



SECURITIES AND  
FUTURES COMMISSION  
證券及期貨事務監察委員會

# Quarterly Report

July - September 2001





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## Operations Highlights

1 July to 30 September 2001

1. By the end of September 2001, the half-yearly operating results of the SFC recorded a deficit of \$18 million, 25% lower than the budgeted half-yearly deficit of \$24.1 million. These interim results have been independently reviewed by the SFC's auditors, KPMG. The review does not constitute an audit.
2. Revenue was reduced as the thin trading turnover cut back on the SFC's transaction levy income. Fees and charges, investment income and other income also decreased. Expenditure for the first six months of this year amounted to \$210.1 million, \$27.9 million higher than in the same period last year. The major increase was in personnel expenses largely as a result of staff increases to cope with additional regulatory functions transferred from the Hong Kong Exchanges and Clearing Limited (HKEx) and increased expenditure on external relations.
3. To ensure Hong Kong's regulatory framework is on a par with other international markets, the SFC continued to work with the Administration and Legislative Council Bills Committee on the clause-by-clause examination of the Securities and Futures Bill during the quarter. Drafting and refinement of subsidiary legislation was also in progress. Three consultation papers were issued to seek public comments on new rules and codes, including the draft Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules, Proposed Index Funds Provisions for the Code on Unit Trusts and Mutual Funds and the draft Code of Conduct for Share Registrars.
4. The SFC continued to work with the Stock Exchange. The amendments to the Listing Rules of the Growth Enterprise Market were released in September to improve the quality of listing on the market. The Code on Takeovers and Mergers was also amended in October to lower the trigger threshold and to reduce the creeper, so as to bring the Code in line with international standards.
5. On market development, the Steering Committee on the Enhancement of Financial Infrastructure met again in August to discuss progress of its various working groups responsible for implementing FinNet, straight-through processing and a scripless market.
6. In August, HKEx successfully migrated its stock options trading to the Hong Kong Futures Automated Trading System, hence increasing efficiency and transparency of the derivatives market. The SFC also approved the rules changes that were necessary to facilitate the launch of international stock futures and options by the HKEx in October.
7. The SFC took disciplinary actions against 20 registrants and successfully prosecuted 14 parties for breaches of the Securities (Disclosure of Interests) Ordinance, Protection of Investors Ordinance and unregistered dealing. One alleged insider dealing case was referred to the Financial Secretary for his consideration of the appointment of an Insider Dealing Tribunal.



8. The SFC completed a Retail Investor Survey in July, which studied the profile and investment behaviour of retail investors, as well as their educational needs. In addition, the SFC reminded the public how they could protect themselves against misappropriation with a radio and newspaper campaign in August. The education column *SFC & You* also continued to run in a key local newspaper.
9. On the international front, the SFC participated in the plenary meeting of the International Financial Action Task Force in its fight against money laundering. It also helped overseas regulators crack down on an international 'boiler room' fraud during the quarter. Boiler rooms are fraudulent activities where operators use temporary offices (boiler rooms) to sell fraudulent products via aggressive selling techniques (boiling).
10. With effect from 1 September, the Unified Exchange Compensation Fund has been receiving transaction levy at 0.002% chargeable for every leviable transaction on the Stock Exchange. During the six months ended 30 September 2001, the Fund recognised \$5.6 million transaction levy.



## Review of Operations

1 July to 30 September 2001

This is the Securities and Futures Commission's (SFC) second Quarterly Report for the financial year 2001/2002.

Major world economies slowed further following the 11 September tragedy in the US, with Hong Kong being no exception. But the Hong Kong securities and derivatives markets remained open and fully operational. The SFC Coordination Centre sprang into operation on 12 September and monitored the trading, clearing and settlement functions, which operated normally and in an orderly manner. A total of 1,049 authorised mutual funds were suspended due to the closure of stock markets in the US and other countries. They resumed trading after periods ranging from a single day to one week. Impact on investors was minimal as there were few redemption requests.

During the quarter, the Hang Seng Index dropped from its peak of 13,207.53 (on 4 July) to its lowest level at 8,934.20 (on 21 September). By the end of September, it closed at 9,950.70, a drop of 24% from the previous quarter's 13,042.53 close (on 29 June). Average daily turnover on the stock market decreased by 33% to \$6.7 billion during the quarter, compared with an average of \$10 billion in the previous quarter. The average daily turnover in the same quarter last year was \$12.2 billion.

In these turbulent times, the SFC remains vigilant to ensure market integrity and efficiency. The SFC is committed to working with the markets on a series of market reforms and de-regulation exercises to ensure that Hong Kong remains in the leading rank of global financial centres.

### Financial Highlights

Due to declining revenue, the SFC recorded a \$20.2 million deficit for the quarter ended 30 September. Including the \$2.2 million surplus brought forward from the first quarter, the half-yearly operating results of the SFC recorded a deficit of \$18 million, well within the approved budgeted half-yearly deficit of \$24.1 million. The SFC's reserves amounted to \$660.2 million at the end of September 2001.

A comparison with the half-yearly results of last financial year indicated a swing from a surplus of \$82.2 million to this half-year's deficit of \$18 million. Roughly three quarters of the swing was due to the sharp decline in revenue. With the average daily turnover for the first half of the financial year down by 31% to \$8.5 billion compared with \$12.3 billion for the same period last year, the declining transaction levy income accounted for over half of the revenue decrease. Income from fees and charges declined due to a reduced number of licensing applications and corporate finance transactions. Investment income was also lower because of contributions to the compensation fund in the financial year 2000/2001. Other income was also sharply lower because there was an exceptional court award in last year.



