds for trading of futures or options shall engage a futures commission merchant to execute the trading, provided that a futures commission merchant approved by the FSC shall be engaged for any trading on an overseas exchange of futures or options of which any underlying involves any Taiwan securities, securities portfolio, or stock price index. The enterprise shall also instruct a custodial institution to carry out matters in connection with clearance, settlement, or exercise.

6. A SITE may engage a qualified futures commission merchant with an interest in the enterprise or the custodial institution to undertake

futures or options trading on its behalf, provided that the commission paid to the futures commission merchant may not be higher than those paid to the average futures commission merchant.

7. When a SITE uses a securities investment trust fund to engage in trading of securities-related instruments such as interest rate swap trading by means of price negotiation on the over-the-counter market, the counterparty may not be an interested party of the SITE. Interest rate swaps furthermore shall be confined to plain vanilla swaps and basis swaps.

8. When a SITE uses a securities investment trust fund to engage in trading of securities-related instruments such as interest rate swap trading by means of price negotiation on the over-the-counter market, the counterparty shall be a financial institution with a credit rating satisfying any one of the following:

A. A long-term debt rating of at least BBB-, and a short-term debt rating of at least A-3 from Standard & Poor's Corp.

B. A long-term debt rating of at least Baa3, and a short-term debt rating of at least P-3 from Moody's Investors Service.

C. A long-term debt rating of at least BBB-, and a short-term debt rating of at least F3 from Fitch Ratings Ltd.

D. A long-term debt rating of at least twBBB-, and a short-term debt rating of at least twA-3 from Taiwan Ratings Corporation.

E. A long-term debt rating of at least BBB- (tw), and a short-term debt rating of at least F3 (tw) from Fitch Ratings Limited, Taiwan Branch.

#### Article 4

A SITE utilizing a domestically-investing securities investment trust fund may engage in trading of TAIFEX futures or options and New Taiwan dollar denominated futures trading contracts listed on a foreign futures exchange under a cooperation agreement entered into with the Taiwan Futures Exchange Corporation and approved by the FSC. A SITE utilizing a domestically-and-overseas-investing or overseas-investing securities investment trust fund may engage in futures or options trading on overseas exchanges. When a securities investment trust fund is used to engage in trading of securities-related products by means of price negotiation on the over-the-counter market, the counterparty may not be a financial institution of the mainland China area.

#### Article 5

A SITE utilizing a securities investment trust fund to engage in trading of securities-related products shall abide by the following trading ratios and related rules:

1. Method for calculating the trading of securities-related products conducted by a securities investment trust fund for hedging needs:

A. The total market value on any business day of open short positions that the fund holds in futures contracts plus the total (notional) value of put options purchased, call options written, and interest rate swaps may not exceed the total market value of corresponding securities that the fund holds.

B. The term "corresponding securities" in the preceding item means securities (or investment portfolios) having a high correlation to the price movement of the underlyings of the futures contracts, option contracts, or interest rate swap contracts.

2.Method for calculating the risk exposure of a securities investment trust fund engaging in the trading of securities-related products for purposes of increasing investment efficiency:

A.Except for leveraged ETFs and inverse ETFs, the sum total on any business day of a fund's holdings in the following categories may not exceed 40 percent of the fund's net asset value:

a.The total market value of open long positions in futures contracts plus the total (notional) value of call options purchased and put options written.

b.The net amount by which the total market value of open short positions in futures contracts plus the total (notional) value of put options purchased and call options written exceeds the total market value of corresponding securities that the fund holds.

c.The total (notional) value of interest rate swap contracts for purposes of increasing investment efficiency.

d.The total (notional) value of forward rate transactions (including non-deliverable forwards) and currency swap contracts for purposes of increasing investment efficiency.

B.For a leveraged ETF or inverse ETF, the sum total of all sub-items of the preceding item engaged in to meet the needs of the strategy of replicating the multiple or inverse multiple of the underlying index may not exceed 110 percent of the multiple or inverse multiple of the net asset value of the fund.

C.The total market values of open long and short positions in futures contracts for purposes of increasing investment efficiency under the preceding two items may be mutually netted in compliance with the following netting principles:

a.Futures or options that are derived from the same currencies, securities, interest rates, or indexes, and furthermore for which physical delivery is prohibited, may be netted.

b.Interest rate swaps, futures, or options that are derived from fixed-income securities prices or characterized by highly correlated interest rate movements, and furthermore for which physical delivery is prohibited, may be netted; provided also that in the case of trading by means of price negotiation on the over-the-counter market, the trading counterparty shall be the same.

D.When a securities investment trust simultaneously writes call options and writes put options derived from the same currencies, securities, interest rates, or indexes, the trades may not be netted.

3.The total amount invested by a securities investment trust fund each business day in securities issued by any one company plus the notional value of the call options purchased on that company's stocks and the put options written on that company's stocks and the total market value of open long positions in single-stock futures contracts of that company may not exceed 10 percent of the net asset value of the fund.

4.For a securities investment trust fund, the total premium amount in each business day for open call options may not exceed 5 percent of the net asset value of the fund; the total (notional) value in each business day for open put options purchased may not exceed 25 percent of the net asset value of the fund.

