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*This is the Securities and Futures Commission's first Quarterly Report for the financial year from 1 April 2005 to 31 March 2006. The report aims to enhance the transparency and accountability of the Commission.*

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## Operations Highlights

1 April to 30 June 2005

### Financial Position

1. The SFC recorded a surplus of \$48.6 million in the first quarter, compared with a projected surplus of \$2.5 million in the approved budget. Reserves stood at \$908.6 million on 30 June.
2. Total revenue was \$164.6 million, 13% higher than the same quarter last year. Levy income, fees and charges income and investment income all increased owing to increased market activity and higher interest rates. Total expenditure (including depreciation) amounted to \$116 million, 8% lower than the approved budget of \$126 million.

### Regulatory Developments

3. We are working with the Government and HKEx to further develop the Government's proposed statutory framework to enhance listing regulation in light of the consultation responses.
4. We are reviewing the submissions to the consultation on proposed amendments to the Securities and Futures (Stock Market Listing) Rules to codify important listing requirements.
5. We concluded the consultation on a review of the disclosure of interests regime and are working with the Government to prepare the legislative amendments.
6. Amendments to the Securities and Futures (Investor Compensation - Levy) Rules were submitted to the LegCo for negative vetting. The amended rules are expected to commence operation in mid-October.
7. The SFC is consulting the public on a proposed set of specific entry criteria for and ongoing compliance obligations on sponsors to raise sponsor standards.
8. We consulted on proposed revisions to the Prevention of Money Laundering and Terrorist Financing Guidance Note.
9. We are finalising the amendments to the Codes on Takeovers and Mergers and Share Repurchases and aim to implement them in October.
10. The SFC assisted exchange participants in the appointment of an insurance broker to arrange and administer better fidelity insurance schemes for this year.
11. We amended the Code on REITs to allow SFC-authorized REITs to invest in overseas properties and to introduce other facilitative amendments.
12. We issued a consultation paper on proposals to revise the Hedge Funds Guidelines in light of market developments.

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13. We worked closely with HKMA and HKEx to facilitate the launch of two index funds under the Asia Bond Fund 2 framework.
  14. We worked with HKEx to ensure the successful launch of the FTSE/Xinhua China 25 Index Futures and Options Contracts.
  15. The Code on Unit Trusts and Mutual Funds was amended in April to allow SFC-authorized funds to invest in REITs that are listed overseas.
  16. We are working with the fund industry on a long-term approach to UCITS III applications.
  17. The SFC approved HKEx's rule amendments on the reduction of minimum spreads for shares trading above \$30. The new spreads came into effect on 4 July.
  18. As a member of the eXtensive Business Reporting Language (XBRL) Preparatory Working Group, we are formulating a roadmap for the development of XBRL in Hong Kong.

### **Supervisory and Enforcement Actions**

19. During the quarter, the SFC had 18 successful prosecutions. We took disciplinary action against 14 licensees for various regulatory breaches.
20. We imposed licensing conditions on a brokerage firm in June to help it adopt prudent business practice and strengthen its risk management.

### **Others**

21. The SFC jointly produced a radio drama series, "The Star Analysts' Fans Family", with Radio Television Hong Kong to arouse investors' awareness of the issue of conflicts.
22. We started a weekly FAQ column in the freely distributed Metropolis Daily in June.
23. We launched a new round of investor education workshops for teachers and received a record 1,950 enrolments.
24. The SFC's Annual Report 2004-2005 was tabled at the LegCo on 11 May.
25. We signed Letters of Intent with our counterparts in Sri Lanka, India, Guernsey and Malaysia on the enhancement of regulatory co-operation relating to investment funds.
26. We signed a Statement of Intent with the Financial Services Agency of Japan on co-operation, consultation and the exchange of information and exchanged Side Letters with the Monetary Authority of Macau under an existing MOU on exchange of information.
27. An SFC delegation participated in the IOSCO Annual Conference in Colombo, Sri Lanka in April and promoted Hong Kong, the host city of the Annual Conference in 2006.
28. The SFC jointly organised a securities regulation conference in Hong Kong in May with the Financial Stability Institute of the Bank for International Settlements for 30 central bankers from across the region.