The current operating expenditure for the first half-year was \$27.9 million higher than for the same period last year. The major increase was in personnel expenses largely as a result of staff increases to cope with additional regulatory functions transferred from the Hong Kong Exchanges and Clearing Limited (HKEx) and increased expenditure on external relations due to working with Mainland and overseas regulators. As of 30 September 2001, the total number of staff was 415 comprising 355 permanent staff and 60 temporary staff. The SFC continued to devote more resources to improving its productivity via computerisation and staff training. Depreciation increased by about 32%, reflecting the SFC's commitment to capital expenditure on computer systems development.

The outlook for the rest of the year depends very much on market turnover and fee income, as the average daily turnover in the quarter was \$6.8 billion, 38% below the \$11 billion assumed in the approved budget for the year. Whilst daily turnover in October showed a small recovery at \$7 billion, we expect the deficit for the year will be significantly higher than our budget of \$52.9 million, unless there is significant improvement during the rest of the financial year. The SFC will continue to exercise tight control on expenses, but the room for manoeuvre is limited as over 80% of the operating expenditure is incurred by personnel and rental costs. The SFC has already implemented a wage and hiring freeze.

#### **The Securities and Futures Bill**

The clause-by-clause examination by the Legislative Council Bills Committee of the Securities and Futures Bill continued. The SFC attended 10 Committee meetings during the quarter to help Committee members vet the Bill, and help formulate Committee Stage Amendments. Drafting and refinement of subsidiary legislation was also in progress. Considerable staff resources are committed to the legislative reforms. The SFC hopes to see the Bill enacted early next year.

#### **Enhancing Regulatory Framework**

During the quarter, three consultation papers for regulatory reforms were issued, compared with three last quarter and two issued in the same quarter last year: -

<b>SFC Consultation that Began / Closed during the Period 1 July to 30 September 2001</b>			
<b>Issue Date</b>	<b>Closing Date</b>	<b>Consultation Paper</b>	<b>Status</b>
20 July	20 August	A Consultation Paper on Proposed Index Funds Provisions for the Code on Unit Trusts and Mutual Funds	Completed
22 August	21 September	A Consultation Paper on the Draft Code of Conduct for Share Registrars	Completed
28 September	9 November	A Consultation Document on the Draft Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules	Completed



The SFC is working actively to reduce compliance costs for intermediaries. In August it issued a circular exempting fund managers from compliance with certain provisions of the Fund Manager Code of Conduct when they are dealing with professional investors. A review of licensing fees under the Securities and Futures Bill is in progress.

By the end of September, the number of licensed registrants and exempt persons increased by 2.1% to 30,049, 4.9% higher than in the same quarter last year (28,654).

Number of SFC Registrants under Various Ordinances and Exempt Persons			
	September 2001	June 2001	September 2000
Securities Ordinance (exclude Securities Margin Financiers)	23,712	23,012	22,379
Securities Ordinance (as Securities Margin Financiers)	239	266	N/A
Commodities Trading Ordinance	4,981	5,110	5,093
Leveraged Foreign Exchange Trading Ordinance	920	840	980
Exempt Persons	197	199	202
<b>Total</b>	<b>30,049</b>	<b>29,427</b>	<b>28,654</b>

The SFC continued to work with the Stock Exchange of Hong Kong Limited (SEHK) on various Listing Rules reforms. On 25 September, the final amendments to the Listing Rules of the Growth Enterprise Market (GEM) were announced, designed to improve the quality of listings on GEM. The SFC also approved the SEHK's new Listing Rules relating to the share options schemes of listed companies, effective 1 September.

On the completion of the public consultation exercise, the SFC on 19 October announced the amendments to the Code on Takeovers and Mergers with immediate effect. The trigger threshold (the percentage of shareholdings at which a mandatory general offer is required under Rule 26 of the Takeovers Code) was reduced from 35% to 30% and the creeper (the percentage by which holders of between the trigger percentage and 50% can increase their holdings without being required to make a mandatory offer under Rule 26 of the Code) from 5% to 2% in any 12-month period. Transitional provisions were put in place for 10 years for shareholders with existing holdings of between 30% and 34.9%.

### Encouraging Market Development

The SFC has worked closely with the industry on market development activities to consolidate Hong Kong's competitive edge as an international financial centre.

On infrastructural development, the Steering Committee on the Enhancement of Financial Infrastructure (SCEFI) has already defined the implementation path for FinNet (an electronic financial services network), straight-through processing and scripless market. HKEx's third generation Central Clearing and Settlement System (CCASS/3) will be offered to all securities and futures market participants as part of the FinNet functions.



