

H&Q LIFE SCIENCES INVESTORS

STATEMENT OF ADDITIONAL INFORMATION

August 17, 2006

H&Q Life Sciences Investors (the “Trust”) is a diversified, closed-end, management investment company registered under the Investment Company Act of 1940, as amended (the “Investment Company Act”). The Trust’s investment objective is to seek long-term capital appreciation by investing primarily in equity and related securities (including securities subject to legal or contractual restrictions as to resale) of U.S. and foreign companies principally engaged in the development, production or distribution of products or services related to scientific advances in life sciences (including biotechnology, pharmaceuticals, diagnostics, managed healthcare and medical equipment, hospitals, healthcare and information technology and services, devices, supplies and other healthcare-related subsectors), agriculture and environmental management (“Life Sciences Companies”). The Trust will invest primarily in securities of U.S. and foreign companies that are believed by the Investment Adviser to have significant potential for above-average, long-term growth in revenues and earnings. The Trust emphasizes investment in securities of emerging growth Life Sciences Companies, some of which may offer limited products or services or which are at the research and development stage with no marketable or approved products or technologies. The securities of most emerging growth Life Sciences Companies in which the Trust will invest are expected to be traded in the over-the-counter market. The Trust may also invest up to 40% of its net assets in securities subject to legal or contractual restrictions as to resale (“Restricted Securities”), including venture capital investments. Such securities may be acquired in connection with venture capital opportunities, as well as in private placements of public companies. No assurance can be given that the Trust will achieve its investment objective. The Trust’s investment adviser is Hambrecht & Quist Capital Management, LLC (the “Investment Adviser”).

This Statement of Additional Information (“SAI”) is not a prospectus, but should be read in conjunction with the Prospectus for the Trust dated August 17, 2006 (the “Prospectus”). This SAI does not include all information that a prospective investor should consider before purchasing shares of beneficial interest (“Shares”) of the Trust, and investors should obtain and read the Prospectus prior to purchasing Shares. A copy of the Prospectus may be obtained without charge, by calling the Information Agent at (800) 870-0126. This SAI incorporates by reference the entire Prospectus.

The Prospectus and this SAI omit certain of the information contained in the Trust’s registration statement filed with the Securities and Exchange Commission (the “Commission”). Information about the Trust can be reviewed and copied at the Commission’s Public Reference Room in Washington, DC. Call (202) 942-8090 for information on the operation of the Public Reference Room. This information is also available in the Commission’s Internet site at <http://www.sec.gov>, and copies may be obtained upon payment of a duplicating fee by writing the Public Reference Section of the Commission, Washington, DC 20549-0102.

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ADDITIONAL INFORMATION ABOUT INVESTMENTS, INVESTMENT TECHNIQUES AND RISKS

Some of the different types of securities in which the Trust may invest, subject to its investment objective, policies and restrictions, are described in the Prospectus under “Investment Objective and Policies” and “Risk Factors.” Additional information concerning certain of the Trust’s investments, investment techniques and investment restrictions is set forth below.

The Trust may utilize the following investment practices:

Short Sales

In furtherance of its objective of capital appreciation, the Trust may effect short sales of any securities that it has the authority to purchase, subject to the limitation that the Trust will not effect a short sale if, as a result of such sale, the current market value of securities sold short would exceed 25% of the Trust’s net assets. Short sales are transactions in which the Trust sells a security it does not own in anticipation of an expected decline in the price of that security. In such a transaction, the Trust must borrow the security to make delivery to the buyer. The Trust is obligated to replace the borrowed security and may realize a gain if it purchases the security for replacement at a lower price. However, the price at which the Trust purchases the security may be more or less than the price at which the security was sold. The Trust will incur a loss as a result of a short sale if the cost of purchasing the borrowed security, and transaction and carrying costs associated with the short sale, are more than the amount realized from the short sale. Although the Trust’s potential for gain as a result of a short sale is limited to the price at which it sold the security short less the cost of borrowing the security, its potential for loss is theoretically unlimited because there is no limit to the cost of replacing the borrowed security.

If the Trust borrows a security in order to enter into a short sale, the proceeds of the short sale will be retained by a broker, as security for the borrowing to the extent necessary to meet margin requirements, until the short position is closed out. The Trust is also required to pay to the lender of the security the amount of any dividends or interest paid on the borrowed security. To borrow the security, the Trust also may be required to pay a premium, which would increase the cost of the security sold short. The amount of any gain will be decreased, and the amount of any loss increased, by the amount of any

premium or dividends or interest paid on the borrowed security that the Trust may be required to pay in connection with the short sale.

A short sale “against the box” is a transaction in which the Trust enters into a short sale of a security that the Trust owns or has the right to acquire at no additional cost. The proceeds of a short sale are held by a broker until the Trust delivers the security to close the short position, at which time the Trust will receive the net proceeds from the sale. A short sale “against the box” may be used to defer recognition for federal income tax purposes of any net gain or loss in the securities while the securities are subject to such a position. The diversification requirements applicable to the Trust to maintain its status as a regulated investment company under the federal income tax laws may limit the extent to which the Trust will be able to engage in short sales. See “Tax Matters.”

When the Trust engages in short sales other than “against the box,” the Trust will “cover” its position. For example, the Trust may cover by holding a call option on the security sold short having a strike price no higher than the price at which the security was sold or, the Trust may maintain in an account with its custodian a segregated amount of cash or U.S. Government Securities, high quality debt obligations or other liquid securities equal to the excess of (1) the market value of the securities sold short at the time they were sold short, over (2) any cash, U.S. Government Securities, high quality debt obligations or other liquid securities required by the broker to be deposited as collateral in connection with the short sale (not including the proceeds from the short sale). Until the borrowed security is replaced, the Trust will maintain this account at a level so that the amount deposited in the account, plus the collateral deposited with the broker, will equal the current market value of the securities sold short, but not less than the market value of the securities at the time they were sold short.

When-Issued and Delayed Delivery Transactions

The Trust may purchase securities on a “when issued” basis or a “delayed delivery” basis. “When-issued” securities are securities whose terms are available and for which a market exists, but which are not available for immediate delivery. “Delayed delivery” transactions are those in which the Trust purchases a security but settlement of the transaction is to occur after the customary settlement date. The Trust will enter into such transactions for the purpose of acquiring securities that it wishes to purchase but that are not currently available for purchase. The Trust may dispose of a commitment to purchase prior to settlement. However, the Trust does not intend to make such purchases for speculative purposes. When such transactions are negotiated, the purchase price is fixed at the time the commitment is made, but delivery and payment for the securities take place at a later date. During the period between commitment and settlement, no payment is made for the securities purchased, and no interest or dividends accrue to the Trust. However, the securities are subject to market fluctuation, and the value at settlement may be less than the purchase price. While awaiting settlement, the Trust will cover its position consistent with Commission guidelines. For example, the Trust could maintain with in segregated account cash, U.S. Government Securities, high quality debt obligations or other liquid securities having a value at least equal to its purchase commitments. The commitment to purchase a security for which payment will be made on a future date may be deemed a separate security and involves a risk of loss if the security declines prior to the settlement date, which risk is in addition to the risk of decline of the Trust’s other assets.

Repurchase Agreement

A repurchase agreement is an arrangement under which the Trust acquires a security subject to the obligation of the seller to repurchase and the Trust to resell such security at a fixed time and price (representing the Trust’s cost and interest). It is the Trust’s present intention to enter into repurchase agreements for a relatively short period (usually not more than one week) only with commercial banks

and registered broker-dealers and only with respect to U.S. Government Securities and money market instruments. The Repurchase agreements may also be viewed as loans made by the Trust, which are collateralized by the securities subject to repurchase. The Trust intends to take possession of collateral, and the Investment Adviser will monitor repurchase transactions to ensure that the value of the underlying securities will at all times be at least equal to the total amount of the repurchase obligation, including the interest factor. If the seller defaults the Trust could realize a loss on the sale of the underlying security to the extent that the proceeds of sale, including accrued interest, are less than the resale price provided in the agreement, including interest. In addition, if the seller should be involved in bankruptcy or insolvency proceedings, the Trust may incur delay and costs in selling the underlying security or may suffer a loss of principal and interest if the Trust is treated as an unsecured creditor and required to return the underlying collateral to the seller. The Trust may not enter into repurchase agreements with respect to more than 10% of its net assets.

Loans of Portfolio Securities

In an attempt to make productive use of its assets, the Trust may lend its portfolio securities, subject to the limitation that the Trust will not lend a security if, as a result of such loan, all securities then subject to loans would exceed 20% of the Trust's net assets. Under applicable regulatory requirements (which are subject to change), the loan collateral must, on each business day, be at least equal to the value of the loaned securities and must consist of cash, bank letters of credit or U.S. Government Securities. To be acceptable as collateral, letters of credit must obligate a bank to pay amounts demanded by the Trust if the demand meets the terms of the letter. Such terms and the issuing bank must be satisfactory to the Trust. When the Trust lends a security, it continues to be entitled to receive any dividends or interest on the loaned security and also receives one or more of: (i) a negotiated loan fee; (ii) interest on securities used as collateral for the loan; or (iii) interest on short-term debt securities purchased with the loan collateral. Either type of interest may be shared with the borrower of the security. The Trust may also pay reasonable finder's, custodian and administrative fees. The terms of the Trust's loans of securities must meet certain requirements under the Internal Revenue Code of 1986, as amended, such as providing that the Trust may terminate the loan upon no more than five days' notice, and must permit the Trust to reacquire loaned securities in time to vote on any important matter. The Trust will make such loans only to banks and dealers with which it may enter into repurchase agreements. If the borrower fails to return the loaned security, the Trust's risks include: (1) any costs in disposing of the collateral; (2) loss from a decline in value of the collateral to an amount less than 100% of the securities loaned; (3) being unable to exercise its voting or consent rights with respect to the security; (4) any loss arising from the Trust being unable to settle a sale of such securities in a timely manner; and (5) the inability of the Trust to reacquire the loaned securities.

Hedging

In order to hedge against changes in the value of its portfolio securities, the Trust may from time to time engage in certain hedging strategies. The Trust will engage in hedging activities from time to time in the Investment Adviser's discretion, and may not necessarily be engaging in such activities when movements in the securities markets, foreign exchange rates, or interest rates that could affect the value of the assets of the Trust occur. The Trust's ability to pursue certain of these strategies may be limited by applicable regulations of the Commodity Futures Trading Commission ("CFTC") and the federal income tax requirements applicable to regulated investment companies.

Although the Trust believes that use of such strategies will benefit the Trust, if the Investment Adviser's judgment about the general direction of securities market movements, foreign exchange rates or interest rates is incorrect the Trust's overall performance could be poorer than if it had not pursued those strategies. Moreover, changes in the value of the instruments that the Trust purchases to hedge its

portfolio securities may not correlate precisely with changes in the value of the portfolio securities the Trust is attempting to hedge. In addition, in situations where the Trust has insufficient cash, it may have to sell assets from its portfolio to meet margin requirements at a time when it may be disadvantageous to do so. The Trust's hedging activities may also result in a higher portfolio turnover rate and additional brokerage costs.

Options on Securities. The Trust may purchase and sell (or write) put or call options on any security in which it is permitted to invest or on any security the change in value of which has positive or negative correlation with the changes in value of the Trust's portfolio securities.

Purchasing Put and Call Options. By purchasing a call option on a security, the Trust will obtain the right to buy the securities underlying the option from its counterparty at a specified exercise price prior to or at the expiration of the option. The Trust might for example, purchase call options in anticipation of an increase in the price of the security. Conversely, when the Trust purchases a put option on a security it gives the Trust the right to sell the securities underlying the option to its counterparty at the exercise price prior to or at the expiration of the option. The Trust might for example, purchase put options in anticipation of a decline in the market value of securities in its portfolio (or which the Trust intends to or has the right to acquire).

In case of either put or call options that it has purchased, if the option expires without being sold or exercised, the Trust will experience a loss in the amount of the option premium plus any related commissions.

Writing Put and Call Options. When the Trust sells (writes) put and call options, it receives a premium as the writer of the option. By selling (writing) a call option, the Trust will obligate itself to sell the securities underlying the option to its counterparty at the specified exercise price prior to or at the expiration of the option if it is assigned an exercise notice. If the price of the underlying securities at expiration of the option is below the exercise price, the Trust will retain the full amount of the option premium. That amount, less the commission paid for the option, provides a partial hedge against any decline that may have occurred in the Trust's portfolio securities. During the term of the option, however, a covered call writer has, in return for the premium on the option, given up the opportunity for capital appreciation above the exercise price of the option if the value of the underlying securities increases, but has retained the risk of loss should the price of the underlying security decline. Conversely, by selling (writing) a put option, the Trust obligates itself to buy the securities underlying the option from its counterparty at the exercise price prior to or at the expiration if it is assigned an exercise notice. Writing a put option constitutes a partial hedge against increasing prices of securities the Trust intends to purchase. If the price of the securities at the expiration of the option is higher than the exercise price, the Trust will retain the full amount of the option premium which provides a partial hedge against any increase in the price of securities which the Trust intends to purchase. A secured put writer, however, retains the risk of loss should the market value of the underlying security decline below the exercise price of the option, less the premium received on the sale of the option.

Closing Purchase or Sale Transactions. Prior to exercise or expiration, an option position can be terminated only by entering into a closing purchase or sale transaction. Closing purchase transactions are ordinarily effected to realize a profit on an outstanding call option, to prevent an underlying security from being called, to permit the sale of an underlying security or to enable another call option on the underlying security (with either a different exercise price or expiration date or both) to be written. If the Trust is not able to enter into a closing transaction or an offsetting position, it will be required to maintain the securities subject to the call, or the collateral underlying the put, even though it might not be advantageous to do so, until a closing transaction can be entered into or the option is exercised or expires.

The Trust's ability to close out its position as a writer of an option is dependent upon the existence of a liquid secondary market. There is no assurance that a liquid market will exist, particularly in the case of OTC options, since OTC options will generally be closed out only by entering into a closing transaction with a dealer. In the case of OTC options, the Trust is also subject to the credit risk associated with its counterparties.

Stock Index Options. The Trust may purchase and sell (write) options on stock indices ("index options"). Index options are similar to options on securities except that, rather than taking or making delivery of securities underlying the option at a specified price upon exercise, an index option gives the holder the right to receive cash upon exercise of the option if the level of the stock index upon which the option is based is greater, in the case of a call, or less, in the case of a put, than the exercise price of the option.