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29. Mr Martin Wheatley was appointed as an Executive Director and Dr York Liao was re-appointed as a Non-Executive Director. Mr Henry Chan, Mr Jack Maisano, Mr Peter Sullivan, Ms Ada Tse and Mr Yip Lai-shing were appointed as new members of the Advisory Committee.



## Review of Operations

1 April to 30 June 2005

This is the Securities and Futures Commission's first Quarterly Report for the financial year starting 1 April 2005.

During the quarter, the US Fed raised the Fed Funds Target Rate twice for a total of 50 basis points. The Fed indicated that rate hikes would continue in a measured pace. Oil prices also surged to their record highs at quarter-end. The stock markets ended mixed, with the Dow slipping 2.2% and the S&P and NASDAQ rising 0.9% and 2.9% respectively. European markets outperformed their US counterparts, with the DAX, CAC and FTSE rising 5.5%, 4.0% and 4.5% respectively.

The Mainland markets slid to eight-year lows. The Mainland authorities launched a pilot scheme to float the non-tradable shares of 46 listed companies. Concerns over the overhang of stocks weighed down the markets. The Shanghai Composite Index and Shenzhen Composite Index fell 8.5% and 12.1% respectively.

In Hong Kong, speculation over a RMB revaluation cooled off slightly and HKMA's refinements to the Linked Exchange Rate System triggered interest rate hikes and funds outflow. However, the positive performance of overseas markets lent support to local stocks. The property stocks also pushed the markets higher on strong sales of residential projects. The HSI advanced 5.1% to close at 14,201 on 30 June, while the H-shares and red chips indices rose 1.4% and 7.8% respectively.

Trading was less active than the previous quarter. The average daily turnover on the Main Board declined 16.5% to \$15.3 billion. The average daily turnover of HSI constituent stocks dropped 13.9% to \$6.5 billion. The average daily turnover of H-shares dropped 6.5% to \$3.1 billion and red chips' turnover fell 19.9% to \$2.1 billion.

On the Growth Enterprise Market, the S&P/HKEx GEM Index fell 4% during the quarter to close at 899. Average daily turnover was \$82 million, representing a 10.1% increase from the previous quarter.

IPO activities on the Main Board became more active during the quarter with 14 IPOs, compared with five in the previous quarter. Funds raised through IPOs totalled \$54.3 billion, almost eight times higher than the previous quarter. This was the highest record since the second quarter of year 2000 during which \$70.3 billion was raised. There were no IPOs on GEM.

At the end of June, the open interest of HSI futures was 122,315 contracts, 28.7% higher than the end-March level. The open interest of the Hang Sang Index Options and the H-shares Index Options were 162,811 contracts and 33,135 contracts respectively, representing increases of 20.5% and 37.2% respectively from three months earlier.



## Financial Highlights<sup>1</sup>

Compared to the same quarter last year, total revenue increased 13% to \$164.6 million. Levy income increased 14% to \$109.7 million as the average daily stock market turnover rose 11% to \$16.5 billion<sup>2</sup>. Fees and charges income also increased 14% to \$45.9 million owing to receipt of more disclosure-related waiver fees and licensing-related annual and application fees. Investment income was up 33% to \$6.9 million because of higher interest rates.

First quarter expenditure (including depreciation) amounted to \$116 million, 8% lower than the approved budget of \$126 million and 15% higher than the same quarter last year. The increase was mainly because no provision for staff variable pay was made in last year's first quarter expenditure. If a provision had been made last year, expenditure for the quarter would only be 6% higher than that of the same period last year. This moderate increase was mainly attributable to an increase in staff number and hence 5% higher staff costs. The total number of staff at the end of June 2005 was 436, comprising 392 regular staff and 44 temporary staff. There were 412 staff a year ago.

As a result, the Commission recorded a surplus of \$48.6 million in the first quarter, compared to the projected surplus of \$2.5 million in the approved budget and the \$44.2 million surplus recorded in the same period last year.