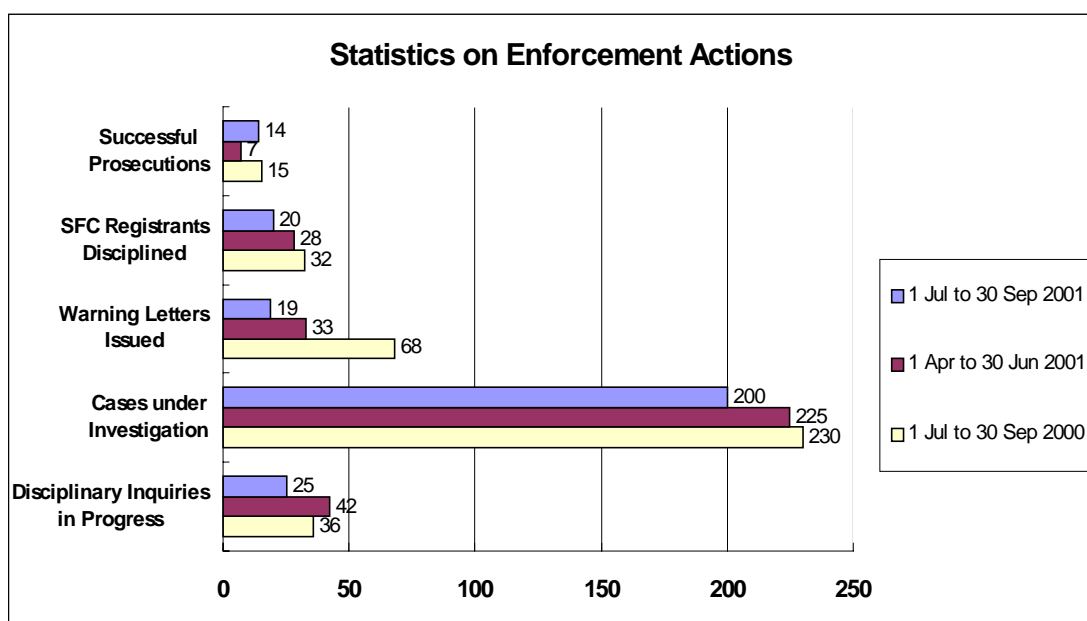
Following the migration of trading in the Hang Seng Index futures and options contracts from the open outcry system to the Hong Kong Futures Automated Trading System (HKATS) last year, HKEx successfully migrated the stock options trading to HKATS on 6 August. The move has further increased efficiency and enhanced transparency in the derivatives market.

On the product side, the SFC approved the rules changes that were necessary to facilitate the launch by HKEx of 20 international stock futures and 20 international stock options in October. More exchange traded funds and new derivatives products are being considered.

### Upholding Market Discipline

During the quarter, disciplinary actions were taken against 20 registrants for various types of misconduct leading to suspension, public reprimand and private reprimand. The SFC also successfully prosecuted 14 parties for breaching the Securities (Disclosure of Interests) Ordinance and Protection of Investors Ordinance as well as unregistered dealing.

During the quarter, one alleged insider dealing case was referred to the Financial Secretary for his consideration of the appointment of an Insider Dealing Tribunal.



### Empowering Investors to Protect Themselves

The SFC completed its Retail Investor Survey in July, which studied the profile and investment behaviour of retail investors in Hong Kong, as well as their educational needs. The survey helped the SFC to gauge the effectiveness of its investor protection initiatives and provided a benchmark against which the performance of the SFC is measured. Information collected in this survey will facilitate the SFC in drawing up a strategic plan for forthcoming investor education programmes.





In August, the SFC ran a thematic campaign through major local newspapers and radio channels to remind investors how to protect themselves against misappropriation, the wrongful use of client assets in brokerage accounts. The educational column *SFC & You* also continued to run in the Oriental Daily News (the preferred newspaper according to the SFC Retail Investor Survey) to explain a variety of topics relating to investment and regulation.

During the quarter, the SFC received 742 enquiries and 203 complaints about registrants or market conduct, compared with 649 enquiries and 137 complaints in the previous quarter. The corresponding figures for the same quarter last year were 883 and 132.

### **Participating in International Community**

The SFC continued to participate actively in the international securities regulatory community. The SFC has cooperated with overseas regulators in relation to cross-border supervision of fund management activities and helped to crack down on an international 'boiler room' fraud. Boiler rooms are fraudulent activities where operators use temporary offices (boiler rooms) to sell fraudulent products via aggressive selling techniques (boiling). During the quarter, the SFC participated in the first plenary meeting of the International Financial Action Task Force in its fight against money laundering.

### **Looking Ahead**

The departure of several Executive Directors and senior staff has recently triggered some market concerns. But the SFC was fortunate enough to be able to attract and find high quality talents from the markets to succeed the outgoing Executive Directors. Ashley Alder succeeded David Stannard as Executive Director (Corporate Finance) on 1 October and Alan Linning succeeded Paul Bailey as Executive Director (Enforcement) on 1 November. Alexa Lam will also replace Andrew Procter as Executive Director (Intermediaries and Investment Products) effective 1 December. I welcome them all and offer my deepest thanks to Mr Stannard, Mr Bailey and Mr Procter for their dedication and contribution to the Commission and the Hong Kong market.

I am also honoured to be re-appointed as the Chairman of the SFC for a period of two years and to continue serving the markets and the community. There is much to do. While the work to modernise Hong Kong's securities legislation and to enhance the local financial infrastructure is now in full swing, the SFC is committed to seeing through the implementation of these major market reform initiatives and to helping Hong Kong excel as a world-class financial market.

Andrew Sheng  
Chairman

14 November 2001



# **Independent Review Report**

## **To The Securities and Futures Commission (SFC)**

**(Established in Hong Kong under the Securities and Futures Commission Ordinance)**

### **Introduction**

We have been instructed by the SFC to review the interim financial report for the six-month period ended 30 September 2001 set out on pages 9 to 12.

### **Directors' responsibilities**

The directors are responsible for preparing an interim financial report of the SFC to match the requirements in the relevant provisions of The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and to comply with International Accounting Standard 34 "Interim financial reporting" issued by the International Accounting Standards Committee. The interim financial report is the responsibility of, and has been approved by, the directors.