5.A SITE utilizing a leveraged ETF or inverse ETF to trade securities-related products need not be restricted by the preceding two subparagraphs if such trading is necessary to match the fund's investment strategy and mechanisms for controlling the investment and trading positions have furthermore been expressly set out in the securities investment trust agreement.

6.A securities investment trust fund that trades securities-related products for hedging needs shall specify in the trade analysis report the highly correlated securities (or investment portfolios) held by the fund, and shall prescribe in the internal control system the standard for measuring the foregoing high correlation and the measures for risk monitoring and management in trades involving the writing of call options.

7.In trading by a domestically-investing securities investment trust fund on any given business day of futures or options of which the underlyings are domestic securities, securities portfolios, or stock price indices, of the sum total of the total market value of open positions in futures contracts held plus the total (notional) value of options contracts held, the amount that is in the domestic futures market shall be greater than 200 percent of the amount that is in overseas futures markets, except that this requirement shall not apply in cases where deviation herefrom is due to settlement upon expiration of a domestic futures or options contract or contracts.

#### Article 6

A SITE shall observe the following procedures in utilizing securities investment trust funds to engage in trading of securities-related products:

1.Four steps shall be taken in trading: analysis of trades, decision-making, execution of trades, and post-trade evaluation. The content of each step shall be formulated by each SITE according to these Directions and implemented by resolution of the enterprise's board of directors.

2.The documentation required with respect to the four steps of analysis, decision-making, execution of trades, and post-trade evaluation, and the responsibilities of SITE employees in trading shall be as follows:

A.Trade analysis: The report on trading of securities-related products shall specify the reason for the trade, the projected price of the trade, the long (or short) direction and the content of contracts, and shall describe in detail the analytical foundation, basis, and recommendations. The author of the securities-related products trading report, the reviewing personnel, and the authorized executive officer are responsible for this step.

B.Trade decisions: The fund manager prepares a written trade decision based on the contents of the securities-related products trading report and submits it for execution. The content of the trade decision shall specify particulars such as trade prices, long (or short) directions, and the content and the quantity of contracts. The fund manager, the reviewing personnel, and the authorized executive officer are responsible for this step.

C.Trade execution: The trader executes trades based upon the contents of the trade decision and prepares a trade execution record. The content of the trade execution record shall specify particulars such as the actual transaction price, long (or short) direction, the content and the quantity

of contracts and any discrepancies between the trade decision and the trade execution record and reasons for those discrepancies. The trader, the reviewing personnel, and the authorized executive officer are responsible for this step.

D. Post-trade evaluation: securities-related products trading post-trade evaluation report. The fund manager, the reviewing personnel, and the authorized executive officer are responsible for this step.

#### Article 7

Securities investment trust enterprises shall issue a monthly public notice detailing the use of funds under their management in futures trading and, in the monthly, semi-annual, and annual reports prepared under Article 76 of the Fund Regulations, and shall disclose the particulars listed below. In addition to filing the monthly, semi-annual, and annual fund reports with the FSC, copies thereof shall also be sent to the TAIEX.

1. Quantity, contract content, guaranty amount, (notional) contract values, the unrealized profit or loss for all open long positions held by the fund.

2. The sum total of the following items held, for purposes of increasing investment efficiency, each business day by the fund, expressed as a ratio of the fund's net asset value:

A. Total market value of open long position futures contracts, plus the notional value of call options purchased and put options written.

B. Net amount by which the total market value of open short positions in futures contracts plus the total (notional) value of put options purchased and call options written exceeds the total market value of corresponding securities that the fund holds.

C. Total (notional) value of interest rate swap contracts for purposes of increasing investment efficiency.

D. Total (notional) value of forward rate transactions (including non-deliverable forwards) and currency swap contracts for purposes of increasing investment efficiency.

3. The total amount invested in securities issued by any one company, plus the total (notional) values of call options purchased and put options written on that company's stock and the total market value of open long positions in single-stock futures contracts of that company expressed as a ratio of the fund's net asset value.

4. The total market value of open short positions in futures contracts, plus the total (notional) value of put options purchased, call options written, and interest rate swap contracts, held by the fund for hedging purposes, expressed as a ratio of the fund's net asset value, and as a ratio of the total market value of the corresponding securities held by the fund.

5. The total value of the premium on open options purchased and options written as a ratio of the fund's net asset value.

6. In trading of futures or options of which the underlyings are domestic securities, securities portfolios, or stock price indices, of the sum total of the total market value of open positions in futures contracts held plus the total (notional) value of options contracts held, the ratio of the amount that is in the domestic futures market to the amount that is in overseas futures markets.

7. Data on the volume of trading of overseas futures and options that the fund engages in through overseas futures commission merchants.

Article 8

Securities investment trust enterprises shall each day report to the TAIEX the ratio of funds engaged in trading of securities-related products on the given day for the portfolio of each individual securities investment trust fund the enterprise manages.

Article 9

A SITE may not, in any advertising or any other business promotion activities, characterize a given securities investment trust fund as being "low risk" because it engages in hedge trading in securities-related products.

Article 10

The prospectus for a securities investment trust fund shall specify the risks involved in trading of securities-related products.

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Data Source : Financial Supervisory Commission Laws and Regulations Retrieving System