At the end of June, reserves stood at \$908.6 million, equivalent to 1.8 times the approved annual operating expenditure (including depreciation) of \$508 million.

## Securities and Futures Ordinance (SFO)

We continued the maintenance and update of the SFO in light of market developments.

We are amending various provisions of the SFO, including the amendments required to implement the Government's proposed statutory framework to enhance listing regulation. Meanwhile, we are reviewing the submissions to the consultation on proposed amendments to the Securities and Futures (Stock Market Listing) Rules to codify important listing requirements and are working with the Government and HKEx to develop the proposals further in light of the consultation responses.

The consultation conclusions paper on a review of the disclosure of interests regime under Part XV of the SFO was issued during the quarter. With general market support, the SFC recommended adoption of most of the proposals contained in the January consultation paper. We are working with the Government to prepare the legislative amendments. We will also be revising the Outline on Part XV and the various disclosure forms and notices. However, as there was no consensus on the disclosure of security interests,

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<sup>1</sup> We have consolidated the financial results of Investor Compensation Company Limited in this financial report.

<sup>2</sup> For income purpose, the turnover figure includes the amount of new fund raisings, which also attract transaction levy.



the SFC will set up a working group comprising market participants, investors and representatives of the securities lending industry to examine if there are better alternatives.

Consultation on the proposed amendments to Schedule 5 to the SFO ended in the previous quarter. The proposals aimed to fine-tune the legal definitions of certain regulated activities to accommodate the latest market development, including extending the definition of "asset management" to include real estate investment scheme management. We will issue the consultation conclusions paper in the near future.

Amendments to the Securities and Futures (Investor Compensation - Levy) Rules, which provide for an automatic investor compensation levy triggering and suspension mechanism, were gazetted in June and submitted to the LegCo for negative vetting in July. It is expected that the Amendments Rules will commence operation in mid-October.

### **Raising Market Standards**

The SFC in June consulted the public on a proposed set of specific entry criteria for and ongoing compliance obligations on sponsors. It is the second part of a two-stage initiative adopted by the SFC and HKEx to raise sponsor standards. HKEx concluded the first stage with Listing Rules amendments and the introduction of the Practice Notes on Due Diligence. Upon completion of this second stage, we will have a specific regulatory regime for sponsors, including a set of clear benchmarks to assess the compliance standards of sponsors. The consultation will end on 31 August.

The SFC issued in April a consultation paper on proposed revisions to the Prevention of Money Laundering and Terrorist Financing Guidance Note in order to bring our regulatory requirements in line with international standards. The consultation ended in June and we are analysing the responses.

The consultation on a review of the Codes on Takeovers and Mergers and Share Repurchases closed in the previous quarter. The Takeovers Panel met in June to discuss the responses received and finalise the proposals. It also approved a consultation conclusions paper which includes details of the amendment to the Codes. It is expected that the consultation conclusions paper will be issued in August and the amendments will come into effect on 1 October.

The guidelines to address analyst conflicts of interest came into effect on 1 April. The guidelines aim to remove, reduce and manage conflicts faced by analysts and their firms. The SFC continues to monitor licensees' compliance with the requirements.

### **Partnership with the Industry**

The number of intermediaries licensed by or registered with the SFC steadily increased by 4.4% from 22,810 as at 31 March to 23,805 as at 30 June.

Through a rigorous tender process assisted by the SFC, an industry working group represented by

various brokers' associations and brokerage houses appointed a new insurance broker to arrange and administer the fidelity insurance schemes for the scheme year that started on 1 April 2005. Apart from better coverage, stock exchange participants are paying 17% less and futures exchange participants 29% less in gross premiums compared to the previous year.

During the quarter, we met with Alternative Investment Management Association, Hong Kong Chapter and certain major prime brokers to get a better understanding of the hedge fund industry and also clarified with them our licensing process and requirements. We have also set up a dedicated team to deal with licence applications and enquiries of managers for real estate investment trusts (REITs) to facilitate their participation in this new market.