The Trust will enter into transactions in index options for a number of reasons including, for example, to hedge against adverse price movements in the stock market generally or in particular market segments. If the Investment Adviser anticipates a general market decline, the Trust could purchase a stock index put option. If the expected market decline materialized, the resulting decrease in the value of the Trust's portfolio securities would be offset to the extent of the increase in the value of the put option. If the Investment Adviser anticipates a market rise, the Trust may purchase a stock index call option to enable the Trust to participate in the rise until the Trust completes anticipated purchases of securities. Purchasing and selling stock index options may also enable the Investment Adviser to achieve changes in equity positions more efficiently. Stock index options involve risks similar to those associated with options on securities. Because exercises of stock index options are settled in cash, however, call writers such as the Trust cannot provide in advance for their potential settlement obligations by acquiring and holding the underlying securities.

Futures Contracts and Options on Futures Contracts

Futures Contracts. The Trust may enter into contracts for the purchase or sale for future delivery (a "futures contract") of baskets of securities, financial indices, financial instruments or foreign currencies. The Trust would purchase or sell futures contracts to attempt to protect the value of its securities from market-wide price movements and fluctuations in interest or foreign exchange rates without actually buying or selling securities or foreign currency.

A "sale" of a futures contract (or a "short" futures position) means the assumption of a contractual obligation to deliver the securities or currency underlying the contract at a specified price at a specified future time. A "purchase" of a futures contract (or a "long" futures position) means the assumption of a contractual obligation to acquire the securities or currency underlying the contract at a specified price at a specified future time.

Options on Futures Contracts. Upon exercise of a call option, the Trust receives a long position in the underlying futures contract. As with the purchase of futures contracts, when the Trust is not fully invested it may purchase a call option on a futures contract to hedge against a market advance in which it would not otherwise participate. The purchase of a put option on a futures contract is similar in some respects to the purchase of protective put options on portfolio securities. Upon exercise of a put option, the Trust receives a short position in the underlying futures contract. For example, the Trust may purchase a put option on a futures contract to hedge the Trust's portfolio against the risk of declining securities values. The writing of a call option on a futures contract constitutes a partial hedge against declining prices of the components of the futures contract, whereas the writing of a put option on a futures contract constitutes a partial hedge against increasing prices of the financial instrument which is deliverable upon termination of the futures contracts. If the options expire unexercised, the Trust will retain the full amount

of the option premium, which provides a partial hedge against any increase in the price of securities which the Trust intends to purchase. If a put or call option the Trust has written is exercised, the Trust will incur a loss which will be reduced by the amount of the premium it receives.

Margin Requirements. At the time a futures contract is purchase or sold, the Trust must allocate cash or securities as a deposit payment (“initial margin”). It is expected that the initial margin on U.S. exchanges may range from approximately 3% to approximately 15% of the value of the securities or commodities underlying the contract. Under certain circumstances, however, such as periods of high volatility, the Trust may be required by an exchange to increase the level of its initial margin payment. Additionally, initial margin requirements may be increased generally in the future by regulatory action. An outstanding futures contract is valued daily and the payment in cash of “variation margin” may be required, a process known as “mark to the market”.

Regulatory Limitations on the Use of Futures Contracts and Options on Futures Contracts. Regulations of the CFTC applicable to the Trust currently require that all of the Trust’s futures and options on futures transactions constitute bona fide hedging transactions or be undertaken incidental to the Trust’s activities in the securities markets. In accordance with CFTC regulations, the Trust may not purchase or sell futures contracts or options thereon if immediately thereafter the sum of the amounts of initial margin deposits on the Trust’s existing futures and options on futures positions and premiums paid for options on futures would exceed 5% of the fair market value of the Trust’s total assets. The Investment Adviser reserves the right to comply with such different standard as may be established by CFTC rules and regulations with respect to the purchase or sale of futures contracts or options thereon.

Considerations Concerning Futures Contracts and Options on Futures Contracts. Futures contracts entail special risks. The ordinary spreads between values in the cash and futures markets, due to differences in the character of these markets, are subject to distortions relating to (1) investor’s obligations to meet additional variation margin requirements, (2) decisions to make or take delivery, rather than entering into offsetting transactions and (3) the difference between margin requirements in the securities markets and margin deposit requirements in the futures markets. The possibility of such distortion means that a correct forecast of general market, foreign exchange rate or interest rate trends by the Investment Adviser may still not result in a successful transaction. The Trust’s ability to establish and close out positions in futures contracts and options on futures contracts will be subject to the development and maintenance of a liquid market. Although the Trust generally will purchase or sell only those futures contracts and options thereon for which there appears to be a liquid market, there is no assurance that a liquid market on an exchange will exist for any particular futures contract or option thereon at any particular time. Under certain circumstances, exchanges may establish daily limits in the amount that the price of a futures contract or related options contract may vary either up or down from the previous day’s settlement price. Once the daily limit has been reached in a particular contract, no trades may be made that day at a price beyond that limit.

Exchange Rate Risk

The Trust may enter into forward foreign currency exchange contracts (“forward contracts”) and may purchase and sell (or write) exchange-traded or OTC options on currencies, foreign currency futures contracts and options on foreign currency futures contracts to protect against a decline in the U.S. Dollar equivalent value of its foreign currency portfolio securities or the payments thereon that may result from an adverse change in foreign currency exchange rates. The accurate projection of short-term currency market movements is extremely difficult, and the successful execution of a short-term hedging strategy is highly uncertain.

Forward Contracts. A forward contract obligates one party to purchase and the other party to sell a definite amount of a given foreign currency at some specified future date. In some circumstances the purchase or sale of appropriate forward contracts may help offset declines in the U.S. Dollar equivalent value of the Trust's foreign currency denominated assets and income available for distribution to the Trust's shareholders that result from adverse changes in the exchange rate between the U.S. Dollar and the various foreign currencies in which the Trust's assets or income may be denominated. The U.S. Dollar equivalent value of the principal of and rate of return on foreign currency denominated securities will decline if the exchange rate of the U.S. Dollar rises in relation to that currency. Such declines could be partially or completely offset by an increase in the value of a forward contract on that foreign currency.

While the use of foreign currency forward contracts may protect the Trust against declines in the U.S. Dollar equivalent value of its assets, their use will reduce the possible gain from advantageous changes in the value of the U.S. Dollar against particular currencies in which their assets are denominated. Moreover, the use of foreign currency forward contracts will not eliminate fluctuations in the underlying U.S. Dollar equivalent value of the prices of or rates of return on the assets held in the portfolio and the use of such techniques will subject the Trust to certain risks.

The foreign exchange markets can be highly volatile, subject to sharp price fluctuations. In addition, trading forward contracts can involve a degree of leverage. As a result, relatively small movements in the rates of exchange between the currencies underlying a contract could result in immediate and substantial losses to the Trust. Trading losses that are not offset by corresponding gains in assets being hedged could sharply reduce the value of the Trust's portfolio.

Options on Foreign Currencies. Similarly, the Trust may purchase and sell (or write) put and call options on foreign currencies to protect against a decline in the U.S. Dollar equivalent value of its portfolio securities or payments due thereon or a rise in the U.S. Dollar equivalent cost of securities that it intends to purchase. A foreign currency put option grants the holder the right, but not the obligation, at a future date to sell a specified amount of a foreign currency to its counterparty at a predetermined price. Conversely, a foreign currency call option grants the holder the right, but not the obligation, to purchase at a future date a specified amount of a foreign currency at a predetermined price. Where currency exchange rates do not move in the direction or to the extent anticipated, however, the Trust could sustain losses on transactions in foreign currency options which would require it to forego a portion or all of the benefits of advantageous changes in such rates.

As with options on securities or futures contracts, the Trust may write options on foreign currencies in order to receive a premium that may wholly or partially offset any declines in the value of its portfolio securities denominated in foreign currencies. When the Trust writes options on foreign currencies, the Trust also may be required to forego all or a portion of the benefits that might otherwise have been obtained from favorable movements in exchange rates.

Futures Contracts and Options on Futures Contracts on Foreign Currencies. Buyers and sellers of foreign currency futures contracts are subject to the same risks that apply to the use of futures generally. In addition, there are risks associated with foreign currency futures contracts and their use as hedging devices similar to those associated with options on foreign currencies described above. Further, settlement of a foreign currency futures contract must occur within the country issuing the underlying currency. Thus, the Trust must accept or make delivery of the underlying foreign currency in accordance with any U.S. or foreign restrictions or regulations regarding the maintenance of foreign banking arrangements by U.S. residents and may be required to pay any fees, taxes or charges associated with such delivery that are assessed in the country of the underlying currency.

Options on foreign currency futures contracts may involve certain additional risks. Trading options on foreign currency futures contracts is relatively new. The ability to establish and close out positions in such options is subject to the maintenance of a liquid secondary market. To mitigate this problem, the Trust will not purchase or write options on foreign currency futures contracts unless and until, in the Investment Adviser's opinion, the market for such options has developed sufficiently that the risks in connection with such options are not greater than the risks in connection with transactions in the underlying foreign currency futures contracts. Compared to the purchase or sale of foreign currency futures contracts, the purchase of call or put options thereon involves less potential risk to the Trust because the maximum amount at risk is the premium paid for the option (plus transaction costs). However, there may be circumstances when the purchase of a call or put option on a foreign currency futures contract would result in a loss, such as when there is no movement in the price of the underlying currency or futures contract, whereas use of the underlying futures contract would not result in a loss.

Coverage Requirements

All options on securities, securities indices, other indices and foreign currencies written by the Trust are required to be covered. When the Trust writes a call option during the life of the option, the Trust may own or have the contractual right to acquire the securities or foreign currency subject to the option, or may maintain with the Trust's custodian in a segregated account cash, U.S. Government Securities, other appropriate high quality liquid debt obligations or other liquid securities in an amount at least equal to the market value of the securities or foreign currency underlying the option or may utilize any other instrument or transaction consistent with Commission guidelines. When the Trust writes a put option, the Trust may maintain with the Trust's custodian in a segregated account cash, U.S. Government Securities, other appropriate high quality debt obligations or other liquid securities in an amount at least equal to the exercise price of the option or may utilize any other instrument or transaction consistent with Commission guidelines.

All futures and forward currency contracts purchased or sold by the Trust are also required to be covered. When the Trust purchases a futures or forward currency contract, the Trust will maintain with the Trust's custodian in a segregated account an amount of cash, U.S. Government Securities, other appropriate high quality liquid debt obligations or other liquid securities so that the amount so segregated, plus the amount of initial and variation margin held in the account of its broker, if applicable, equals the market value of the futures or forward currency contract or may utilize any other instrument or transaction consistent with Commission guidelines.

When the Trust sells a futures or forward currency contract, during the life of the futures or forward currency contract, the Trust will own or have the contractual right to acquire the securities or foreign currency subject to the futures or forward currency contract, or will maintain with the Trust's custodian in a segregated account cash, U.S. Government Securities, other appropriate high quality liquid debt obligations or other liquid securities in an amount at least equal to the market value of the securities or foreign currency underlying the futures or forward currency contract or may utilize any other instrument or transaction consistent with Commission guidelines.

If the market value of the contract moves adversely to the Trust, or if the value of the securities in the segregated account declines, the Trust will be required to deposit additional cash or securities in the segregated account at a time when it may be disadvantageous to do so.

INVESTMENT RESTRICTIONS

The Trust has adopted certain fundamental restrictions, which, like its investment objective, may not be changed without the affirmative vote of the holders of a majority of the Trust's outstanding Shares. As used in this Statement of Additional Information, a "majority of the Trust's outstanding Shares" means the lesser of (i) 67% of the Shares represented at a meeting at which more than 50% of the outstanding Shares are represented or (ii) more than 50% of the outstanding Shares. The Trust may not:

1. With respect to 75% of its total assets, invest in securities of any one issuer if immediately after and as a result of such investment more than 5% of the total assets of the Trust, taken at market value, would be invested in the securities of such issuer, or purchase more than 10% of the outstanding voting securities of any one issuer. These restrictions do not apply to investments in U.S. Government Securities.
2. Purchase or sell physical commodities or physical commodities contracts.
3. Purchase or sell real estate; provided that the Trust may invest in securities secured by real estate or interests therein or issued by companies which invest in real estate or interests therein.
4. Underwrite securities of other issuers, except to the extent that, in connection with the disposition of its portfolio securities, the Trust may be deemed an underwriter under federal or state securities laws.
5. Issue senior securities or borrow amounts in excess of 10% of its net assets at the time of borrowing, and then only from banks (except in the case of reverse repurchase agreements) as a temporary measure for extraordinary or emergency purposes or for the repurchase of its securities. The Trust will not repurchase its securities during periods when it has outstanding borrowings in excess of 5% of its net assets. The Trust will not borrow for investment purposes.
6. Make loans of money, which for the purposes of this restriction does not include the purchase of debt obligations in which the Trust may invest consistent with its investment objective and policies. The Trust reserves the authority to enter into repurchase agreements and to make loans of its portfolio securities to qualified institutional investors, brokers, dealers, banks or other financial institutions, so long as the terms of the loans are not inconsistent with the requirements of the Investment Company Act. Such loans of portfolio securities may not exceed an aggregate amount of 20% of the Trust's net assets.
7. Purchase securities of other investment companies, if (a) more than 10% of its total assets would be invested in securities of other investment companies, (b) more than 5% of its total assets would be invested in the securities of any one investment company, or (c) the Trust would own more than 3% of any other investment company's securities.
8. Invest less than 25% of its net assets in securities of Life Sciences Companies in the healthcare industry, except that, during periods in which the Investment Adviser believes the healthcare industry is affected by adverse economic conditions, the Trust may temporarily have less than 25% of the value of its net assets so invested.

Except as otherwise noted, all percentage limitations set forth above apply immediately after a purchase and a subsequent change in the applicable percentage resulting from market fluctuations does not require elimination of any security from the portfolio. For purposes of the investment restriction that prohibits the Trust from purchasing more than 10% of the outstanding voting securities of any issuer indicated in item number 1 above, the Board of Trustees has determined that for purposes of that restriction, the Trust will consider outstanding voting securities of an issuer to include any security of the issuer that entitles the owner or holder to vote for the election of directors of the issuer (a "voting

security”) and any other outstanding security of the issuer that is exercisable for or convertible into a voting security within 60 days from the date of the calculation.

TRUSTEES AND OFFICERS

The Trust’s Declaration of Trust provides that the Trust will indemnify Trustees and officers and may indemnify employees and agents of the Trust against liabilities and expenses incurred in connection with claims or litigation in which they may be involved because of their offices with the Trust. However, nothing in the Declaration of Trust or the By-laws of the Trust protects or indemnifies a Trustee, officer, employee or agent against any liability to which he would otherwise be subject by reason of willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of his office.

