Crowe Horwath

Equalisation Accounting

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Introduction

Most hedge funds charge a performance or incentive fee at a percentage of the net gains from the investment performance made by the fund. **Equalisation** are the accounting methodology, designed to ensure that not only the investment manager is paid the correct performance or incentive fee, but also that the incentive fees are fairly allocated between each investor in the fund.

Equalisation Credit / Contingent Redemption

If an investor subscribes for Participating Shares of any Class at a time when the Net Asset Value per Participating Share of such Class is other than the Peak Net Asset Value (commonly referred to as the "**High Water Mark**") per Participating Share of such Class, certain adjustments will be made to reduce any unfairness that could otherwise result to such Shareholder or to the Manager.

(i) If Participating Shares of any Class are subscribed where the Net Asset Value per Participating Share of such Class is less than the High Water Mark per Participating Share of such Class (a "**Contingent Redemption**"), the Shareholder will be required to pay a Performance Fee with respect to any subsequent appreciation in the Net Asset Value of those Participating Shares of such Class. With respect to any appreciation in the Net Asset Value per Participating Share of such Class at the date of subscription up to the High Water Mark per Participating Share of such Class, the Performance Fee will be charged at the end of each Performance Period by redeeming such number of the Shareholder's Participating Shares of such Class as having an aggregate Net Asset Value (after accrual for any Performance Fee) equal to the **Relevant Percentage** of any such appreciation applicable to such Class (a "Performance Fee Redemption"). The aggregate Net Asset Value of the Participating Shares of such Class so redeemed will be paid to the Manager as a Performance Fee. Performance Fee Redemptions ensure that the Fund maintains a uniform Net Asset Value per Participating Share in the same Class. As regards the Shareholder's remaining Participating Shares of such Class, any appreciation in the Net Asset Value per Participating Share of such Class above the High Water Mark per Participating Share of such Class will be charged a Performance Fee in the normal manner. In the event that a Shareholder redeems Participating Shares of such Class midway through a Performance Period and an adjustment is required to such Participating Shares, such adjustment shall be deducted from the redemption proceeds and shall be paid to the Manager.

(ii) If Participating Shares of any Class are subscribed where the Net Asset Value per Participating Share of such Class is greater than the High Water Mark per Participating Share of such Class, the Shareholder will be required to pay an amount in excess of the current Net Asset Value per Participating Share of such Class which is equal to the Relevant Percentage applicable to such Class, of the difference between the Net Asset Value per Participating Share of such Class (before accrual for the Performance Fee) and the High Water Mark per Participating Share of such Class (an "**Equalisation Credit**"). As at the date of subscription, the Equalisation Credit will equal the Performance Fee per Participating Share of such Class accrued with respect to the other Participating Shares in the same Class (the "**Maximum Equalisation Credit**"). The Equalisation Credit accounts for the fact that the Net Asset Value per Participating Share of such Class has been reduced to reflect an accrued Performance Fee to be borne by existing Shareholders and serves as a form of credit against a Performance Fee that might otherwise be payable by the Fund but that should not, in fairness, be charged against the holder of Participating Shares of such Class making the subscription (because, in relation to the new Participating Shares of such Class, no favourable performance has yet occurred). The Equalisation Credit mechanism seeks to ensure that all holders of Participating Shares in the same Class have the same amount of capital at risk per Participating Share of such Class.

Any additional amount invested as the Equalisation Credit will be at risk in the Fund and will therefore appreciate or depreciate based on the performance of the Participating Shares of any Class subsequent to the issue of the relevant Participating Shares of the same Class (but will never exceed the Maximum Equalisation Credit). In the event of a decline as at any Valuation Point in the Net Asset Value per Participating Share of any Class, the Equalisation Credit will also be reduced by an amount equal to the

Relevant Percentage applicable to such Class, of the difference between the Net Asset Value per Participating Share of such Class (before accrual for the Performance Fee) at the date of issue and as at that Valuation Point. Any subsequent appreciation in the Net Asset Value per Participating Share of any Class will result in the recapture of any reduction in the Equalisation Credit but only to the extent of the previously reduced Equalisation Credit up to the Maximum Equalisation Credit.