Statistical Information and Financial Position of the Securities Industry		
	As at 30 Jun 2005	As at 30 Jun 2004
Total number of securities dealers and securities margin financiers	634	667
Total number of active cash clients (Note 1)	629,960	666,621
Total number of active margin clients (Note 1)	76,332	75,419
<b>Balance Sheet (Note 2)</b>	<b>(\$ Million)</b>	<b>(\$ Million)</b>
Cash in hand and at bank (Note 3)	101,286	99,811
Amounts receivable from margin clients (Note 4)	17,333	16,008
Amounts receivable from clients and other dealers arising from dealing in securities	110,562	77,496
Proprietary positions	85,055	52,392
Other assets	73,456	51,362
<b>Total assets</b>	<b>387,692</b>	<b>297,069</b>
Amounts payable to clients and other dealers arising from dealing in securities	168,770	124,815
Total borrowings from financial institutions	59,880	41,642
Short positions held for own account	26,717	20,322
Other liabilities	54,147	36,183
Total shareholders' fund (Note 5)	78,178	74,107
<b>Total liabilities and shareholders' fund</b>	<b>387,692</b>	<b>297,069</b>

Note 1: Active clients are clients for whom the licensed corporation is required to prepare and deliver monthly statement of accounts in respect of the relevant reporting month in accordance with Securities and Futures (Contracts Notes, Statements of Account and Receipts) Rules.

Note 2: The significant increases in the various items of the balance sheet are mainly attributable to the increase in market turnover during the period.

Note 3: Cash in hand and at bank includes trust monies held on behalf of clients amounting to \$46,037 million (30/6/2004: \$43,019 million).

Note 4: Average collateral coverage (the number of times the aggregate market value of securities collateral deposited by clients covers the amounts receivable from margin clients on a given date on an industry-wide basis):

<u>As at 30 Jun 2005</u>	<u>As at 30 Jun 2004</u>
4.2	4.3

Note 5: The value of shareholder's fund includes value of redeemable shares.

Sources: Monthly Financial Returns submitted in accordance with the Securities and Futures (Financial Resources) Rules by securities dealers and securities margin financiers.



## Facilitating Market Development

The Consultation on Draft Practice Note on Overseas Investments by SFC-authorized REITs was concluded in June. With unanimous market support, the Code on REITs has been amended to allow SFC-authorized REITs to invest in real estate around the world. The Practice Note provides specific guidance in this respect. Other amendments included the relaxation of the gearing ratio to 45% of the gross asset value of a REIT and the acceptance of special product features by the SFC on a case-by-case basis.

In May, the SFC issued a consultation paper on proposals to revise the Hedge Funds Guidelines. The SFC proposed to strengthen the assessment criteria of hedge fund managers and provide greater flexibility in recognising the experience of their key personnel; require additional disclosure by hedge funds to enhance transparency; and codify existing practices of the SFC in authorising hedge funds. The consultation ended on 30 June. We are considering the 11 responses received and expect to issue the consultation conclusions paper and the revised Guidelines by the second half of the year.

The SFC worked closely with HKMA and HKEx to facilitate the launch of two exchange traded funds (ETFs) under the Asian Bond Fund 2 (ABF2). Under the ABF2 framework, there are eight single market bond index tracking funds and a pan Asia bond index tracking fund investing in sovereign and quasi sovereign local currency bonds. The ABF Hong Kong Bond Index Fund and the ABF Pan Asia Bond Index Fund have been authorised by the SFC and were listed on HKEx in June and July respectively.

The FTSE/Xinhua China 25 Index Futures and Options Contracts started trading in May. The underlying FTSE/Xinhua China 25 Index tracks the performance of the 25 largest and most liquid H-shares and red chips. In the meantime, the Hang Seng FTSE/Xinhua China 25 Index ETF was launched to track the FTSE/Xinhua China 25 Index. The SFC worked closely with HKEx to ensure the successful launch of these products.

Following market consultation in the previous quarter, the Code on Unit Trusts and Mutual Funds was amended in April to allow SFC-authorized funds to invest in REITs listed on a stock exchange anywhere in the world. This helps broaden the investment choice of SFC-authorized schemes.