The names of the Trustees and officers of the Trust, their addresses, age and principal occupations during the past five years, and, in the case of the Trustees, their positions with certain other organizations and publicly-held companies, are provided in the tables below. Trustees that are deemed “interested persons” (as that term is defined in Section 2(a)(19) of the Investment Company Act) of the Trust or the Investment Adviser are included in the table titled “Interested Trustees.” Trustees who are not interested persons as described above are referred to as “Independent Trustees”. The Trust and H&Q Healthcare Investors (“HQH”), another closed-end investment company advised by the Investment Adviser, are the only two portfolios in the Fund Complex.

Trustees

Name, Address (1) and age	Position(s) held with Trust, Term of Office (2) and Length of Time Served	Principal Occupation(s) During Past 5 Years and Other Directorships Held	Number of Portfolios in Trust complex Overseen by Trustee
Independent Trustees:			
Lawrence S. Lewin Age:68	Trustee (since 1992) and Chairman (since 2000)	Executive Consultant (since 1999) of The Lewin Group (healthcare public policy and management consulting), a subsidiary of Quintiles Transnational Corp.; Director (since 2003) of Medco Health Solutions, Inc.; Director (since 2001) of CardioNet, Inc.(mobile cardiac outpatient telemetry); Director (since 2005) of Care Fusion (provides solutions for patient care providers) and Director (since 1984) of Intermountain Healthcare (non-profit organization).	2
Robert P. Mack Age:70	Trustee (since 1992)	Orthopedic Surgeon at Orthopedic Associates of Aspen (since 2000).	2

Name, Address (1) and age	Position(s) held with Trust, Term of Office (2) and Length of Time Served	Principal Occupation(s) During Past 5 Years and Other Directorships Held	Number of Portfolios in Trust complex Overseen by Trustee
Eric Oddleifson Age:71	Trustee (since 1992)	Self-employed Consultant (since November 2005); Investment Committee Chair (from 2003-2005) and Partner (from 1997-2003) of GMO Renewable Resources LLC (timber investment management).	2
Oleg M. Pohotsky Age:59	Trustee (since 2000)	Self-employed Financial Consultant (since 2002). Senior Vice President (from 1991-2001) of FAC/Equities, a division of First Albany Corporation (investment bank).	2
Uwe E. Reinhardt, Ph.D. Age:68	Trustee (since 1992)	Professor of Economics (since 1968) at Princeton University; Director (since 2000) of Triad Hospitals, Inc.; Director of Boston Scientific (since 2002); Director of Amerigroup, Inc. (since 2002); Director of Duke University (since 2001); Director of The Duke University Health System (since 2001) and Director of the National Bureau of Economic Research (since 2002).	2
Lucinda Stebbins, CPA Age: 60	Trustee (since 2006)	Self-employed Financial Consultant (since 2004); Director of Deutsche Asset Management (2002-2004); Senior Vice President Scudder Investments (2000-2002).	2
Henri A. Termeer Age:60	Trustee (since 1992)	Chairman (since 1988), Chief Executive Officer (since 1985) and President (since 1983) of Genzyme Corporation (human healthcare products); Director (since 1987) of ABIOMED, Inc.; Director (1996-2002) of Diaqirl.	2

Interested Trustees:

Name, Address (1) and age	Position(s) held with Trust, Term of Office (2) and Length of Time Served	Principal Occupation(s) During Past 5 Years and Other Directorships Held	Number of Portfolios in Trust complex Overseen by Trustee
Daniel R. Omstead, Ph.D. (3) Age:53	President (since 2001); Trustee (since 2003)	President of HQH and HQL (since 2001); Trustee of HQH and HQL (since 2003); President, Chief Executive Officer and Managing Member of Hambrecht & Quist Capital Management LLC (since 2002); President and Chief Executive Officer (2001-2002) and Managing Director (2000-2002) of Hambrecht & Quist Capital Management, Inc.; Director (since 2003) of Concentric Medical, Inc.; President and Chief Executive Officer (from 1998-2000) of Repronogenesis, Inc. (biotech company).	2

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- (1) The address for each Trustee is c/o the Trust at the Trust’s address as set forth above.
 - (2) Each Trustee currently is serving a three year term.
 - (3) Trustee considered to be an “interested person” within the meaning of the Investment Company Act of 1940, as amended (the “1940 Act”) through position or affiliation with Hambrecht & Quist Capital Management, LLC, the Trust’s investment adviser. Trustee also serves as Executive Officer. Each Officer serves in such capacity for an indefinite period of time at the pleasure of the Trustees.

Executive Officers who are not Trustees

Name, Address (1) and age	Position(s) held with Trust, Term of Office (2) and Length of Time Served	Principal Occupation(s) During Past 5 Years and Other Directorships Held	Number of Portfolios in Trust complex Overseen by Trustee
Kathleen M. Eckert Age:39	Chief Compliance Officer (since 2004); Treasurer and Secretary (since 2005)	Chief Compliance Officer of Hambrecht & Quist Capital Management, LLC (since October 2004); Chief Compliance Officer (since October 2004), Treasurer and Secretary (since February 2005) of HQH and HQL (since October 2004); Senior Vice President of Ivy Mackenzie Services Corp. (mutual fund distributor and administrator), from June 2002 to January 2004. Chief Compliance Officer of Mackenzie Investment Management, Inc. from June 2002 to June 2003. Director of Fund Administration of Mackenzie Investment Management, Inc. from 1999 to June 2003.	2

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- (1) The address for each Executive Officer is c/o the Trust at the Trust’s address as set forth above.
 - (2) Each Officer serves in such capacity for an indefinite period of time at the pleasure of the Trustees.

Ownership of Securities

As of March 15, 2006, the Trust’s Trustees and executive officers, as a group, beneficially owned less than 1% of the Trust’s outstanding Shares. The information as to beneficial ownership of securities which appears below is based on statements furnished to the Trust by its Trustees and executive officers.

To the knowledge of the Trust, as of August 7, 2006, there were no control persons of the Trust and no persons were known to own, either beneficially or of record, 5% or more of the Shares of the Trust.

As of March 15, 2006, the dollar range of equity securities owned beneficially by each Trustee in the Trust and in any registered investment companies overseen by the Trustee within the same family of investment companies as the Trust is as follows:

Independent Trustees

Name of Director	Dollar Range of Equity Securities in the Trust	Aggregate Dollar Range of Equity Securities in all Registered Investment Companies Overseen by Trustee in Family of Investment Companies
Lawrence S. Lewin	\$10,0001-\$50,000	\$50,001-\$100,000
Robert P. Mack, M.D.	None	\$50,001-\$100,000
Eric Oddleifson	\$50,001-\$100,000	Over \$100,000
Oleg M. Pohotsky	None	None
Uwe E. Reinhardt, Ph.D.	\$1-\$10,000	\$10,001-\$50,000
Lucinda H. Stebbins, CPA	None	None
Henri A. Termeer	None	None

Interested Trustees

Name of Director	Dollar Range of Equity Securities in the Trust	Aggregate Dollar Range of Equity Securities in all Registered Investment Companies Overseen by Trustee in Family of Investment Companies
Daniel R. Omstead, Ph.D.	\$50,001-\$100,000	Over \$100,000

Dr. Omstead and Ms. Eckert serve as executive officers of the Trust. As of December 31, 2005, the executive officers of the Trust beneficially owned 3,999 Shares of the Trust, or less than 1% of the Shares outstanding on that date.

Standing Committees

Audit Committee. The Trust has an Audit Committee comprised solely of Trustees who are not “interested persons” (as that term is defined in Section 2(a)(19) of the Investment Company Act) of the Trust or the Investment Adviser and who are “independent” as defined in the New York Stock Exchange (“NYSE”) Listing Standards (each an “Independent Trustee”). The Trust’s Board of Trustees has adopted a written charter for the Audit Committee. The principal purpose of the Trust’s Audit Committee is to assist the Board of Trustees in fulfilling its responsibility to oversee the integrity of the Trust’s financial statements and the Trust’s compliance with legal and regulatory requirements to oversee management’s conduct of the Trust’s financial reporting process, including reviewing the financial reports and other financial information provided by the Trust, the Trust’s systems of internal accounting and financial controls and the annual independent audit process.

For the Trust, the Audit Committee’s role is one of oversight, and it is recognized that the Trust’s management is responsible for preparing the Trust’s financial statements and that the outside auditor is responsible for auditing those financial statements. Although the Audit Committee member must be financially literate and one member must have accounting or financial management expertise (as determined by the Board of Trustees in its business judgment), Audit Committee members are not professionally engaged in the practice of accounting or auditing and are not experts in the fields of accounting or auditing, including with respect to auditor independence. Audit Committee members rely,

without independent verification, on the information provided to them and on the representations made by management and the Trust's independent public accountants.

The members of the Trust's Audit Committee are Messrs. Oddleifson, Pohotsky, Reinhardt and Ms. Stebbins. Mr. Pohotsky is the Chairman of the Trust's Audit Committee. The Trust's Audit Committee held five meetings during the fiscal year ended September 30, 2005.

Governance Committee. The Trust has a Governance Committee comprised solely of Independent Trustees who are "independent" as defined in the NYSE Listing Standards. The Trust's Board of Trustees has adopted a written charter for the Governance Committee. The Trust's Governance Committee's mission under its charter is to review, evaluate, and enhance the effectiveness of the Trust's Board of Trustees in its role in governing the Trust and to oversee management of the Trust in accordance with the Corporate Governance Guidelines, which have been adopted by the Trust's Board of Trustees.

The Trust's Governance Committee shall review, discuss and make recommendations to the Board of Trustees relating to those issues that pertain to the effectiveness of the Board of Trustees in carrying out its responsibilities in governing each Trust and overseeing each Trust's management. The members of the Trust's Governance Committee are Messrs. Lewin, Termeer, Dr. Mack and Ms. Stebbins. Mr. Lewin is the Chairman of the Trust's Governance Committee. The Trust's Governance Committee met twice during the fiscal year ended September 30, 2005.

Nominating Committee. The Trust has a Nominating Committee comprised solely of Independent Trustees who are "independent" as defined in the NYSE Listing Standards. The Trust's Board of Trustees has adopted a written charter for the Nominating Committee. The Nominating Committee charter is not available on the Trust's website, but was included as Exhibit A to the Trust's Joint Proxy dated May 10, 2006.

The charter of the Nominating Committee provides that each prospective trustee candidate have a college degree or equivalent business experience, and that each candidate is not serving in a similar capacity on the board of a registered investment company which (i) is not sponsored or advised by the Trust's investment adviser or its affiliates and (ii) the Board in its discretion has determined to be competitive with the Fund taking into account such registered investment company's investment mandate. The Trust's Nominating Committee may also take into account other factors when considering and evaluating potential trustee candidates, including but not limited to: (i) availability and commitment to attend meetings and perform responsibilities of the Board; (ii) relevant industry and related experience; (iii) educational background; (iv) financial expertise; (v) the candidate's ability, judgment and expertise; and (vi) the overall diversity of the Board's composition.

The Trust's Nominating Committee may identify prospective trustees from any reasonable source, including, but not limited to, the consultation of third-party trustee search services. The Trust's Nominating Committee will consider potential trustee candidates recommended by shareholders, provided that the proposed candidates (i) satisfy any minimum qualifications of the Trust for its trustees; (ii) are not "interested persons" (as that term is defined in Section 2(a)(19) of the 1940 Act) of the Trust or the Investment Adviser; and (iii) are "independent" as defined in the NYSE Listing Standards. In order to be evaluated by the appropriate Committee, trustee candidates recommended by shareholders must also meet certain eligibility requirements as set out in the Committee's Charter. Other than those eligibility requirements, the Committee shall not evaluate shareholder trustee nominees in a different manner than other nominees. The standard of the Committee is to treat all equally qualified nominees in the same manner.

All shareholder recommended nominee submissions must be received by the Trust by the deadline for submission of any shareholder proposals which would be included in the Trust's proxy statement for the next annual meeting of the Trust. Each nominating shareholder or shareholder group must meet the requirements stated in the Nominating Committee Charter. A nominating shareholder or shareholder group may not submit more than one nominee per year. When nominating a trustee candidate, shareholders must include in their notice to the Trusts' Secretary: (i) the shareholder's contact information; (ii) the trustee candidate's contact information and the number of fund shares owned by the proposed candidate; (iii) all information regarding the candidate that would be required to be disclosed in solicitations of proxies for elections of trustees required by Regulation 14A of the Securities Act of 1934, as amended; and (iv) a notarized letter executed by the trustee candidate, stating his or her intention to serve as nominee and be named in the Trust's proxy statement, if nominated by the Board of Trustees, and to be named as a trustee if so elected. Once a nomination has been timely received in proper form, the nominee will be asked to complete an eligibility questionnaire to assist the Trust in assessing the nominee's qualifications as a potential Independent Trustees and as someone who is "independent" under the NYSE Listing Standards. The Nominating Committee will make such determinations in its sole discretion and such determinations shall be final.

The members of each Trust's Nominating Committee are Messrs. Lewin and Termeer and Dr. Mack. Mr. Lewin is the Chairman of each Trust's Nominating Committee. The Trust's Nominating Committee met one time during the fiscal year ended September 30, 2005.

Valuation Committee. The Board has delegated to the Trust's Valuation Committee general responsibility for determining, in accordance with the Trust's valuation procedures, the value of assets held by the Trust on any day on which the net asset value per share is determined. The Valuation Committee may appoint, and has appointed, a Sub-Committee made up of employees and officers of the Investment Adviser, to deal in the first instance with day to day valuation decisions, subject to oversight by the Valuation Committee. The Valuation Committee shall meet as often as necessary to ensure that each action taken by the Sub-Committee is reviewed within approximately a calendar quarter of the occurrence. In connection with its review, the Valuation Committee shall ratify or revise the pricing methodologies authorized by the Sub-Committee since the last meeting of the Valuation Committee. The Valuation Committee is charged with the responsibility of determining the fair value of the Trust's securities or other assets in situations set forth in the Trust's valuation procedures.

The members of the Trust's Valuation Committee are Messrs. Oddleifson and Pohotsky and Dr. Mack. The Trust's Valuation Committee held four meetings during the fiscal year ended September 30, 2005.