### **Review work performed**

We conducted our review in accordance with Statement of Auditing Standards 700 "Engagements to review interim financial reports" issued by the Hong Kong Society of Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

### **Review conclusion**

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six-month period ended 30 September 2001.

KPMG  
Certified Public Accountants  
Hong Kong, 13 November 2001



## Securities and Futures Commission

### Income and Expenditure Account

For the six months ended 30 September 2001

(Expressed in Hong Kong Dollars)

	Note	Unaudited		Unaudited	
		30-Sep 01	30-Sep 00	30-Sep-01	30-Sep-00
		\$'0 00	\$'0 00	\$'0 00	\$'0 00
<b>Income</b>					
Levies		45,841	87,701	108,433	145,986
Fees and charges		26,172	31,173	59,169	70,667
Investment income		11,248	14,996	23,853	30,281
Other income		124	16,916	656	17,447
		<u>83,385</u>	<u>150,786</u>	<u>192,111</u>	<u>264,381</u>
		-----	-----	-----	-----
<b>Expenses</b>					
Staff costs		80,776	69,764	161,676	139,300
Premises					
- rent		5,002	5,001	10,005	10,004
- other		2,797	2,287	5,617	4,906
Other expenses		9,060	12,812	21,938	19,770
		<u>97,635</u>	<u>89,864</u>	<u>199,236</u>	<u>173,980</u>
		-----	-----	-----	-----
Depreciation		5,985	4,497	10,912	8,231
		<u>103,620</u>	<u>94,361</u>	<u>210,148</u>	<u>182,211</u>
		-----	-----	-----	-----
<b>(Deficits)/Surplus</b>	2	<u>(20,235)</u>	<u>56,425</u>	<u>(18,037)</u>	<u>82,170</u>
		-----	-----	-----	-----

We have not prepared a separate statement of recognised gains and losses as the (deficits)/surplus would be the only component of such a statement.

The notes on page 12 form an integral part of the condensed financial statements.



## Securities and Futures Commission

### Balance Sheet

At 30 September 2001

(Expressed in Hong Kong Dollars)

	<u>Note</u>	Unaudited At 30 Sep 2001 \$'000	Audited At 31 Mar 2001 \$'000
<b>Non-current assets</b>			
Fixed assets		39,006	38,696
Held-to-maturity debt securities		361,200	370,204
<b>Current assets</b>			
Held-to-maturity debt securities		73,984	277,046
Bank deposits		257,074	102,624
Debtors, deposits and prepayments		26,708	29,821
Cash at bank and in hand		2,095	4,469
		<u>359,861</u>	<u>413,960</u>
		-----	-----
<b>Current liabilities</b>			
Provision for contribution to the Unified Exchange Compensation Fund		30,000	66,174
Fees received in advance		31,681	31,271
Creditors and accrued charges		38,224	47,216
		<u>99,905</u>	<u>144,661</u>
		-----	-----
<b>Net current assets</b>		<u>259,956</u>	<u>269,299</u>
		-----	-----
<b>Net assets</b>		<u>660,162</u>	<u>678,199</u>
		-----	-----
<b>Funding and reserves</b>			
<b>Initial funding by Government</b>		42,840	42,840
<b>Accumulated Surplus</b>	2	617,322	635,359
		<u>660,162</u>	<u>678,199</u>
		-----	-----

The notes on page 12 form an integral part of the condensed financial statements.



## Securities and Futures Commission

### Cash Flow Statement

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	Unaudited Six months ended 30 Sep 2001 \$'000	Unaudited Six months ended 30 Sep 2000 \$'000
<b>Net cash (outflow)/inflow from operating activities</b>	(35,075)	49,763
<b>Returns on investments - interest received</b>	22,504	27,199
<b>Payments to the Unified Exchange Compensation Fund</b>	(36,174)	(150,000)
<b>Investing activities</b>		
Held-to-maturity debt securities bought	-	(149,972)
Held-to-maturity debt securities redeemed	212,000	-
Held-to-maturity debt securities sold	-	183,176
Fixed assets bought	(11,272)	(11,599)
Fixed assets sold	93	143
<b>Net cash inflow from investing activities</b>	200,821	21,748
Increase/(decrease) in cash and cash equivalents	152,076	(51,290)
Cash and cash equivalents at beginning of the six months	107,093	155,439
<b>Cash and cash equivalents at end of the six months</b>	259,169	104,149
<b>Reconciliation of (deficits)/surplus of income over expenses to net cash (outflow) / inflow from operating activities :</b>		
(Deficits)/Surplus	(18,037)	82,170
Investment income	(23,853)	(30,281)
Depreciation	10,912	8,231
(Profit)/loss on sale of fixed assets	(43)	40
Decrease in debtors, deposits and prepayments	4,528	11,276
Decrease in creditors and accrued charges	(8,992)	(22,340)
Increase in fees received in advance	410	667
<b>Net cash (outflow) / inflow from operating activities</b>	(35,075)	49,763
<b>Analysis of the balance of cash and cash equivalents :</b>		
	Unaudited At 30 Sep 2001 \$'000	Unaudited At 30 Sep 2000 \$'000
Bank deposits	257,074	102,834
Cash at bank and in hand	2,095	1,315
	259,169	104,149



# Securities and Futures Commission

## Notes to the Condensed Financial Statements

For the six months ended 30 September 2001

*(Expressed in Hong Kong dollars)*

### 1. Basis of preparation

The interim financial report has been prepared in accordance with the requirements of the Main Board Listing Rules of the Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard 34 "Interim financial reporting" issued by the International Accounting Standards Committee.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2001 included in this report does not constitute the SFC's statutory accounts for that financial year but is derived from those accounts.