The SFC continued to monitor the latest regulatory developments relating to the Undertakings for Collective Investment in Transferable Securities (UCITS) III, the new regulations issued by the European Union Commission that govern funds domiciled in the EU states. By the end of June, the SFC has authorised 544 UCITS III funds, representing over 75% of the applications received. We are working with the fund industry on a long-term approach to UCITS III applications.



Number of SFC Authorised Collective Investment Schemes			
	30 Jun 2005	31 Mar 2005	30 Jun 2004
Unit trusts and mutual funds	1,943	1,942	1,927
Investment-linked assurance schemes	182	177	165
Pooled retirement funds	37	37	37
MPF master trust / industry schemes	45	45	46
MPF pooled investment funds (Note 1)	275	274	255
Other schemes (Note 2)	87	78	47
<b>Total</b>	<b>2,569</b>	<b>2,553</b>	<b>2,477</b>
Note 1: There are 118 funds included in this category that are offered both as retail unit trusts as well as pooled investment funds for MPF purpose.			
Note 2: The schemes included equity-linked deposits.			

In May, the SFC approved HKEx's rule amendments on the reduction of minimum spreads for shares trading above \$30. The amendments enhance the competitiveness, efficiency and liquidity of the market. The new spreads came into effect on 4 July.

During the quarter, an industry-wide Preparatory Working Group (PWG), of which the SFC is the convenor and a member, was formed to promote the adoption of the eXtensible Business Reporting Language (XBRL) in Hong Kong. XBRL is an evolving global standard for faster and more accurate electronic communication of business and financial data. The PWG comprises a Steering Committee and three sub-groups. They are working to formulate a roadmap for the development of XBRL in Hong Kong.

### Enforcement and Regulatory Actions

In April-June, the SFC successfully prosecuted 18 people and companies - for market manipulation, failure to attend SFC's investigation interviews, disclosure of interests breaches, unlicensed activities, failure to report liquid capital deficiencies, and short selling. We offered no evidence against one entity.

Separately, the Court of First Instance dismissed Ms Tsang Wai Lin's appeal against conviction in April. Tsang had earlier been convicted after trial and fined \$60,000 for unlicensed leveraged foreign exchange trading.

During the quarter, the SFC took disciplinary action against 14 licensees for various regulatory breaches:

- *Settlement without formal sanction* - Gain Asset Management Limited consented to pay \$500,000 to settle the SFC's disciplinary action against it. Gain Asset in 2003 pledged client securities collateral with other licensed corporations while not licensed to do so. It also failed to maintain the required liquid capital while obtaining loans for an IPO.
- *Settlement with sanctions* - Berich Brokerage Limited agreed to pay \$1.4 million, reimburse the SFC's legal costs and expenses incurred in the disciplinary proceedings, and be publicly reprimanded.

Its licensed representative and two of its responsible officers were suspended for two years, one month and three months respectively. Berich window-dressed two Financial Resources Rules (FRR) returns in 2002, failed to comply with its undertakings to the SFC and had internal control failures.

- *Suspensions* - The Securities and Futures Appeals Tribunal affirmed the SFC's decision to suspend a licensed representative for account opening failings and aiding and abetting unlicensed dealing, but reduced the two-month suspension to five weeks considering his extraordinary circumstances. Two other licensed individuals were suspended for five months and three years respectively for providing misleading statements to the SFC and negligence in conducting due diligence and serious misconduct in selling investment products.
- *Reprimands and fines* - Two licensed corporations were reprimanded and fined for breaching the FRR while a third was reprimanded and fined for breaching the Client Identity Rule Policy and failing to comply with an undertaking given to the SFC. A licensed representative was reprimanded and fined for assisting an unlicensed person to conduct regulated activities.
- *Reprimands* - A licensed corporation was reprimanded for being negligent in conducting due diligence and for misconduct in selling investment products. A responsible officer was reprimanded for breaching the FRR.