Qualified Legal Compliance Committee. The Trust has a Qualified Legal Compliance Committee ("QLCC") comprised solely of Independent Trustees. The Trust's Board of Trustees has adopted a written charter for the QLCC. The principal purpose of the Trust's QLCC is to review and respond to reports of Evidence of a Material Violation (as defined in the QLCC charter). Reporting Evidence of a Material Violation is required under the Standards of Professional Conduct for Attorneys adopted by the Commission under the Sarbanes-Oxley Act of 2002 (the "Standards"). Under the Standards, if an attorney appearing and practicing before the Commission in the representation of an issuer, such as the Trust, becomes aware of Evidence of a Material Violation by the issuer or by any officer, trustee, employee or agent of the issuer, the Standards provide for the attorney to report such evidence to the issuer's QLCC forthwith. In discharging its role, the QLCC is granted the power to investigate any Evidence of a Material Violation brought to its attention with full access to all books, records, facilities and personnel of the Trust and the power to retain outside counsel, auditors or other experts for this purpose.

The members of the Trust's QLCC are Messrs. Lewin, Oddleifson and Pohotsky. Mr. Pohotsky is the Chairman of the Trust's QLCC. The Trust's QLCC did not meet during the fiscal year ended September 30, 2005.

Compensation of Trustees

For the fiscal year ended September 30, 2005, the Trust paid its Independent Trustees a retainer fee of \$20,000. The Trust currently pays each Independent Trustee \$500 for each Board and Committee meeting attended in person and \$250 for each Board and Committee meeting attended by phone. The Chairman of the Board of Trustees, the Chairman of the Audit Committee and the Chairman of the Valuation Committee of the Trust each receives an additional annual fee of \$2,500. Currently, the Chairman of the Nominating Committee and the Chairman of the Governance Committee receives an additional fee of \$1,250. Independent Trustees are also reimbursed for travel expenses incurred in connection with attending such meetings. For the fiscal year ended September 30, 2005, the Independent Trustees as a group received \$155,958 for fees and reimbursed expenses. The Trust did not pay any additional compensation to the Trustees for the fiscal year ended September 30, 2005. The Trust has entered into a Services Agreement (the "Agreement") with the Investment Adviser. Pursuant to the terms of the Agreement, the Trust reimburses the Investment Adviser for a portion of payment of salary and provision of benefits to the Trust's Chief Compliance Officer. During the year ended September 30, 2005 these payments amounted to \$66,017. Trustees and officers of the Trust other than the Chief Compliance Officer, who hold positions with the Investment Adviser, receive indirect compensation from the Trust in the form of the investment advisory fee paid to the Investment Adviser. The following table sets forth information regarding compensation of Trustees by the Trust for the year ended September 30, 2005, but does not include expenses.

**COMPENSATION TABLE
FOR THE FISCAL YEAR ENDED SEPTEMBER 30, 2005**

Name of Trustee	Aggregate Compensation From Trust	Pension or Retirement Benefits Accrued As Part of Trust Expense	Estimated Annual Benefits Upon Retirement	Total Compensation From Trust and Trust Complex Paid to Trustees
Independent Trustees:				
Lawrence S. Lewin	\$ 27,000	N/A	N/A	\$ 54,000
Robert P. Mack, M.D.	\$ 24,250	N/A	N/A	\$ 48,500
Eric Oddleifson	\$ 27,000	N/A	N/A	\$ 54,000
Oleg M. Pohotsky	\$ 31,000	N/A	N/A	\$ 62,000
Uwe E. Reinhardt, Ph.D.	\$ 22,000	N/A	N/A	\$ 44,000
Henri A. Termeer	\$ 22,000	N/A	N/A	\$ 44,000
Interested Trustee:				
Daniel R. Omstead, Ph.D.	\$ 0	N/A	N/A	\$ 0

THE TRUST

The Trust's capitalization consists of an unlimited number of Shares, \$.01 par value. Each Share represents an equal proportionate beneficial interest in the Trust and, when issued and outstanding, will be fully paid and non-assessable by the Trust. Upon any liquidation of the Trust, Shareholders will be entitled to share pro rata in the net assets of the Trust available for distribution after paying or adequately providing for the payment of all liabilities. The Trust will send annual and semi-annual financial statements to Shareholders and may also issue more abbreviated interim reports to update Shareholders on a quarterly basis. The Trust will hold annual meetings of its Shareholders in accordance with the provisions of the Trust's By-laws and the rules of the New York Stock Exchange ("NYSE").

Shareholders are entitled to one vote for each whole Share held and a proportionate fractional vote for each fractional Share held. The Trust's Shares do not have cumulative voting rights, which means that the holders of more than 50% of the Shares of the Trust voting for the election of Trustees can elect all of the Trustees, and, in such event, the holders of the remaining Shares will not be able to elect any Trustees. The Trust has a staggered Board, whereby one class of Trustees is elected each year.

The Trust is an entity of the type commonly known as a "Massachusetts business trust." Under Massachusetts law, shareholders of such a trust under certain circumstances may be determined to be personally liable as partners for the Trust's obligations. However, the Trust's Declaration of Trust contains an express disclaimer of shareholder liability for the acts or obligations of the Trust and provides for indemnification and reimbursement of expenses out of the Trust's property for any shareholder held personally liable for the obligations of the Trust. Thus, the risk of a shareholder incurring financial loss on account of a Trust liability is limited to circumstances in which the Trust is unable to meet its obligations from the liquidation of its portfolio investments.

The overall management of the Trust is vested in the Board. The Board approves all significant agreements between the Trust and persons or companies furnishing services to it, including the Trust's agreements with its Investment Adviser, Administrator, Custodian, any foreign sub-custodians, Registrar and Transfer Agent. The management of the day-to-day operations of the Trust is delegated to its officers and to the Investment Adviser, subject always to the investment objective and policies of the Trust and to general supervision by the Board.

In addition, the Declaration of Trust requires the affirmative vote or consent of the holders of 75% of the Shares of the Trust to authorize certain transactions with a person or entity that is directly, or indirectly through affiliates, the beneficial owner of 5% or more of the outstanding Shares of the Trust unless the Board takes certain actions to approve such a transaction. These provisions could make it more difficult to change the management of the Trust and could have the effect of depriving Shareholders of an opportunity to sell their Shares at a premium over prevailing market prices by discouraging a third party from seeking to obtain control of the Trust in a tender offer or similar transaction. See "Risk Factors — Certain Provisions of the Declaration of Trust" in the Trust's Prospectus.

Repurchase of Shares and Tender Offers

The Trust is a closed-end, management investment company and as such its Shareholders do not, and will not, have the right to redeem their Shares of the Trust. The Trustees, however, intend to consider, from time to time, but not less frequently than annually, the desirability of open market purchases or tender offers. Any such repurchases will be made in accordance with the applicable provisions of the Investment Company Act and Massachusetts law in open market transactions. Shares repurchased by the Trust will be held in its treasury. Although the Trust has no present intention of doing so, it reserves the

right to incur debt to finance such repurchases or tender offers, provided that it will not repurchase securities during the periods when it has outstanding borrowings in excess of 5% of its net assets. See “Investment Restrictions.” Interest on any borrowings to finance Share repurchase transactions will increase the Trust’s expenses and will reduce the Trust’s net income. There can be no assurance that Share repurchases, if any, will cause the Shares to trade at a price equal to or in excess of their net asset value. Nevertheless, the possibility that a portion of the Trust’s outstanding Shares may be the subject of repurchases may reduce the spread between market price and net asset value that might otherwise exist. The Trust may not repurchase Shares except (1) on a securities exchange and after notification to Shareholders of its intent to purchase Shares within the six months preceding the purchase, (2) pursuant to a tender offer to all Shareholders, or (3) as otherwise permitted by the Commission.

The Shares of the Trust will trade in the open market at a price which will be a function of several factors, including their supply, demand, investment performance and yield. The shares of closed-end investment companies generally sell at market prices varying from their net asset value (“NAV”) and such shares frequently trade at a discount to NAV, but in some cases trade at a premium. The market price of the Shares will be determined by factors including trading volume of such Shares, general market and economic conditions and other factors beyond the control of the Trust. Therefore, the Trust cannot predict whether its Shares will trade at, below or above NAV. When the Trust repurchases its Shares for a price below their NAV, the NAV of those Shares that remain outstanding will be enhanced, but this does not necessarily mean that the market price of those outstanding Shares will be affected, either positively or negatively.

Conversion to Open-End Investment Company Status

Under the Declaration of Trust, the conversion of the Trust from a closed-end to an open-end investment company would require (1) the approval of the Board of Trustees, and (2) the affirmative vote or consent of the holders of 66 2/3% of the Shares outstanding and entitled to vote. Such a vote would be in addition to any vote or consent required in addition to the vote or consent of Shareholders otherwise required by law or any agreement between the Trust and the NYSE. The Investment Company Act requires that the Trust receive a vote of a majority of its outstanding voting Shares in order to convert the Trust from a closed-end to an open-end investment company.

Such amendment would have to be approved by the Board prior to its submission to Shareholders. The Board is required under the Declaration of Trust to consider and vote annually upon the proposal to convert to open-end status. A proposal to convert the Trust to an open-end company might be supported or opposed by the Board depending on the Board’s judgment as to its advisability in light of circumstances prevailing at the time.

Shareholders of an open-end investment company may require the company to redeem their shares at any time (except in certain circumstances as authorized by or under the Investment Company Act) at their NAV, less such redemption charge, if any, as might be in effect at the time of a redemption. Conversion to an open-end investment company could require the disposal of illiquid investments to meet current requirements of the Commission that no more than 15% of an open-end investment company’s assets consist of illiquid securities, and would likely require involuntary liquidation of portfolio securities, and the inherent realization of net long-term capital gains in connection therewith, to meet periodic requests for redemption. Moreover, Shares of the Trust would no longer be listed on the NYSE.

INVESTMENT ADVISER AND INVESTMENT ADVISORY AGREEMENT

Hambrecht & Quist Capital Management LLC, a limited liability company under the laws of the State of Delaware, serves as the investment adviser to the Trust. The Investment Adviser is an investment adviser registered under the Investment Advisers Act of 1940, as amended. The Investment Adviser is located at 30 Rowes Wharf, Fourth Floor, Boston, MA 02110-3328.

At inception, Hambrecht & Quist Capital Management Incorporated (“HQCM, Inc.”) was the Trust’s investment adviser. HQCM, Inc. was formed as a wholly-owned subsidiary of Hambrecht & Quist Group. HQCM, Inc. remained the Investment Adviser as The Chase Manhattan Corporation (“Chase”) first acquired Hambrecht & Quist Group and then merged with J.P. Morgan Incorporated to form J.P. Morgan Chase & Co. In 2002, the management of HQCM, Inc. formed an independent entity, Hambrecht & Quist Capital Management LLC (“HQCM LLC”), to effect a buyout of HQCM, Inc. In this transaction, HQCM LLC acquired certain of the assets of HQCM, Inc., and substantially all of the management and staff of HQCM, Inc. became employees of HQCM LLC. HQCM LLC, the Trust’s current investment adviser, is owned by Daniel R. Omstead, Mary Omstead and the Alan G. Carr Irrevocable Trust. Mr. Carr, a former portfolio manager, president and trustee of the Trust, passed away in October 2003. Dr. Omstead is currently the President and Chief Executive Officer of the Investment Adviser. Mary Omstead is Dr. Omstead’s wife. Under the terms of HQCM LLC’s current Amended and Restated Limited Liability Company Agreement, HQCM LLC will purchase the Alan G. Carr Irrevocable Family Trust’s interest in HQCM LLC.

The Investment Advisory Agreement between the Investment Adviser and the Trust (the “Advisory Agreement”) provides that, subject to the supervision and direction of the Board, the Investment Adviser is responsible for the actual management of the Trust’s portfolio. The Investment Adviser is also obligated to supervise or perform certain administrative and management services for the Trust and is obligated to provide the office space, facilities, equipment and personnel necessary to perform its duties under the Advisory Agreement. The responsibility for making decisions to buy, sell or hold a particular security rests with the Investment Adviser. However, the Investment Adviser may consider investment analysis from various sources, including broker-dealers with which the Trust does business. See “Portfolio Transactions and Brokerage.”

Subject to the supervision and direction of the Board of Trustees of the Trust, the Investment Adviser manages the Trust’s portfolio in accordance with the Trust’s investment objective and policies as stated in the Trust’s Prospectus; makes investment decisions for the Trust; places purchase and sale orders for portfolio transactions for the Trust; supplies the Trust with office facilities (which may be in the Investment Adviser’s own offices), statistical and research data, data processing services, clerical, internal executive and administrative services, and stationery and office supplies; supplies or directs and supervises a third party administrator or custodian in the provision to the Trust of accounting and bookkeeping services, the calculation of the net asset value of shares of the Trust, internal auditing services, and other clerical services in connection therewith; and prepares or supervises and directs a third party administrator or custodian in the preparation of reports to shareholders of the Trust, tax returns and reports to and filings with the Commission and state Blue Sky authorities. In providing these services, the Investment Adviser provides investment research and supervision of the Trust’s investments and conducts a continual program of investment, evaluation and, if appropriate, sale and reinvestment of the Trust’s assets. In addition, the Investment Adviser furnishes the Trust with whatever statistical information the Trust may reasonably request with respect to the securities that the Trust may hold or contemplate purchasing.

Starting July 1, 2006, for the services provided by the Investment Adviser under the Advisory Agreement, the Trust pays a fee, computed and payable monthly, equal when annualized to (i) 2.5% of the average net assets for the month of its venture capital and other Restricted Securities (as defined) up to 25% of its net assets and (ii) for the month for all other assets, 0.98% of the average net assets up to \$250 million, 0.88% of the average net assets for the next \$250 million, 0.80% of the average net assets for the next \$500 million and 0.70% of the average net assets thereafter. The aggregate monthly fee may not exceed a rate when annualized of 1.375% (approximately 0.11% per month). Prior to July 1, 2006, the Trust paid a fee computed and payable monthly, equal, when annualized, to (i) 2.5% of the average net assets for the month of its venture capital and other Restricted Securities (as defined) up to 25% of net assets and (ii) for the month, for all other assets, 1.0% of the average net assets up to \$250 million, 0.90% of the average net assets for the next \$250 million, 0.80% of the average net assets for the next \$500 million and 0.70% of the average net assets thereafter. The aggregate fee could not exceed a rate when annualized of 1.375% (approximately 0.11% per month).

The Investment Adviser will not participate directly in the capital appreciation of Restricted Securities. The Investment Adviser may also provide managerial assistance to issuers of securities in which the Trust invests. For purposes of calculation of the investment advisory fee, “average net assets” for any month shall be equal to the average of the net asset value of such assets as of the last business day of such month and the net asset value of the appropriate assets as of the last business day of the preceding month. In determining average net assets for purposes of clauses (1) and (2) above, liabilities and expenses of the Trust shall be allocated pro rata based on the ratio that the assets referred to in each clause bear to the total assets of the Trust. Such fee shall be payable for each month within five business days after the end of such month.