At the end of each Performance Period, if the Net Asset Value per Participating Share of any Class (before accrual for the Performance Fee) exceeds the High Water Mark per Participating Share of such Class, that portion of the Equalisation Credit equal to the Relevant Percentage applicable to such Class, of such excess amount, multiplied by the number of Participating Shares of the same Class subscribed for by the Shareholder, will be applied to subscribe for additional Participating Shares of the same Class for such Shareholder. Additional Participating Shares of such Class will continue to be so subscribed for at the end of each Performance Period until the Equalisation Credit, as it may have appreciated or depreciated in the Fund after the original subscription for Participating Shares of such Class was made, has been fully applied. If the holder of such Class of Participating Shares redeems its Participating Shares of such Class before the Equalisation Credit has been fully applied, the holder of such Class of Participating Shares will receive additional redemption proceeds being equal to the Equalisation Credit then remaining multiplied by a fraction, the numerator of which is the number of Participating Shares of such Class being redeemed and the denominator of which is the number of Participating Shares of such Class held by the holder of such Class of Participating Shares immediately prior to the redemption (in respect of which an Equalisation Credit was paid on subscription).

Illustration of Equalisation Accounting

Equalisation Credit and Contingent Redemption procedure can be illustrated as follows:

<u>Consider a Fund with the following criteria</u>:

Subscription Price+ @ 1st January:	$100 per share
Performance Period:	Yearly
Performance Fee Rate:	20%
NAV Frequency:	Monthly
GAV* as of 31 December:	$110 per share
NAV as of 31 December:	$108 per share

+Represent the High Water Mark of the Fund at the inception of the performance period.
*Defined as gross asset value before deducting performance fee.

There are four dealing days during the performance period as listed in Table 1 below. Table 2 illustrates the equalisation credit and contingent redemption adjustments on each investor's account based on the year-end NAV.

Table 1: Shareholder Dealing

Dealing Date	Transaction	Investor	Subscription Amount	Subscription Price (Based on GAV)	Shares Issued
1st January	Subscription	A	$100,000	$100	1,000.000
1st March	Subscription	B	$105,000	$105	1,000.000
1st June	Subscription	C	$120,000	$120	1,000.000
1st September	Subscription	D	$90,000	$90	1,000.000

Table 2 Summary of Shareholder Accounting

Investor	Shares	Year -End NAV	Performance Fee Payable	Equalisation Credit / (Contingent Redemption)	Crystallised Equalisation Credit / (Contingent Redemption)	Remaining Equalisation Credit / (Contingent Redemption)	Shares to Be Issued / (Redeemed)
A	1,000.000	$108	$2,000	Zero	Zero	Zero	Zero
B	1,000.000	$108	$2,000	$1,000	$1,000	Zero	9.259
C	1,000.000	$108	$0.00	$4,000	$2,000	$2,000	18.518
D	1,000.000	$108	$2,000	($2,000)	($2,000)	Zero	(18.518)

An explanation of each investor scenario is provided as below:-

<u>Investor A:</u>

No equalisation is applied as the Investor subscribed at the Fund's High Water Mark of $100.

<u>Investor B:</u>

Investor will be given an equalisation credit as the Investor subscribed at Gross NAV of $105 (i.e., higher than the High Water Mark of $100). The difference between $105 and $100 per share will give rise to an equalisation credit value of $1,000 (($105-$100) x 20% x No. of shares). After the performance fee of $2,000 ((Gross NAV of $110-High Water Mark of $100) x 20% x No. of shares) was crystallised at the end of the performance period (i.e., 31 December), Investor will receive additional 9.259 shares (equivalent to $1,000 based on the issue price of $108) at the end of the performance period.

<u>Investor C:</u>

Investor subscribed at $120 per share on entry. The price was inclusive of fee accrual of $4 per share (($120-$100) x 20%) being performance fee payable to the Manager for the positive performance over the past months. As such, Investor will be granted an equalisation credit of $4,000 (($120-$100) x 20% x No. of shares) as compensation that Investor did not participate in the past months' performance. As the GAV of $110 is lower than the subscription price of $120, an equalisation credit of $2 per share (($120-$110) x 20%) will be crystallised and thus Investor will receive additional 18.518 shares (equivalent to $2,000 based on the issue price of $108). The remaining equalisation credit value of $2 per share will be retained in the Fund until the next High Water Mark is achieved.

<u>Investor D:</u>

Investor enjoyed an increase in the value of investment of $20 per share (Gross NAV of $110-Subscription price of $90) and accordingly should pay the Manager a fee of 20% of this gain. However, as the NAV of the Fund as at year-end is $108, to ensure the Investor does not get a "free ride" between the subscription price of $90 and the Fund's High Water Mark of $100, Investor will compensate the Manager with the performance fee of $2,000 (($90-$100) x 20% x No. of shares) via Contingent Redemption procedure. Accordingly, an adjustment of 18.518 shares (equivalent to $2,000 based on the redemption price of $108) will be redeemed at the end of performance period.