The same accounting policies adopted in the financial statements for the year ended 31 March 2001 have been applied to the interim financial report.

### 2. Accumulated surplus

Movements of accumulated surplus during the six months ended 30 September 2001 are as follows :

	<b><u>Unaudited</u></b>
	\$'0 00
Balance at 31 March 2001	635,359
Deficits for the period	(18,037)
	<hr/>
Balance at 30 September 2001	<u>617,322</u>



# Unified Exchange Compensation Fund (the Fund)

## Report of the Securities Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the six-month period ended 30 September 2001.

### 1. ESTABLISHMENT OF THE FUND

Part X of the Securities Ordinance (Chapter 333) established the Fund.

### 2. FINANCIAL RESULTS

The committee presents the financial results which are set out in the condensed financial statements on pages 15 to 21.

### 3. MEMBERS OF THE COMMITTEE

The members of the Committee during the six months and up to the date of this report were: -

Mr. Mark Dickens  
Mr. Andrew Procter  
Mr. David M. Roberts  
Mr. Kwong Ki Chi, GBS  
Hon. Bernard Chan (appointed on 1 April 2001)

### 4. INTERESTS IN CONTRACTS

No contract of significance to which the Fund was a party and in which a Committee Member had a material interest, whether directly or indirectly, subsisted at the balance sheet date or at any time during the six months.

On behalf of the Committee

Mark Dickens  
Chairman

6 November 2001



# **Independent review report to the board of directors of Securities and Futures Commission (the SFC)**

**(Established in Hong Kong under the Securities and Futures Commission Ordinance)**

## **Introduction**

We have been instructed by the SFC to review the interim financial report for the six-month period ended 30 September 2001 of the Unified Exchange Compensation Fund (the Fund) established under Section 99 of the Hong Kong Securities Ordinance set out on pages 15 to 21.

## **Directors' responsibilities**

The SFC is responsible for preparing an interim report of the Fund to match the requirements in the relevant provisions of The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and to comply with International Accounting Standard 34 "Interim financial reporting" issued by the International Accounting Standards Committee. The interim financial report is the responsibility of the SFC and has been approved by the Securities Compensation Fund Committee.

## **Review work performed**

We conducted our review in accordance with Statement of Auditing Standards 700 "Engagements to review interim financial reports" issued by the Hong Kong Society of Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

## **Review conclusion**

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six-month period ended 30 September 2001.

KPMG  
Certified Public Accountants  
Hong Kong, 6 November 2001





## Unified Exchange Compensation Fund

### Income and Expenditure Account

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	Unaudited		Unaudited	
	Three Months Ended		Six Months Ended	
	30 Sep 2001	30 Sep 2000	30 Sep 2001	30 Sep 2000
	\$	\$	\$	\$
<b>Income</b>				
Investment Income	9,939,908	7,116,344	19,972,787	12,251,283
	-----	-----	-----	-----
<b>Expenses</b>				
Auditors' remuneration	10,350	9,720	20,700	19,440
Bank charges	39,375	99,770	75,151	110,857
Professional fees	56,406	33,000	127,638	66,000
Sundry expenses	40	680	1,220	680
	-----	-----	-----	-----
	106,171	143,170	224,709	196,977
	-----	-----	-----	-----
<b>Surplus</b>	9,833,737	6,973,174	19,748,078	12,054,306
<b>Accumulated surplus brought forward</b>	201,448,236	164,632,621	191,533,895	159,551,489
	-----	-----	-----	-----
<b>Accumulated surplus carried forward</b>	<u>211,281,973</u>	<u>171,605,795</u>	<u>211,281,973</u>	<u>171,605,795</u>

The notes on pages 19 to 21 form an integral part of the condensed financial statements.



## Unified Exchange Compensation Fund

### Balance Sheet

At 30 September 2001

(Expressed in Hong Kong dollars)

	Note	Unaudited At 30 Sep 2001 \$	Audited At 31 Mar 2001 \$
<b>Non-current assets</b>			
Held-to-maturity debt securities		247,630,742	390,060,457
<b>Current assets</b>			
Held-to-maturity debt securities		142,019,846	123,146,790
Contributions receivable		30,000,000	102,347,362
Interest receivable		3,316,974	5,358,046
Levy receivable		5,581,052	-
Bank fixed and call deposits		343,847,361	132,127,801
Cash at bank		207,675	57,360
		524,972,908	363,037,359
<b>Current liabilities</b>			
Accounts payable and accrued charges		2,307,255	585,635
Provision for compensation	3	31,438,997	123,280,031
		33,746,252	123,865,666
<b>Net current assets</b>		491,226,656	239,171,693
<b>Net assets</b>		738,857,398	629,232,150
Representing: <b>Compensation fund</b>			
Contributions from the SEHK		46,450,000	46,450,000
less: Compensation paid	2	(78,712,005)	(72,581,920)
Provision for compensation	3	(6,374,301)	(10,880,262)
Add: Recoveries		11,793,549	9,853,688
Replenishments from the SEHK		16,360,196	16,360,196
		(10,482,561)	(10,798,298)
Excess transaction levy from the SEHK		353,786,882	353,786,882
Special contribution		3,500,000	3,500,000
Additional contributions from the SEHK and the SFC		630,000,000	630,000,000
Special levy surplus		3,002,104	3,002,104
Transaction Levy	4	5,581,052	-
Accumulated surplus		211,281,973	191,533,895
		1,207,152,011	1,181,822,881
Less: Compensation paid	2	(432,747,356)	(429,392,664)
Provision for compensation	3	(25,064,696)	(112,399,769)
		749,339,959	640,030,448
		738,857,398	629,232,150

The notes on pages 19 to 21 form an integral part of the condensed financial statements.