For purposes of the calculation of the investment advisory fee, “venture capital and other Restricted Securities” shall be securities of issuers for which no market quotations are readily available and securities of companies for which market quotations are readily available but which are subject to legal or contractual restrictions on resale. Securities of companies for which public information is available but as to the sale of which the safe harbor provided by Rule 144(k) is not available shall be considered to be subject to legal or contractual restrictions on resale.

The investment advisory fee paid by the Trust exceeds that paid by most registered investment companies to their investment advisers. The Trust believes that the fee is commensurate with the nature and quality of the services required for identifying, evaluating and monitoring the Trust’s Restricted Securities investments.

The Advisory Agreement provides that the Investment Adviser shall not be liable for any loss incurred by any act or omission of any broker. The Advisory Agreement also provides that the Investment Adviser shall not be liable to the Trust or to any Shareholder of the Trust for any error or judgment or for any loss suffered by the Trust in connection with rendering services under the Advisory Agreement except (1) a loss resulting from a breach of fiduciary duty with respect to the receipt of compensation for services (in which case any award of damages shall be limited to the period and the amount set forth in Section 36(b)(3) of the Investment Company Act) or (2) a loss resulting from willful misfeasance, bad faith or gross negligence on the part of the Investment Adviser, or reckless disregard of its obligations and duties under the Advisory Agreement. Subject to the foregoing, the Advisory Agreement also provides that the Trust shall indemnify the Investment Adviser, and any officer, director and employee of the Investment Adviser to the maximum extent permitted by Article V of the Trust’s Declaration of Trust.

For the fiscal years ended September 30, 2005, September 30, 2004 and September 30, 2003, the Trust paid the Adviser \$2,676,602, \$2,651,448 and \$2,320,306, respectively, in advisory fees.

The services of the Investment Adviser to the Trust are not deemed to be exclusive, and nothing in the Advisory Agreement prevents the Investment Adviser, or any affiliate thereof, from providing similar services to other companies and other clients or from engaging in other activities.

Under the Advisory Agreement, the Investment Adviser has agreed to bear all expenses in connection with the performance of its services under the Advisory Agreement, including compensation of and office space for officers and employees of the Trust connected with investment and economic research, trading and investment management of the Trust, as well as the fees of all Trustees of the Trust who are “affiliated persons” of the Investment Adviser, as that term is defined in the Investment Company Act, or any of its “affiliated persons.”

Under the Advisory Agreement, the Trust must pay (or, in the event that such expenses are paid by the Investment Adviser, shall reimburse the Investment Adviser for) all other expenses incurred in the organization and operation of the Trust including, among other things, expenses for legal and auditing services, costs of printing proxy statements, prospectuses, stock certificates and shareholder reports, charges of the custodian, any sub-custodian and transfer agent, expenses in connection with the Dividend Reinvestment Plan, the Commission, and National Association of Securities Dealers, Inc. fees, fees and expenses of the Trustees who are not “affiliated persons” of the Investment Adviser or any of its “affiliated persons,” accounting and valuation costs, administrator’s fees, membership fees in trade associations, fidelity bond coverage for the Trust’s officers and employees, errors and omissions insurance coverage for Trustees and officers, interest, brokerage costs, taxes, stock exchange listing fees and expenses, expenses of qualifying the Trust’s Shares for sale in various states, expenses associated with personnel performing exclusively shareholder servicing functions, certain other organization expenses, litigation and other extraordinary or non-recurring expenses, and other expenses properly payable by the Trust. The Trust may enter into arrangements to have third parties assume any expenses for which it is responsible.

Unless earlier terminated as described below, the Advisory Agreement will remain in effect from year to year if approved annually (1) by the Board or by the holders of a majority of the Trust’s outstanding Shares and (2) by the majority of the Trustees who are not parties to the Advisory Agreement or interested persons of any such party. The Advisory Agreement may be terminated without penalty by (1) the Trust or the Investment Adviser at any time without penalty upon not less than 30 and no more than 60 days’ written notice or (2) a vote of the holders of a majority of the Trust’s outstanding Shares, and will automatically terminate in the event of its assignment. Action by the Trust under (1) above may be taken either by (i) vote of a majority of its Trustees, or (ii) the affirmative vote of a majority of the outstanding shares of the Trust.

The Investment Advisory Agreement (Advisory Agreement) between the Trust and the Adviser provides that the Advisory Agreement will continue in effect so long as its continuance is approved at least annually by (i) by the Trustees of the Trust or the shareholders by affirmative vote of a majority of the outstanding shares and (ii) a majority of the Trustees of the Trust who are not interested persons, by vote cast in person at a meeting called for the purpose of voting on such approval.

On April 20, 2006, the Board, and the independent Trustees voting separately, determined that the terms of the Advisory Agreement are fair and reasonable and approved the continuance of the Advisory Agreement as being in the best interests of the Trust and its shareholders. In making its determination, the Board considered materials that were specifically prepared by the Adviser at the request of the Board and Trust counsel for purposes of the contract review process, including comparisons of (i) the Trust’s performance to its benchmark and to certain other investment companies, (ii) the Trust’s expenses and expense ratios to those of a peer group of other investment companies, and (iii) the Adviser’s profitability with respect to its services for the Trust to the profitability of other investment managers. The Trustees

took into account that the Adviser presently provides investment management services only to the Trust and to H&Q and does not derive any benefit from its relationship with the Trust other than receipt of advisory fees pursuant to the Advisory Agreement. The Board also considered information received periodically about the portfolio, performance, investment strategy, portfolio management team and fees and expenses of the Trust.

The Investment Adviser's use of the term "H&Q" is pursuant to a written license agreement (the "License Agreement"), a copy of which the Investment Adviser has provided to the Trust. Under the License Agreement, the Investment Adviser may sublicense the term "H&Q" to an investment company for which it serves as investment adviser, for use as part of the investment company's name, pursuant to a written sublicense agreement that (a) is at least as protective of the rights of the licensor under the License Agreement as the License Agreement and (b) does not permit the investment company to sub-sublicense the term "H&Q". The Trust has agreed that its right to use the term "H&Q" is subject in all respects to the terms of the License Agreement. The Trust has also agreed that if the License Agreement terminates for any reason, or if the Investment Adviser ceases to act as investment adviser to the Trust, the Trust's sublicense to use the term "H&Q" as part of its name will terminate, at which time the Trust will take all necessary action to change its name to a name not including such term. The Investment Adviser may at any time permit others to use the term "H&Q" under a similar sublicense.

Portfolio Management

Currently Daniel R. Omstead, Ph.D., Christopher F. Brinzey, M.B.A., Frank T. Gentile, Ph.D. and Jason C. Akus, M.D./M.B.A. are members of the team that makes investments on behalf of the Trust. These members also perform other duties, including making investment decisions on behalf of H&Q Healthcare Investors, a closed-end mutual fund, but do not otherwise manage any other accounts.

Security Ownership of Portfolio Managers

As of March 15, 2006, the dollar range of Trust securities beneficial owned by Dr. Omstead was \$50,001 - \$100,000. As of August 15, 2006, none of the other members of the team owned securities of the Trust.

Portfolio Manager Compensation Structure

Dr. Omstead receives a base salary as compensation for his contribution to the portfolio management team and for his contribution to the general management of the Adviser. As part owner of the Investment Adviser, Dr. Omstead receives additional compensation from the Trust indirectly by virtue of the investment advisory fee paid to the Investment Adviser.

Mr. Brinzey, Dr. Gentile and Dr. Akus receive a combination of base compensation and discretionary compensation, in the form of a cash bonus paid annually. The methodology used to determine compensation is applied to all accounts managed by the team. Two components are described in detail below.

Base Salary Compensation. The team members receive a base salary compensation linked to individual experience and responsibilities. The amount of base salary is reviewed annually.

Discretionary Compensation. Discretionary Compensation is in the form of a cash bonus, paid annually, which may be up to 60% of the team member's base salary. Several factors affect discretionary compensation, which can vary by team member and circumstances. The discretionary compensation component is determined based on four factors including investment performance of accounts managed

by the team relative to an appropriate benchmark and/or peer funds, performance of specific investments proposed by the individual, financial performance of the Investment Adviser and a qualitative assessment of the individual overall contribution to the investment team and to the Investment Adviser. Discretionary compensation is evaluated annually after the completion of the Trust's fiscal year.

PROXY VOTING POLICY AND PROCEDURES

The Board of Trustees of the Trust has adopted a proxy voting policy and procedure (the "Proxy Voting Policy"), pursuant to which the Trustees have delegated proxy voting responsibility to the Investment Adviser in accordance with the Fund's Proxy Voting Policy. A copy of the Proxy Voting Policy for the Trust and the Investment Adviser are attached as Appendix A to this SAI.

A description of the Trust's proxy voting policies and procedures and information on how the Trust voted proxies relating to portfolio securities during the most recent 12-month period ended June 30, 2005 is available (i) without charge, upon request by calling 1-800-451-2597; (ii) by writing to Hambrecht & Quist Capital Management, LLC at 30 Rows Wharf, Suite 430, Boston, MA 02110-3328; (iii) on the Trust's website at www.hqcm.com; and (iv) on the SEC's website at www.sec.gov.

CODE OF ETHICS

The Trust's Board of Trustees and the Investment Adviser have approved a Code of Ethics under Rule 17j-1 of the Investment Company Act that covers certain personnel of the Trust and the Investment Adviser. The Code of Ethics establishes procedures for personal investing and restricts certain transactions by certain personnel covered by the Code of Ethics. Persons subject to the Code of Ethics may invest in securities for their personal investment accounts, including, in certain cases, securities that may be purchased or held by the Trust. The Code of Ethics applies to investments by covered persons in their personal accounts, the accounts of family members living in the same household, and accounts in which the covered person has a beneficial interest (i.e., ownership, voting or investment control). Some of the restrictions set forth in the Code of Ethics do not apply to the Trust's Independent Trustees. In general terms, the Code of Ethics is designed to ensure that the investing activities of covered personnel are conducted in a manner that avoids potential or actual conflicts of interest with the Trust and its Shareholders and that covered personnel conduct their personal investing in a manner consistent with their fiduciary duty towards the Trust and its shareholders.

The Code of Ethics requires pre-clearance for certain investments in equities (not including mutual funds), imposes reporting requirements, and imposes sanctions for violations. Specifically, among other things, the Code of Ethics prohibits sales of securities to or purchases of securities from the Trust and prohibits the purchase or sale of any security under consideration for trading by the Trust within seven days before or after the Trust trades in the security.

The Trust's Code of Ethics is filed as an exhibit to this registration statement. In addition, you may read and copy the Code of Ethics at the Commission's Public Reference Room in Washington, DC. You may obtain information on operations of the Public Reference Room by calling the Commission at (202) 551-8090. In addition, the Code of Ethics is available on the EDGAR Database on the Commission Internet site at <http://www.sec.gov>. You may obtain copies of the Code of Ethics, after paying a duplicating fee, by electronic request at the following email address: publicinfo@sec.gov, or by writing to the Commission's Public Reference Section, 100 F Street, NE, Washington, DC 20549.

NET ASSET VALUE

The net asset value (“NAV”) of the Trust’s Shares is calculated at the close of regular trading on the NYSE (generally 4:00 p.m., Eastern time) every day that the NYSE is open. The Trust makes this information available daily by telephone (800) 451-2597, via its web site (www.hqcm.com) and through electronic distribution for media publication, including major internet-based financial services web sites and portals (bloomberg.com, yahoo.com, cbsmarketwatch.com, etc.). Currently, The Wall Street Journal, The New York Times and Barron’s publish NAVs for closed-end investment companies at least weekly.

NAV is calculated by dividing the value of the securities held by the Trust plus any cash or other assets minus all liabilities, including accrued expenses, by the total number of Shares outstanding at such time. Securities for which market quotations are readily available are valued at market price. Portfolio securities that are traded on one or more U.S. national securities exchanges or in the over-the-counter market that are National Market System securities are valued at the last sale price or, lacking any sales, at the mean between last bid and asked prices. Other over-the-counter securities are valued at the most recent bid prices as obtained from one or more dealers that make markets in the securities. Redeemable securities issued by a registered open-end investment company are valued at net asset value per share. Other securities are valued at the mean between the closing bid and asked prices. Short-term investments that mature in 60 days or less are valued at amortized cost, unless the Board determines that such valuation does not constitute fair value.

Bonds, other than convertible bonds, are valued using a third-party pricing system. Convertible bonds are valued using this pricing system only on days when there is no sale reported. Temporary cash investments with maturity of 60 days or less are valued at amortized cost. Puts and calls generally are valued at the close of regular trading on the securities or commodities exchange on which they are primarily traded. Options on securities generally are valued at their last bid price in the case of exchange-traded options or, in the case of OTC-traded options, the average of the last bid price as obtained from two or more dealers unless there is only one dealer, in which case that dealer’s price is used. Forward foreign currency contracts are valued on the basis of the value of the underlying currencies at the prevailing currency exchange rate. The prevailing currency exchange rate shall be determined within one hour of when the most recently available exchange rate information has been received based on information obtained from a bank or banks.

Securities that are primarily traded on foreign securities exchanges generally are valued at the last sale price on the exchange on which they are primarily traded. Foreign securities that are primarily traded on the foreign over-the-counter market are generally valued at the last sale quotation, if market quotations are available, or the last reported bid price if there is no active trading in a particular security on a given day. However, if intervening events result in market volatility that significantly affects the value of any such foreign securities after the close of trading on the relevant foreign market, but before the Trust values its Shares on any particular day on which the Trust is required to value its Shares, the Trust may, but is not required to, determine the value of such securities at “fair value,” as determined in good faith by or under the direction of the Board of Trustees.

Quotations of foreign securities in foreign currencies are converted, at current exchange rates, to their U.S. Dollar equivalents in order to determine their current value. In addition, to the extent that the Trust values its foreign securities (other than ADR’s and ADS’s) as of the close of trading on various exchanges and over-the-counter markets throughout the world, the calculation of the Trust’s net asset value may not take place contemporaneously with the valuation of foreign securities held by the Trust.

The value of any security or other asset for which market quotations are not readily available shall be determined in a manner that most fairly reflects the security’s (or asset’s) “fair value.” Each such determination is based on a consideration of all relevant factors, which are likely to vary from one pricing context to another. Examples of such factors may include, but are not limited to: (1) the type of the

security; (2) the size of the holding (including percent of outstanding securities of issuer held by the Trust); (3) the initial cost of the security; (4) the existence of any contractual restrictions on the security's disposition and the time to freedom from such restrictions; (5) the price and extent of public trading in similar securities of the issuer or of comparable companies; (6) quotations or prices from broker-dealers and/or pricing services; (7) information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); (8) an analysis of the company's financial statements; (9) an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold (e.g., the existence of pending merger activity, public offerings or tender offers that might affect the value of the security); and (10) the price of securities in a subsequent round of financing of an issuer in an arm's-length transaction, if the round includes a new third party investor.

Sometimes a "significant valuation event" may cause the market value of a security to differ from the fair market value of that security. A "significant valuation event" is an event that causes or is likely to cause a market quotation to be unavailable or unreliable, and may include: situations relating to a single issue in a market sector; significant fluctuations in U.S. or foreign markets; market disruptions or closings caused by human error, equipment failures, natural disasters, armed conflicts, acts of God, governmental actions or other developments, as well as the same or similar events which may affect specific issues or the securities markets even though not tied directly to the securities markets. A significant valuation event occurring after the close of trading but before the time of valuation may mean that the closing price for the security does not constitute a readily available market quotation. If a significant valuation event has occurred, the security will be valued at fair value as determined in good faith by the Board in accordance with the procedures hereinafter described. Such valuations and procedures will be reviewed periodically by the Board.

The fair value of investments for which no market exists cannot be precisely determined. With respect to securities of a company in its early stage of development, valuation will typically be based upon the original cost to the Trust. This methodology will typically be used until significant developments affecting the portfolio company provide a basis for a change in valuation. The status of portfolio companies is monitored for progress against plan, advancement of the stage of product development, and other factors. When revenues and earnings are present they are monitored. Valuation changes are event driven. When an appropriate event occurs (e.g., the completion of a third party transaction or a significant change in business model) valuation is changed accordingly. In addition the Trust will typically base changes in valuation on actual transactions or on actual firm offers by sophisticated independent investors unaffiliated with the Investment Adviser. Legal or contractual restrictions on the sale of portfolio securities by the Trust will be considered in the valuation of such securities.

Other assets, which include cash, prepaid and accrued items, accounts receivable and income on investments and from the sale of portfolio securities, are carried in accordance with generally accepted accounting principles, as are all liabilities. Liabilities primarily include accrued expenses, sums owed for securities purchased and dividends payable.

PORTFOLIO TRANSACTIONS AND BROKERAGE

Subject to policies established by the Board, the Investment Adviser is primarily responsible for the execution of the Trust's portfolio transactions and the allocation of brokerage. In executing transactions for the portfolio and selecting brokers or dealers (which brokers or dealers may include any affiliate of the Investment Adviser to the extent permitted by the Investment Company Act), the Investment Adviser will use its best efforts to obtain the best price and execution for the Trust. In assessing the best price and execution available for any portfolio transaction, the Investment Adviser will consider all factors it deems relevant including, but not limited to, price (including any applicable

brokerage commission or dealer spread), size of order, difficulty of execution, and operational facilities of the firm involved and the firm's risk in positioning a block of securities. The Investment Adviser may cause the Trust to pay a broker-dealer that furnishes brokerage and research services a higher commission than that which might be charged by another broker-dealer for effecting the same transaction, provided that the Investment Adviser determines in good faith that such commission is reasonable in relation to the value of the brokerage and research services provided by such broker-dealer, viewed in terms of either the particular transaction or the overall responsibilities of the Investment Adviser to the Trust. In selecting brokers or dealers to execute a particular transaction and in evaluating the best price and execution available, the Investment Adviser may consider the brokerage and research services (as those terms are defined in Section 28(e) of the Securities Exchange Act of 1934, as amended) provided to the Trust and/or other accounts over which the Investment Adviser exercises investment discretion. Such brokerage and research services might consist of reports and statistics on specific companies or industries, general summaries of groups of bonds and their comparative earnings and yields, or broad overviews of the securities markets and the economy. It is further understood that such services may be useful to the Investment Adviser in connection with its services to other clients. While the Investment Adviser generally seeks reasonably competitive commission rates, the Trust will not necessarily pay the lowest commission available.

The Trust has no obligation to deal with any broker or group of brokers in executing transactions in portfolio securities. Brokers who provide supplemental research, market and statistical information to the Investment Adviser may receive orders for transactions by the Trust. The term "research, market and statistical information" includes advice as to the value of securities, the advisability of purchasing or selling securities and the availability of securities or purchasers or sellers of securities, and furnishing analyses and reports concerning issuers, industries, securities, economic factors and trends, portfolio strategy and the performance of accounts. Information so received will be in addition to and not in lieu of the services required to be performed by the Investment Adviser under the Advisory Agreement and the expenses of the Investment Adviser will not necessarily be reduced as a result of the receipt of such supplemental information. Such information may be useful to the Investment Adviser in providing services to clients other than the Trust, and not all such information may be used by the Investment Adviser in connection with the Trust. Conversely, such information provided to the Investment Adviser by brokers and dealers through whom other clients of the Investment Adviser in the future may effect securities transactions may be useful to the Investment Adviser in providing services to the Trust. To the extent the Investment Adviser receives valuable research, market and statistical information from a broker-dealer, the Investment Adviser intends to direct orders for Trust transactions to that broker-dealer, subject to the foregoing policies, regulatory constraints and the ability of broker dealers to provide competitive prices and commission rates.

The Investment Company Act restricts transactions involving the Trust and its "affiliates," including among others, the Trust's Trustees, officers and employees, the Investment Adviser and any "affiliates" of such affiliates. Subject to any such restrictions, investment companies advised by the Investment Adviser may concurrently invest with the Trust in Restricted Securities, and the Trust may also invest in companies in which directors of the Investment Adviser or Trustees of the Trust have invested or for which they serve as directors or executive officers. The Trust seeks to deal directly with the dealers who make markets in the securities involved, except as limited by applicable law and in those circumstances where better prices and execution are available elsewhere. Under the Investment Company Act, persons affiliated with the Trust are generally prohibited from dealing as principal with the Trust in the purchase and sale of securities. Under certain circumstances, affiliated persons of the Trust are permitted to serve as its broker in over-the-counter transactions conducted on an agency basis.

It is likely that, subject to applicable law, the Trust may invest in securities concurrently being purchased by other investment companies advised by the Investment Adviser. Such purchases would be

made on terms no less favorable than those under which such investment companies would be acquiring the securities. In the case of concurrent purchases by the Trust and another investment company or companies managed by the Investment Adviser, such purchases would be made where the Investment Adviser has made an independent decision on behalf of the Trust and such other company that the purchase is appropriate in light of the investment objectives, policies, restrictions, current holdings, available cash and portfolio structure of and other factors affecting each. Such investments will be allocated among clients in a manner believed by the Investment Adviser to be equitable to each. The Trust may also from time to time invest in securities of companies in which affiliated persons of the Trust have invested, subject to the provisions of the Investment Company Act and the rules and regulations promulgated thereunder.

The Trust's portfolio transactions in Restricted Securities are generally subject to Rule 144 under the Securities Act. In general, under Rule 144 as currently in effect, if the Trust has beneficially owned Restricted Securities of a publicly held issuer for more than one but less than two years, it will be entitled to sell in any three-month period that number of such securities that will not exceed the greater of 1% of the then outstanding securities of that class or the average weekly trading volume in securities of that class in any national securities exchange and/or in the over-the-counter market during the four calendar weeks immediately preceding the date on which notice of the sale is filed with the Commission. These volume limitations also apply to sales by the Trust of the securities of any issuer as to which it is deemed an affiliate, regardless of whether securities of such issuer are publicly traded. The above-described sales under Rule 144 are subject to certain requirements relating to manner of sale, notice and availability of current public information about the issuer. If the Trust is not deemed to have been an affiliate of the issuer at any time during the 90 days immediately preceding the sale and has beneficially owned Restricted Securities for at least two years, it is entitled to sell such securities under Rule 144(k) without regard to whether the issuer is publicly-held or to the volume limitations or other requirements described above. When Restricted Securities are sold to the public other than pursuant to Rule 144 or 144A, the Trust may be deemed an "underwriter" with respect thereto for purposes of the Securities Act and subject to liability as such thereunder.

On occasions when the Investment Adviser deems the purchase or sale of a security to be in the best interest of the Trust as well as other clients, the Investment Adviser, to the extent permitted by applicable laws and regulations, may, but shall be under no obligation to, aggregate the securities to be sold or purchased in order to obtain the most favorable price or lower brokerage commissions and efficient execution. In such event, allocation of the securities so purchased or sold, as well as the expenses incurred in the transaction, will be made by the Investment Adviser in the manner it considers to be the most equitable and consistent with its fiduciary obligations to the Trust and to such other clients.

Allocation of transactions, including their frequency, to various broker-dealers is determined by the Investment Adviser with respect to the Trust, based on its best judgment and in a manner deemed fair and reasonable to Shareholders. The primary consideration is prompt execution of orders in an effective manner at the most favorable price. Certain investments may be appropriate for the Trust and also for other clients advised by the Investment Adviser. Investment decisions for the Trust and for other investment accounts managed by the Investment Adviser are made independently of each other in the light of differing conditions. However, the same investment decision may be made for two or more of such accounts. When a purchase or sale of the same security is made at substantially the same time on behalf of the Trust and one or more other accounts, the transaction will be averaged as to price, and available investments allocated as to amount, in a manner the Investment Adviser believes to be equitable to each such account. Although the Investment Adviser seeks the most favorable overall net results for all of the accounts in any aggregated transaction, in some cases, this practice may adversely affect the price paid or received by the Trust or the size of the position obtained or sold by the Trust. To the extent permitted by law, the Investment Adviser may aggregate the securities to be sold or purchase for the Trust

with those to be sold or purchased for other investment companies or accounts in order to obtain best execution.

For the fiscal years ended September 30, 2005, September 30, 2004 and September 30, 2003, the Trust paid \$813,281, \$330,000 and \$218,162, respectively, of brokerage commissions. The increase in commissions in September 30, 2005 was due to strategy specific reallocations and market opportunities.

As stated in the Prospectus, the Trust's portfolio turnover rate for the fiscal years ended September 30, 2005 and September 30, 2004 was 73.79% and 34.93%, respectively. The increase in portfolio turnover rate was due to strategy specific reallocations and market opportunities. For a description of the Trust's portfolio turnover policies, see "Portfolio Transactions and Brokerage" in the Trust's Prospectus.

QUARTERLY DISTRIBUTION POLICY

In May 1999, the Trust's Board of Trustees adopted a managed distribution policy with respect to the Trust's Shares. Under the managed distribution policy, the Trust intends to make quarterly distributions to its Shareholders equal to 2.0% of the Trust's net asset value. The current distribution policy is to declare distributions in stock. Distributions will automatically be paid in newly-issued full Shares of the Trust plus cash in lieu of any fraction of a Share, unless otherwise instructed by the Shareholder. The Fund's transfer agent delivers an election card and instructions to each registered Shareholder in connection with each distribution. For shareholders other than registered shareholders with book entry accounts at the Trust's transfer agent, fractional shares will generally be settled in cash. The number of Shares issued will be determined by dividing the dollar amount of the distribution by the lower of net asset value or market value on the pricing date. If a shareholder elects to receive a distribution in cash, rather than in Shares, the Shareholder's relative ownership in the Trust will be reduced. The shares will be valued at the lower of net asset value or market price on the pricing date. Distributions in stock will not relieve shareholders of any federal, state or local income taxes that may be payable on such distributions.

If, for any taxable year, the total distributions required for the Trust's distribution policy exceed the Trust's annual investment company taxable income and net long-term capital gains, the excess will generally be treated as a return of capital (up to the amount of the Shareholder's adjusted tax basis in his or her Shares). The amount treated as a tax-free return of capital will reduce a Shareholder's adjusted basis in his or her own Shares, thereby increasing his or her potential gain or reducing his or her potential loss on the sale of his or her Shares.

If the Trust's investment company taxable income and net long-term capital gains for any taxable year or calendar year exceed the amount required to be distributed under the distribution policy, the Trust will, at a minimum, make distributions necessary to permit it to qualify for treatment as a regulated investment company under the Internal Revenue Code of 1986, as amended (the "Code"). The Trust has the discretion to retain for reinvestment net long-term capital gains in excess of net short-term capital losses, to the extent that it does not need to distribute these gains to meet its managed distribution obligation or tax requirements. Any retained gains may be subject to taxation, although Shareholders may receive credit for taxes paid by the Trust. It is anticipated that net realized capital gains in excess of the total distributed under this policy would be included in the December distribution.

This distribution policy may, under certain circumstances, have certain adverse consequences to the Trust and its Shareholders. To make such distributions, the Trust may have to sell a portion of its investment portfolio at a time when independent investment judgment might not dictate such action. The

Trust's quarterly distribution policy may be changed by the Board of Trustees without Shareholder approval.

The Trust's most recent distribution of \$0.35 per Share was payable to Shareholders of record on June 9, 2006. That distribution was paid in Shares on June 30, 2006. For the 2005 calendar year, the Trust distributed a total of \$2.06 per Share.

TAX MATTERS

The following is only a summary of certain U.S. federal income tax considerations generally affecting the Trust and its shareholders. No attempt is made to present a detailed explanation of the tax treatment of the Trust or its shareholders, and the following discussion is not intended as a substitute for careful tax planning. Shareholders should consult with their own tax advisers regarding the specific federal, state, local, foreign and other tax consequences of investing in the Trust.

Taxation of the Trust

The Trust intends to qualify and has elected to be treated each taxable year as a regulated investment company under the Code. The principal federal income tax benefits of qualifying as a regulated investment company ("RIC"), as compared to an ordinary taxable corporation, are that a RIC generally is not itself subject to federal income tax on ordinary investment income and net capital gains that are currently distributed to its shareholders, and that the character of long-term capital gains which are recognized and properly designated by a RIC flows through to its shareholders, who receive (or are deemed to receive) distributions of such income. However, the Trust is subject to corporate income tax (currently at a maximum marginal rate of 35%) on any undistributed income.