## Unified Exchange Compensation Fund

### Statement of Recognised Gains and Losses

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	<u>Note</u>	<u>Unaudited Six Months Ended 30 Sep 2001 \$</u>	<u>Unaudited Six Months Ended 30 Sep 2000 \$</u>
Recoveries		1,939,861	3,669,520
Decrease in provision for compensation		91,841,034	54,361,892
Compensation paid out of the Fund	2	(9,484,777)	(54,361,892)
Additional Contributions from the SEHK & the SFC		-	300,000,000
Transaction Levy	4	5,581,052	-
<b>Net gains not recognised in the income and expenditure account</b>		<u>89,877,170</u>	<u>303,669,520</u>
Surplus		<u>19,748,078</u>	<u>12,054,306</u>
<b>Total recognised gains</b>		<u><u>109,625,248</u></u>	<u><u>315,723,826</u></u>

The notes on pages 19 to 21 form an integral part of the condensed financial statements.



## Unified Exchange Compensation Fund

### Cash Flow Statement

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended 30 Sep 2001 \$	Unaudited Six Months Ended 30 Sep 2000 \$
<b>Net cash inflow/(outflow) from operating activities</b>	1,496,911	(829,333)
<b>Returns on investments</b> - interest received	22,570,518	10,703,626
<b>Investing activities</b>		
Held-to-maturity debt - securities redeemed	123,000,000	142,000,000
Held-to-maturity debt - securities bought	-	(441,082,010)
<b>Net cash inflow/(outflow) from investing activities</b>	123,000,000	(299,082,010)
<b>Financing</b>		
Recoveries	1,939,861	3,669,520
Compensation paid	(9,484,777)	(54,361,892)
Additional contribution from the SEHK and the SFC	72,347,362	300,000,000
<b>Net cash inflow from financing</b>	64,802,446	249,307,628
Increase/(decrease) in cash and cash equivalents	211,869,875	(39,900,089)
Cash and cash equivalent at beginning of the six months	132,185,161	175,877,044
<b>Cash and cash equivalent at end of the six months</b>	<u>344,055,036</u>	<u>135,976,955</u>
<b>Reconciliation of surplus for the six month period to net cash inflow/(outflow) from operating activities:</b>		
Surplus	19,748,078	12,054,306
Investment Income	(19,972,787)	(12,251,283)
Increase/(decrease) in accounts payable and accrued charges	1,721,620	(632,356)
<b>Net cash inflow/(outflow) from operating activities</b>	<u>1,496,911</u>	<u>(829,333)</u>
<b>Analysis of changes in financing:</b>		
	Recoveries \$	Compensation Paid \$
Balance at 1 April 2000	3,530,920	(438,328,748)
Cash inflow/(outflow) from financing	3,669,520	(54,361,892)
Balance at 30 September 2000	<u>7,200,440</u>	<u>(492,690,640)</u>
Balance at 1 April 2001	9,853,688	(501,974,584)
Cash inflow/(outflow) from financing	1,939,861	(9,484,777)
Balance at 30 September 2001	<u>11,793,549</u>	<u>(511,459,361)</u>
<b>Analysis of the balance of cash and cash equivalents</b>		
	Unaudited At 30 Sep 2001 \$	Unaudited At 30 Sep 2000 \$
Cash at bank	207,675	106,268
Bank fixed and call deposits	343,847,361	135,870,687
	<u>344,055,036</u>	<u>135,976,955</u>



**Unified Exchange Compensation Fund**  
**Notes to the Condensed Financial Statements**  
**For the six months ended 30 September 2001**  
*(Expressed in Hong Kong dollars)*

**1. ACCOUNTING POLICIES**

The interim financial report has been prepared in accordance with the requirements of the Main Board Listing Rules of the Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard 34 "Interim financial reporting" issued by the International Accounting Standards Committee.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2001 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

The same accounting policies adopted in the financial statements for the year ended 31 March 2001 have been applied to the interim financial report.

**2. COMPENSATION PAID**

	\$
Compensation paid up to the \$8 million limit as set out in Section 109(3) of the Securities Ordinance	
Balance as at 1 April 2000	68,815,176
Add: compensation paid during the year ended 31 March 2001	3,766,744
	<hr/>
Balance as at 31 March 2001	72,581,920
Add: compensation paid during the six months ended 30 September 2001	6,130,085
	<hr/>
Balance as at 30 September 2001	<u>78,712,005</u>
Compensation paid in excess of the \$8 million limit pursuant to Section 113(5A) of the Securities Ordinance	
Balance as at 1 April 2000	369,513,572
Add: compensation paid during the year ended 31 March 2001	59,879,092
	<hr/>
Balance as at 31 March 2001	429,392,664
Add: compensation paid during the six months ended 30 September 2001	3,354,692
	<hr/>
Balance as at 30 September 2001	<u>432,747,356</u>



**Unified Exchange Compensation Fund**  
**Notes to the Condensed Financial Statements**  
**For the six months ended 30 September 2001**  
*(Expressed in Hong Kong dollars)*