To qualify as a RIC, the Trust must, among other things, (a) derive in each taxable year at least 90% of its gross income from dividends, interest, payments with respect to securities loans, gains from the sale or other disposition of stock, securities or foreign currencies, net income derived from an interest in a qualified publicly traded partnership and other income derived with respect to its business of investing in such stock, securities or currencies (the "Qualifying Income Requirement"); (b) diversify its holdings so that, at the end of each quarter of the taxable year, (1) at least 50% of the market value of the Trust's assets is represented by cash and cash items, U.S. Government Securities, the securities of other RICs and other securities, with such other securities of any one issuer limited for the purposes of this calculation to an amount not greater than 5% of the value of the Trust's total assets and not greater than 10% of the outstanding voting securities of such issuer, and (2) not more than 25% of the value of its total assets is invested in the securities of (i) any one issuer (other than U.S. Government Securities or the securities of other RICs), (ii) two or more issuers (other than the securities of other RICs) which the taxpayer controls and which are determined to be in the same or similar trades or businesses; or (iii) one or more qualified publicly traded partnership; and (c) distribute at least 90% of its investment company taxable income (which includes, among other items, dividends, interest and net short-term capital gains in excess of net long-term capital losses) each taxable year. The U.S. Treasury Department has authority to promulgate regulations pursuant to which gains from foreign currency (and options, futures and forward contracts on foreign currency) not directly related to a RIC's business of investing in stocks and securities would not be treated as qualifying income for purposes of the Qualifying Income Requirement. To date, such regulations have not been promulgated.

If for any taxable year the Trust were to fail to qualify as a RIC, all of the Trust's taxable income would be subject to federal income tax at the rates applicable to corporations (with no deduction for

distributions to Shareholders), and Trust distributions would be taxable to Shareholders as dividends to the extent of the Trust's earnings and profits.

Amounts not distributed on a timely basis in accordance with a calendar year distribution requirement are subject to a nondeductible 4% excise tax. To avoid the excise tax, the Trust must distribute during each calendar year an amount equal to the sum of (1) at least 98% of its ordinary income (not taking into account any capital gains or losses) for the calendar year, (2) at least 98% of its capital gains in excess of its capital losses (adjusted for certain ordinary losses) for the one-year period ending on October 31 of the calendar year, and (3) all ordinary income and capital gains for previous years that were not distributed during such years. To avoid application of the excise tax, the Trust intends to make its distributions in accordance with the calendar year distribution requirement. A dividend will be treated as paid on December 31 of the calendar year if it is declared by the Trust in October, November or December of the year, payable to shareholders of record on a date in such a month and paid by the Trust during January of the following year. Such dividends will be taxable to shareholders as of December 31 of the calendar year in which the dividends are declared, rather than during the calendar year in which the dividends are received. If the Trust elects to retain net capital gains and treat such gains as having been distributed, all or a portion of such gains may not be treated as having been timely distributed for purposes of satisfying the excise tax calendar year distribution requirement.

Distributions

Dividends paid from investment company taxable income generally will be taxable to shareholders generally as ordinary income whether paid in cash or reinvested in the Trust's Shares. The Trust intends to distribute to its shareholders substantially all of its investment company taxable income, if any, for each year. It is anticipated that the Trust's income distributions will be paid annually in additional Shares unless the shareholder elects payment in cash.

A portion of the dividends paid by the Trust may be treated as "qualified dividend income" which is taxable to individuals at the same rates that are applicable to long-term capital gains. A Trust distribution is treated as qualified dividend income to the extent that the Trust receives dividend income from taxable domestic corporations and certain qualified foreign corporations, provided that certain holding period and other requirements are met by both the Trust and the shareholder. Trust distributions generally will not qualify as qualified dividend income to the extent attributable to interest, capital gains, REIT distributions and distributions from certain non-U.S. corporations. The lower rates on qualified dividends and capital gains are scheduled to expire after 2008 in the absence of further legislation enacted by Congress.

Distributions of the excess, if any, of net long-term capital gains over net short-term capital losses ("net capital gains") designated by the Trust as capital gain dividends will be taxable to shareholders as long-term capital gains, whether paid in cash or reinvested in the Trust's Shares, regardless of how long the shareholders have held the Trust's Shares, and will not be eligible for the dividends received deduction for corporations. The Trust may elect to retain net capital gains. In such event, the Trust will be required to pay federal income taxes on the undistributed net capital gains, but intends to elect to treat such capital gains as having been distributed to shareholders. As a result, such amounts will be included in the gross income of the shareholders as long-term capital gains and shareholders will be able to claim their proportionate share of federal income taxes paid by the Trust on such gains as a credit against their own federal income tax liabilities, and will be entitled to increase the adjusted tax basis of their Shares of the Trust by an amount equal to approximately 65% of the amount of the undistributed capital gains included in their gross income. Organizations or persons not subject to federal income tax on such capital gains (such as, generally, qualified pension and profit-sharing funds, including Individual Retirement Accounts and Keogh plans, and certain trusts, nonresident aliens and foreign corporations) will be entitled

to a refund of their pro rata share of such taxes paid by the Trust upon filing appropriate returns or claims for refund with the Internal Revenue Service (“IRS”). Even if the Trust makes such an election, it is possible that the Trust may incur an excise tax as a result of not having distributed sufficient net capital gains.

A distribution of an amount in excess of the Trust’s current and accumulated earnings and profits will be treated by a Shareholder as a return of capital which is applied against and reduces the Shareholder’s basis in his or her Shares. To the extent that the amount of any such distribution exceeds the shareholder’s basis in his or her Shares, the excess will be treated by the Shareholder as gain from a sale or exchange of the Shares.

If the value of the Trust’s Shares is reduced below a Shareholder’s cost as a result of a distribution of investment company taxable income or net capital gains by the Trust, such distribution will be taxable to the shareholder. The price of Shares purchased at this time may reflect the amount of the forthcoming distribution. Those purchasing just prior to a distribution of investment company taxable income or net capital gains will receive a distribution which will nevertheless be taxable to them.

Dividends (not including capital gain dividends) received by corporate shareholders from the Trust qualify for the dividends received deduction for corporate shareholders to the extent the Trust designates the amount distributed as eligible for the deduction. The aggregate amount designated by the Trust cannot exceed the aggregate amount of dividends received by the Trust from domestic corporations for the taxable year, and the designation of dividend income must generally be the same for all Shares. The dividends received deduction for corporate shareholders may be further reduced if the Shares with respect to which dividends are received are treated as debt-financed or if either those Shares or the Shares of the Trust are deemed to have been held by the Trust or its shareholders, respectively, for less than 46 days.

In addition to furnishing any other required tax statements, the Trust intends to send not later than 60 days after September 30 (the end of the tax and fiscal year of the Trust) written notices to shareholders regarding the tax status of all distributions made during such taxable year, the amount qualifying for the dividends received deduction for corporations and the amount of undistributed net capital gains and related tax credits.

Sale of Shares

Generally, gain or loss realized upon the sale or exchange of Shares will be capital gain or loss if the Shares are capital assets in the shareholder’s hands and generally will be long-term or short-term, depending upon the shareholder’s holding period for the Shares. Investors should be aware that any loss realized upon the sale or exchange of Shares held for six months or less will be treated as a long-term capital loss to the extent of any distributions or deemed distributions of long-term capital gain to the shareholder with respect to such Shares. In addition, any loss realized on a sale or exchange of Shares will be disallowed to the extent the Shares disposed of are replaced within a period of 61 days beginning 30 days before and ending 30 days after the Shares are disposed of, such as pursuant to the Plan. In such case, the basis of Shares acquired will be adjusted to reflect the disallowed loss.

The Trust may invest in shares of foreign corporations which may be classified under the Code as passive foreign investment companies (“PFICs”). In general, a foreign corporation is classified as a PFIC if at least one-half of its assets constitute investment-type assets, or 75% or more of its gross income is investment-type income. If the Trust receives a so-called “excess distribution” with respect to PFIC stock, the Trust itself may be subject to a tax on a portion of the excess distribution, whether or not the corresponding income is distributed by the Trust to shareholders. In general, under the PFIC rules, an

excess distribution is treated as having been realized ratably over the period during which the Trust held the PFIC shares. The Trust itself will be subject to tax on the portion, if any, of an excess distribution that is so allocated to prior Trust taxable years and an interest factor will be added to the tax, as if the tax had been payable in such prior taxable years. Gain from the sale of PFIC shares is treated in the same manner as an excess distribution. Excess distributions and gain from the sale of PFIC shares are characterized as ordinary income even though, absent application of the PFIC rules, such gains and certain excess distributions might have been classified as capital gain.

The Trust may elect to mark to market any PFIC shares in lieu of being subject to U.S. federal income taxation. At the end of each taxable year to which the election relates, the Trust would report as ordinary income the amount by which the fair market value of the PFIC stock exceeds the Trust's adjusted basis in the stock. Any mark-to-market losses and any loss from an actual disposition of shares would be deductible as ordinary losses to the extent of any net mark-to-market gains included in income in prior years. The effect of the election would be to treat excess distributions and gain on dispositions as ordinary income which is not subject to a Trust-level tax when distributed to shareholders as a dividend. Alternatively, the Trust may elect to include as income and gain its share of the ordinary earnings and net capital gain of certain PFICs in lieu of being taxed in the manner described above.

Currency Fluctuations-“Section 988” Gains or Losses

Under the Code, the gains or losses attributable to fluctuations in exchange rates which occur between the time the Trust accrues receivables or liabilities denominated in a foreign currency and the time the Trust actually collects such receivables or pays such liabilities generally are treated as ordinary income or ordinary loss. Similarly, on disposition of foreign currency or debt securities denominated in a foreign currency and on disposition of certain futures and forward contracts, gains or losses attributable to fluctuations in the value of foreign currency between the date of acquisition of the currency, security or contract and the date of disposition also are treated as ordinary gain or loss. These gains or losses, referred to under the Code as “Section 988” gains or losses, may increase or decrease the amount of the Trust's investment company taxable income to be distributed to its Shareholders as ordinary income.

Hedging Transactions

Certain futures and foreign currency contracts in which the Trust may invest are “section 1256 contracts.” While gains or losses on section 1256 contracts are considered 60% long-term and 40% short-term capital gains or losses, certain foreign currency futures and foreign currency contracts may give rise to ordinary income or loss, as described above. Also, section 1256 contracts held by the Trust at the end of each taxable year (and, generally, for purposes of the 4% excise tax, on October 31 of each year) are “marked-to-market” with the result that unrealized gains or losses are treated as though they were realized.

Generally, the hedging transactions undertaken by the Trust may result in “straddles” for U.S. federal income tax purposes. The straddle rules may affect the character of gains (or losses) realized by the Trust. In addition, losses realized by the Trust on positions that are part of a straddle may be deferred under the straddle rules, rather than being taken into account in calculating the taxable income for the taxable year in which the losses are realized. Because only a few regulations implementing the straddle rules have been promulgated, the tax consequences to the Trust of engaging in hedging transactions are not entirely clear.

The Trust may make one or more of the elections available under the Code which are applicable to straddles. If the Trust makes any of the elections, the amount, character and timing of the recognition of gains or losses from the affected straddle positions will be determined under the rules that vary

according to the election(s) made. The rules applicable under certain of the elections may operate to accelerate the recognition of gains or losses from the affected straddle positions.

Notwithstanding any of the foregoing, the Trust may recognize gain (but not loss) from a constructive sale of certain “appreciated financial positions” if the Trust enters into a short sale, offsetting notional principal contract, futures or forward contract transaction with respect to the appreciated position or substantially identical property. Appreciated financial positions subject to this constructive sale treatment are interests (including options, futures and forward contracts and short sales) in stock, partnership interests, certain actively traded trust instruments and certain debt instruments. Constructive sale treatment does not apply to certain transactions closed before the end of the thirtieth day after the close of the taxable year, if certain conditions are met.

Foreign Withholding Taxes

Income received by the Trust from non-U.S. sources may be subject to withholding and other taxes imposed by other countries. Because it is not expected that more than 50% of the value of the Trust’s total assets at the close of its taxable year will consist of stock and securities of non-U.S. corporations, it is not expected that the Trust will be eligible to elect to “pass-through” to the Trust’s shareholders the amount of foreign income and similar taxes paid by the Trust. In the absence of such an election, the foreign taxes paid by the Trust will reduce its investment company taxable income, and distributions of investment company taxable income received by the Trust from non-U.S. sources will be treated as U.S. source income.

Backup Withholding

The Trust may be required to withhold U.S. federal income tax at the rate of 28% of all taxable distributions payable to shareholders who fail to provide the Trust with their correct taxpayer identification number or to make required certifications, or who have been notified by the IRS that they are subject to backup withholding. Backup withholding is not an additional tax. Any amounts withheld may be credited against a shareholder’s U.S. federal income tax liability. Certain persons are exempt from the backup withholding requirements. Questions relating to backup withholding should be directed to your tax adviser.

Foreign Shareholders

U.S. taxation of a shareholder who, as to the U.S., is a non-resident alien individual, a foreign trust or estate, a foreign corporation or foreign partnership (“foreign shareholder”) depends on whether the income from the Trust is “effectively connected” with a U.S. trade or business carried on by such shareholder.

Income Not Effectively Connected

If the income from the Trust is not “effectively connected” with a U.S. trade or business carried on by the foreign shareholder, distributions of investment company taxable income will be subject to a U.S. tax of 30% (or lower treaty rate), which tax is generally withheld from such distributions.

Distributions of capital gain dividends and amounts retained by the Trust which are designated as undistributed capital gains will not be subject to U.S. tax at the rate of 30% (or lower treaty rate) unless the foreign shareholder is a non-resident alien individual and is physically present in the U.S. for more than 182 days during the taxable year and meets certain other requirements. However, this 30% tax on capital gains of non-resident alien individuals who are physically present in the U.S. for more than the

182-day period only applies in exceptional cases, because any individual present in the U.S. for more than 182 days during the taxable year is generally treated as a resident for U.S. federal income tax purposes; in that case, he or she would be subject to U.S. federal income tax on his or her worldwide income at the graduated rates applicable to U.S. citizens, rather than the 30% U.S. tax. In the case of a foreign shareholder who is a non-resident alien individual, the Trust may be required to withhold U.S. federal income tax at a rate of 28% of distributions of net capital gains unless the foreign shareholder certifies his or her non-U.S. status under penalties of perjury or otherwise establishes an exemption. See “Backup Withholding” above. If a foreign shareholder is a non-resident alien individual, any gain such shareholder realizes upon the sale or exchange of such shareholder’s Shares of the Trust in the U.S. will ordinarily be exempt from U.S. tax unless such shareholder is physically present in the U.S. for more than 182 days during the taxable year and meets certain other requirements.

However, subject to certain limitations and the receipt of further guidance from the U.S. Treasury, dividends paid to certain foreign shareholders may be exempt from U.S. tax through 2007 to the extent such dividends are attributable to qualified interest and/or net short-term capital gains, provided that the Trust elects to follow certain procedures. The Trust does not anticipate following the procedures and as a result, the full amount of distributions of ordinary dividends, including distributions of any interest or short-term gains will be subject to withholding at a rate of 30 percent or any applicable lower treaty rate.

Income Effectively Connected

If the income from the Trust is “effectively connected” with a U.S. trade or business carried on by a foreign shareholder, then distributions of investment company taxable income and capital gain dividends, amounts retained by the Trust which are designated as undistributed capital gains and any gains realized upon the sale or exchange of Shares of the Trust will be subject to U.S. federal income tax at the graduated rates applicable to U.S. citizens, residents and domestic corporations. Such foreign shareholders that are corporations may also be subject to the branch profits tax imposed by the Code.

The tax consequences to a foreign shareholder entitled to claim the benefits of an applicable tax treaty may be different from those described herein. Foreign Shareholders are advised to consult their own tax advisers with respect to the particular tax consequences to them of an investment in the Trust.

Other Taxes

Distributions may also be subject to state, local and foreign taxes and/or the alternative minimum tax depending on each Shareholder’s particular situation. Shareholders should consult their own tax advisers with respect to their particular situation.

ADMINISTRATOR, CUSTODIAN AND TRANSFER AGENT, DIVIDEND DISBURSING AGENT AND REGISTRAR

The Trust’s securities and cash are held under a custodian contract with State Street Bank and Trust Company (the “Custodian”), whose principal business address is 225 Franklin Street, Boston, Massachusetts 02110. Rules adopted under the Investment Company Act permit the Trust to maintain its securities and cash in the custody of certain eligible banks and securities depositories. Pursuant to those Rules, the Trust’s portfolio of securities and cash, when invested in Foreign Securities, will be held by sub-custodians who have been approved by the Board in accordance with the rules and regulations of the Securities and Exchange Commission following consideration of a number of factors, including, but not limited to, the relationship of the institution with the Custodian, the reliability and financial stability of the institution, the ability of the institution to perform capably custodial services for the Trust, the

reputation of the institution in its national market, the political and economic stability of the countries in which the sub-custodians will be located and the risks of potential nationalization or expropriation of Trust assets. The Custodian also performs certain accounting related functions for the Trust, including calculation of NAV and net income.

State Street Bank and Trust Company (the “Administrator”) also serves as administrator to the Trust pursuant to an Administration Agreement. Under the Administration Agreement the Trust’s assets are combined with assets of H&Q Healthcare Investors, another closed-end mutual fund managed by the Investment Adviser. The combined assets are charged a fee computed and payable monthly at an annual rate of (i) .034% of the first \$150 million; (ii) .024% of the next \$150 million; (iii) .014% on assets in excess of \$300 million, subject to annual minimum fee of \$77,500. The Administrative Agreement covers administrative costs, including out-of-pocket expenses incurred in the ordinary course of providing services under the Administration Agreement.

Computershare Shareholder Services, Inc. serves as Dividend Disbursing Agent, and as Transfer Agent and Registrar for Shares of the Trust. Computershare Shareholder Services, Inc. has its principal business at 150 Royal Street, Canton, MA 02021.

FINANCIAL STATEMENTS

The audited financial statements of the Trust included in the Prospectus have been audited by Deloitte and Touche LLP, independent registered public accounting firm, whose report dated November 18, 2005 expresses and unqualified opinion. The financial highlights for the years ended September 30, 2003, 2002 and 2001 were audited by PricewaterhouseCoopers LLP, whose report dated November 25, 2003 expresses and unqualified opinion. Certain information appearing under the caption “Financial Highlights” for the fiscal years ended September 30, 2000, 1999, 1998, 1997 and 1996 was audited by Arthur Andersen LLP. Arthur Andersen LLP ceased operations in 2002. Deloitte & Touche LLP has been selected as the independent registered public accounting firm of the Trust for the fiscal year ending September 30, 2006. Deloitte & Touche LLP will provide financial statement audit services to the Trust. Deloitte & Touche LLP’s offices are located at 200 Berkeley Street, Boston, MA 02116-5022.

Any statement contained in the Trust’s annual report that is included in the Prospectus shall be deemed modified or superseded for purposes of the Prospectus and this SAI to the extent a statement contained in the Prospectus or this SAI varies from such statement. Any such statement so modified or superseded shall not, except as modified or superseded, be deemed to constitute a part of the Prospectus or this SAI.

The unaudited financial statements included in the Trust’s Semi-Annual Report to Shareholders for the six months ended March 31, 2006 were mailed to Shareholders on or about May 25, 2006 and are available on the Trust’s website (www.hqcm.com).

APPENDIX A
TRUSTEE AND INVESTMENT ADVISER
PROXY VOTING POLICIES AND PROCEDURES
February 2006

The following are the policies and procedures adopted and implemented by Hambrecht & Quist Capital Management LLC (the “Investment Adviser”) for voting proxies with respect to portfolio securities held by H&Q Healthcare Investors and H&Q Life Sciences Investors (each a “Fund” and collectively the “Funds”). The policies and procedures are reasonably designed to ensure that proxies are voted in the best interest of the Funds and the Funds’ shareholders, in accordance with the Investment Adviser’s fiduciary duties and Rule 206(4)-6 under the Investment Advisers Act of 1940 (the “Investment Advisers Act”). The Investment Adviser considers the “best interests” of the Funds and their shareholders to mean their best long-term economic interests.

The Investment Adviser shall vote proxies for the exclusive benefit, and in the best economic interest, of the Funds and their shareholders. Such exercise of voting rights shall be subject to the same standard of care as is generally applicable to the Investment Adviser’s performance of its duties, as set forth in the advisory agreements with the Funds. The policies and procedures contained herein are designed to be guidelines, however each vote is ultimately cast on a case-by-case basis, taking into consideration the relevant facts and circumstances at the time of the vote. Any material conflicts that may arise will be resolved in the best interests of the Funds and their shareholders.

A proxy committee has been designated and is responsible for administering and overseeing the proxy voting process. The committee consists of the President of the Investment Adviser, the Investment Adviser’s Chief Compliance Officer (“CCO”), and the analyst responsible for oversight of the company that is the subject of the proxy. The committee considers proxy questions and determines the vote on behalf of the Funds.

Procedures

Logistics

The Investment Adviser’s CCO shall be responsible for maintaining the proxy log, monitoring corporate actions and confirming the timely voting of proxies. The proxy log shall contain the following information, in accordance with Form N-PX:

- the name of the issuer;
- the exchange ticker symbol, if available;
- the CUSIP number, if available;
- the shareholder meeting date;
- a brief identification of the matter voted on;
- whether the matter was proposed by the issuer or a security holder;
- whether the Investment Adviser cast its vote on the matter;

- how the Investment Adviser cast its vote on the matter (for, against, abstain; for or withhold regarding the election of directors); and
- whether the Investment Adviser cast its vote for or against management;

The Investment Adviser's CCO shall also record whether any conflicts of interest have been identified and, if so, what action was taken to resolve the conflict with respect to each vote cast and each abstention.

Substantive Voting Decisions

The Investment Adviser's substantive voting decisions turn on the particular facts and circumstances of each proxy vote. The following is a list of common proxy vote issues and the Investment Adviser's standard considerations when determining how to vote such proxies.

Routine Matters/Corporate Administrative Items. After an initial review, the Investment Adviser generally votes with management on routine matters related to the operation of the issuer that are not expected to have a significant economic impact on the issuer and/or its shareholders.

Potential for Major Economic Impact. The Investment Adviser reviews and analyzes on a case-by-case basis, non-routine proposals that are more likely to affect the structure and operation of the issuer and to have a greater impact on the value of the investment.

Corporate Governance. The Investment Adviser reviews and considers corporate governance issues related to proxy matters and generally supports proposals that foster good corporate governance practices.

Special Interest Issues. The Investment Adviser considers: (i) the long-term benefit to shareholders of promoting corporate accountability and responsibility on social issues; (ii) management's responsibility with respect to special interest issues; (iii) any economic costs and restrictions on management; and (iv) the responsibility of the Investment Adviser to vote proxies for the greatest long-term shareholder value.

Limitations on Director Tenure and Retirement. The Investment Adviser considers: (i) a reasonable retirement age for directors, *e.g.* 70 or 72; (ii) the introduction of new perspectives on the board; and (iii) the arbitrary nature of such limitations and the possibility of detracting from the board's stability and continuity.

Directors' Minimum Stock Ownership. The Investment Adviser considers: (i) the benefits of additional vested interest; (ii) the ability of a director to serve a company well regardless of the extent of his or her share ownership; and (iii) the impact of limiting the number of persons qualified to be directors.

D&O Indemnification and Liability Protection. The Investment Adviser considers: (i) indemnifying directors for acts conducted in the normal course of business; (ii) limiting liability for monetary damages for violating the duty of care; (iii) expanding coverage beyond legal expenses to acts that represent more serious violations of fiduciary obligation than carelessness (*e.g.* negligence); and (iv) providing expanded coverage in cases when a director's legal defense was unsuccessful if the director was found to have acted in good faith and in a manner that he or she reasonably believed was in the best interests of the issuer.

Director Nominations in Contested Elections. The Investment Adviser considers: (i) long-term financial performance of the issuer relative to its industry; (ii) management's track record; (iii) background to proxy contest; (iv) qualifications of both slates of nominees; (v) evaluations of what each side is offering shareholders as well as the likelihood that the proposed objectives and goals can be met; and (vi) stock ownership positions.

Cumulative Voting. The Investment Adviser considers: (i) the ability of significant stockholders to elect a director of their choosing; (ii) the ability of minority shareholders to concentrate their support in favor of a director or directors of their choosing; and (iii) the potential to limit the ability of directors to work for all shareholders.

Classified Boards. The Investment Adviser considers: (i) providing continuity; (ii) promoting long-term planning; and (iii) guarding against unwanted takeovers.

Poison Pills. The Investment Adviser considers: (i) the Investment Adviser's position on supporting proposals to require a shareholder vote on other shareholder rights plans; (ii) ratifying or redeeming a poison pill in the interest of protecting the value of the issuer; and (iii) other alternatives to prevent a takeover at a price demonstrably below the true value of the issuer.

Fair Price Provisions. The Investment Adviser considers: (i) the vote required to approve the proposed acquisition; (ii) the vote required to repeal the fair price provision; (iii) the mechanism for determining fair price; and (iv) whether these provisions are bundled with other anti-takeover measures (e.g., supermajority voting requirements) that may entrench management and discourage attractive tender offers.

Equal Access. The Investment Adviser considers: (i) the opportunity for significant shareholders of the issuer to evaluate and propose voting recommendations on proxy proposals and director nominees, and to nominate candidates to the board; and (ii) the added complexity and burden.

Charitable Contributions. The Investment Adviser considers: (i) the potential benefits to shareholders; (ii) the potential to detract the issuer's resources from more direct uses of increasing shareholder value; and (iii) the responsibility of shareholders to make individual contributions.

Stock Authorizations. The Investment Adviser considers: (i) the need for the increase; (ii) the percentage increase with respect to the existing authorization; (iii) voting rights of the stock; and (iv) overall capitalization structures.

Preferred Stock. The Investment Adviser considers: (i) whether the new class of preferred stock has unspecified voting, conversion, dividend distribution, and other rights; (ii) whether the issuer expressly states that the stock will not be used as a takeover defense or carry superior voting rights; (iii) whether the issuer specifies the voting, dividend, conversion, and other rights of such stock and the terms of the preferred stock appear reasonable; and (iv) whether the stated purpose is to raise capital or make acquisitions in the normal course of business.

Director Compensation. The Investment Adviser considers: (i) whether director shares are at the same market risk as those of the shareholders; and (ii) how option programs for outside directors compare with the standards of internal programs.

Golden and Tin Parachutes. The Investment Adviser considers: (i) whether they will be submitted for shareholder approval; and (ii) the employees covered by the plan and the quality of management.

Limitations

The Investment Adviser may abstain from voting a proxy if it concludes that the effect on shareholders' economic interests or the value of the portfolio holding is indeterminable or insignificant. The Investment Adviser may abstain from voting a proxy if it concludes that the cost of voting is disproportionate to the economic impact the vote would have on the portfolio holdings.

Conflicts of Interest

The Proxy Committee identifies any potential conflicts of interest. Each potential conflict must be addressed in a manner which will be in the best interest of the Funds and their shareholders. If any potential conflict is identified the Proxy Committee consults with the Investment Adviser's CCO. Where conflicts of interest arise between clients and the Investment Adviser, the Investment Adviser may convene an ad-hoc committee to debate the conflict and to give a ruling on a preferred course of action. If the ad-hoc committee determines that the Investment Adviser has a conflict of interest in any instance, the Investment Adviser's CCO shall disclose the conflict to the Board and seek voting instructions.

The Investment Adviser may cause the proxies to be voted in accordance with the recommendations of an independent third party service provider that the Investment Adviser may use to assist in voting proxies.

Disclosure

The following disclosure shall be provided in connection with these policies and procedures:

- The Investment Adviser shall provide a description or a copy of these policies and procedures to the Boards of Trustees of the Funds annually and upon request.
- The Investment Adviser shall make available to the Funds its proxy voting records, for inclusion on the Funds' Form N-PX.
- The Investment Adviser shall include its proxy voting policies and procedures in its annual filing on Form N-CSR.
- The Investment Adviser shall cause the Funds' shareholder reports to include a statement that a copy of these policies and procedures is available upon request (i) by calling a toll-free number; (ii) on the Funds' website, (if the Funds choose); and (iii) on the SEC's website.
- The Investment Adviser shall cause the Funds' annual and semi-annual reports to include a statement that information is available regarding how the Funds voted proxies during the most recent twelve-month period (i) without charge, upon request, either by calling a toll-free number or on or through the Funds' website, or both; and (ii) on the SEC's website.

Recordkeeping

The Investment Adviser shall maintain records of proxies voted in accordance with Section 204-2 of the Investment Advisers Act, including proxy statements, a record of each vote cast, and a copy of any document created by the Investment Adviser that was material to making a decision of how to vote the proxy, or that memorializes the basis for the Investment Adviser's decision on how to vote the proxy. The

Investment Adviser shall also maintain a copy of its policies and procedures and each written request from a client for proxy voting records and the Investment Adviser's written response to any client request, either written or oral, for such records. Proxy statements that are filed on EDGAR shall be considered maintained by the Investment Adviser. All such records shall be maintained for a period of five years in an easily accessible place, the first two year in the offices of the Investment Adviser.