**2. COMPENSATION PAID - Cont'd**

Total compensation paid as at 31 March 2001 \$501,974,584

Total compensation paid as at 30 September 2001 \$511,459,361

In five defaults since 1998, the SEHK proposed and the SFC approved increases in the \$8 million limit via payment of up to \$150,000 per claimant or if higher the claimant's proportional share of the \$8 million limit. The relevant defaults where we made payments during the six months ended 30 September 2001 were:

C.A. Pacific Securities Ltd.	\$1,713,036
Chark Fung Securities Co. Ltd.	\$1,641,656
Win Successful Securities Ltd.	\$6,130,085

**3. PROVISION FOR COMPENSATION**

	\$
Provision for compensation to be paid up to the \$8 million limit	
Balance as at 1 April 2000	26,658,386
Less: amount paid during the year ended 31 March 2001	(3,766,744)
unused provision reversed during the year	
ended 31 March 2001	(12,011,380)
	<hr/>
Balance as at 31 March 2001	10,880,262
Add: additional provision made during the six months	
ended 30 September 2001	1,624,124
Less: amount paid during the six months ended 30 September 2001	(6,130,085)
	<hr/>
Balance as at 30 September 2001	<u>6,374,301</u>



## Unified Exchange Compensation Fund

### Notes to the Condensed Financial Statements

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

#### 3. PROVISION FOR COMPENSATION - Cont'd

	\$
Provision for compensation to be paid in excess of the \$8 million limit	
Balance as at 1 April 2000	151,291,614
Less: amount paid during the year ended 31 March 2001	(59,879,092)
Add: additional provision made during the year ended 31 March 2001	20,987,247
	<hr/>
Balance as at 31 March 2001	112,399,769
Less: amount paid during the six months ended 30 September 2001	(3,354,692)
unused provision reversed during the six months ended 30 September 2001	(83,980,381)
	<hr/>
Balance as at 30 September 2001	<u>25,064,696</u>

We made provision for unprocessed claims in respect of five SEHK exchange participants for which the SEHK has published a notice calling for claims pursuant to Section 112 of the Securities Ordinance. The maximum liabilities of the Fund in respect of four of these default cases can exceed the normal \$8 million limit. In respect of three of these default cases, we revised the provision according to claims being processed. During the period, we also reversed provision for claim against two formerly reported default cases, which had been rejected by the SEHK.

#### 4. TRANSACTION LEVY

With effect from 1 September 2001, the Fund would receive transaction levy at 0.002% chargeable for every leviable transaction in the SEHK. During the six months ended 30 September 2001, the Fund recognised \$5,581,052 transaction levy (six months ended 30 September 2000: Nil).

#### 5. CONTINGENT LIABILITIES

As at the date of this report, the SEHK has received claims against eight exchange participants. They are subject to the normal \$8 million ceiling pursuant to Section 109 of the Securities Ordinance. The validity of these claims is under investigation. We have not made any provision for these claims. The maximum contingent liability of the Fund to these claims is \$64 million (As at 31 March 2001: \$96 million).



# Commodity Exchange Compensation Fund (the Fund)

## Report of the Futures Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the six-month period ended 30 September 2001.

### 1. ESTABLISHMENT OF THE FUND

Part VIII of the Commodities Trading Ordinance (Chapter 250) established the Fund.

### 2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 24 to 28.

### 3. MEMBERS OF THE COMMITTEE

The members of the Committee during the six months and up to the date of this report were:-

Mr. Mark Dickens  
Mr. Andrew Procter  
Mr. William D. Grossman  
Mr. Mark Ho  
Hon. Bernard Chan (appointed on 1 April 2001)

### 4. INTERESTS IN CONTRACTS

No contract of significance to which the Fund was a party and in which a Committee Member had a material interest, whether directly or indirectly, subsisted at the balance sheet date or at any time during the six months.

On behalf of the Committee

Mark Dickens  
Chairman

6 November 2001





# **Independent review report to the board of directors of Securities and Futures Commission (the SFC)**

**(Established in Hong Kong under the Securities and Futures Commission Ordinance)**

## **Introduction**

We have been instructed by the SFC to review the interim financial report for the six-month period ended 30 September 2001 of the Commodity Exchange Compensation Fund (the Fund) established under Section 77 of the Hong Kong Commodities Trading Ordinance set out on pages 24 to 28.

## **Directors' responsibilities**

The SFC is responsible for preparing an interim report of the Fund to match the requirements in the relevant provisions of The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and to comply with International Accounting Standard 34 "Interim financial reporting" issued by the International Accounting Standards Committee. The interim financial report is the responsibility of SFC, and has been approved by the Futures Compensation Fund Committee.

## **Review work performed**

We conducted our review in accordance with Statement of Auditing Standards 700 "Engagements to review interim financial reports" issued by the Hong Kong Society of Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

## **Review conclusion**

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six-month period ended 30 September 2001.

KPMG  
Certified Public Accountants  
Hong Kong, 6 November 2001



## Commodity Exchange Compensation Fund

### Income and Expenditure Account

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	Unaudited		Unaudited	
	Three Months Ended		Six Months Ended	
	30 Sep 2001	30 Sep 2000	30 Sep 2001	30 Sep 2000
	\$	\$	\$	\$
<b>Income</b>				
Investment Income	1,549,843	1,665,596	3,227,440	3,271,228
	-----	-----	-----	-----
<b>Expenses</b>				
Auditors' remuneration	10,350	9,720	20,700	19,440
Bank charges	13,498	7,167	25,767	17,712
Professional fees	14,218	3,000	28,437	6,000
Sundry expenses	-	600	900	600
	-----	-----	-----	-----
	38,066	20,487	75,804	43,752
	-----	-----	-----	-----
<b>Surplus</b>	1,511,777	1,645,109	3,151,636	3,227,476
<b>Accumulated surplus brought forward</b>	37,235,665	30,581,313	35,595,806	28,998,946
	-----	-----	-----	-----
<b>Accumulated surplus carried forward</b>	<u>38,747,442</u>	<u>32,226,422</u>	<u>38,747,442</u>	<u>32,226,422</u>

The notes on page 28 form an integral part of the condensed financial statements.



## Commodity Exchange Compensation Fund

### Balance Sheet

At 30 September 2001

(Expressed in Hong Kong dollars)

	Note	Unaudited At 30 Sep 2001 \$	Audited At 31 Mar 2001 \$
<b>Non-current assets</b>			
Held-to-maturity debt securities		43,061,766	43,070,728
<b>Current assets</b>			
Held-to-maturity debt securities		10,998,153	39,505,457
Interest receivable		1,017,283	881,261
Levy receivable		571,082	592,856
Bank fixed and call deposits		53,630,948	19,141,475
Cash at bank		12,463	7,710
		66,229,929	60,128,759
<b>Current liabilities</b>			
Accounts payable and accrued charges		231,836	252,672
		231,836	252,672
<b>Net current assets</b>		65,998,093	59,876,087
<b>Net assets</b>		109,059,859	102,946,815
Representing:			
<b><u>Compensation fund</u></b>			
Contributions from the HKFE	2	21,300,000	21,300,000
Contract levy	3	60,646,056	57,684,648
Accumulated Surplus		38,747,442	35,595,806
		120,693,498	114,580,454
Deduct: Compensation paid		(24,457,172)	(24,457,172)
Add: Recoveries		12,823,533	12,823,533
		109,059,859	102,946,815

The notes on page 28 form an integral part of the condensed financial statements.



## Commodity Exchange Compensation Fund

### Statement of Recognised Gains and Losses

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	<u>Note</u>	Unaudited Six Months Ended 30 Sep 2001 \$	Unaudited Six Months Ended 30 Sep 2000 \$
Net refund of contributions to HKFE		-	(700,000)
Contract levy	3	2,961,408	2,399,197
<b>Net gains not recognised in the income and expenditure account</b>		<hr/> 2,961,408	<hr/> 1,699,197
Surplus		3,151,636	3,227,476
<b>Total recognised gains</b>		<hr/> <u>6,113,044</u>	<hr/> <u>4,926,673</u>

The notes on page 28 form an integral part of the condensed financial statements.



## Commodity Exchange Compensation Fund

### Cash Flow Statement

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended 30 Sep 2001 \$	Unaudited Six Months Ended 30 Sep 2000 \$
<b>Net cash outflow from operating activities</b>	(96,640)	(71,490)
<b>Returns on investments</b> - interest received	3,107,684	3,186,463
<b>Investing activities</b>		
Held-to-maturity debt securities redeemed	28,500,000	5,500,000
Held-to-maturity debt securities bought	-	(7,968,000)
<b>Net cash inflow/(outflow) from investing activities</b>	28,500,000	(2,468,000)
<b>Financing</b>		
Net contribution refunded to HKFE	-	(700,000)
Contract levy received	2,983,182	2,400,553
<b>Net cash inflow from financing</b>	2,983,182	1,700,553
Increase in cash and cash equivalents	34,494,226	2,347,526
Cash and cash equivalents at beginning of the six months	19,149,185	12,290,428
<b>Cash and cash equivalents at end of the six months</b>	<u>53,643,411</u>	<u>14,637,954</u>
<b>Reconciliation of surplus for the six-month period to net cash outflow from operating activities:</b>		
Surplus	3,151,636	3,227,476
Investment Income	(3,227,440)	(3,271,228)
Decrease in accounts payable and accrued charges	(20,836)	(27,738)
<b>Net cash outflow from operating activities</b>	<u>(96,640)</u>	<u>(71,490)</u>

### Analysis of the balance of cash and cash equivalents:

	Unaudited At 30 Sep 2001 \$	Unaudited At 30 Sep 2000 \$
Cash at bank	12,463	13,774
Bank fixed and call deposits	53,630,948	14,624,180
	<u>53,643,411</u>	<u>14,637,954</u>



## Commodity Exchange Compensation Fund

### Notes to the Condensed Financial Statements

For the six months ended 30 September 2001

(Expressed in Hong Kong dollars)

#### 1. ACCOUNTING POLICIES

The interim financial report has been prepared in accordance with the requirements of the Main Board Listing Rules of the Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard 34 "Interim financial reporting" issued by the International Accounting Standards Committee.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2001 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

The same accounting policies adopted in the financial statements for the year ended 31 March 2001 have been applied to the interim financial report.

#### 2. CONTRIBUTIONS FROM HKFE

	\$
Balance as at 1 April 2000	21,800,000
Add: Contribution received during the year ended 31 March 2001	200,000
Deduct: Refunds to outgoing shareholders during the year ended 31 March 2001	(700,000)
Balance as at 31 March 2001	<u>21,300,000</u>
Add: Contributions received during the six months ended 30 September 2001	300,000
Deduct: Refunds to outgoing shareholders during the six months ended 30 September 2001	(300,000)
Balance as at 30 September 2001	<u><u>21,300,000</u></u>

#### 3. CONTRACT LEVY

During the six months ended 30 September 2001, the Fund recognised \$2,961,408 contract levy (six months ended 30 September 2000: \$2,399,197).