<b>Statistics of Enforcement Actions</b>			
	<b>Apr - Jun 2005</b>	<b>Jan - Mar 2005</b>	<b>Apr - Jun 2004</b>
Successful prosecutions	18	16	18
SFC licensees disciplined (including settlement cases)	14	23	15
Warning letters issued (Note 1)	88	44	80
Cases under investigation (Notes 2 and 3)	494	494	519
Disciplinary inquiries in progress (Note 3)	108	112	105
Note 1: The increase from the previous quarter was mainly owing to disclosure of interests breaches.			
Note 2: Some cases are ongoing investigations from the previous quarter.			
Note 3: Number of cases as at end of quarters.			

Separately, having carefully considered the circumstances and assessed all relevant information before us, we proactively exercised our power under section 116(6) of the Securities and Futures Ordinance to impose licensing conditions on REXCAPITAL Securities Limited in June to help the firm adopt prudent business practice and strengthen its risk management.

### **Strengthening Communication with Investors and Other Stakeholders**

"The Star Analysts' Fans Family", a 10-episode radio drama jointly produced by the SFC and the Radio Television Hong Kong (RTHK), was aired on RTHK from April to June. The series aimed to arouse investors' awareness of the potential conflicts stock analysts and their firms may face, and to remind investors to look beyond investment recommendations. In tandem with the show, educational articles were published in the Apple Daily and the Hong Kong Economic Times.



We have been running a weekly FAQ column in the freely distributed Metropolis Daily since June. Topics discussed in June included IPOs, distribution of dividends and shareholders' voting rights.

A new round of investor education teachers workshops commenced in June. The 16 teachers workshops covered a wide range of investment products and services and included a new Personal Financial Planning module. We received a record 1,950 enrolments from secondary school teachers of Economics, Accounting, Commerce and related subjects, as well as vocational education teachers.

During the quarter, our electronic Investor Resources Centre (eIRC) introduced new interactive games on derivative warrants, hedge fund, parallel trading and stock transaction costs, and an online article series about consumerism in engaging investment advisory services.

We also talked to employees of the Consumer Council and the Estate Agent Authority, members of the Hong Kong Chinese Civil Servants' Association, secondary school students, retiring civil servants as well as industry practitioners on a wide range of investment related subjects. These seminars attracted 1,100 attendants.

The educational Dr Wise's Column discussed online investing, fund investing and leveraged forex trading during the quarter. We continued to receive reports on boiler rooms and phishes and added 29 entities to the SFC Alert List. We also issued a press release in June to warn the public of an active boiler room in Hong Kong.

<b>Statistics of Investor Enquiries and Public Complaints</b>			
	<b>Apr - Jun 2005</b>	<b>Jan - Mar 2005</b>	<b>Apr - Jun 2004</b>
Enquiries	1,159	1,110	1,276
Complaints	332	267	342

The SFC's Annual Report 2004-2005 was tabled at the LegCo on 11 May, six weeks after the financial year-end.

To keep the public informed of our work and enforcement actions, we continued to publish our bi-monthly newsletter SFC Alert, the monthly SFC Enforcement Reporter, and the spring issue of Quarterly Bulletin. All these publications are available on the SFC website.

### **International Co-operation and External Relations**

During the quarter, the SFC made good headway in strengthening co-operation with several counterparts. We signed Letters of Intent (LOIs) with the Securities and Exchange Commission of Sri Lanka, the Securities and Exchange Board of India, and the Financial Services Commission of Guernsey. The LOIs aim to enhance co-operation with a view to working towards the mutual recognition of investment products authorised in their respective jurisdictions for cross-border distribution. In July, we signed a similar LOI with Malaysia's Securities Commission.



In May, we signed a Statement of Intent (SOI) with the Financial Services Agency of Japan on co-operation, consultation and the exchange of information. We also exchanged Side Letters with the Monetary Authority of Macau (AMCM) under an existing Memorandum of Understanding (MOU) on mutual assistance and exchange of information to specify what information will be provided and how it will be provided under the MOU.

In April, I led a delegation to the 30th Annual Conference of the International Organization of Securities Commissions (IOSCO) in Colombo, Sri Lanka. The conference was attended by about 500 participants from around the world. As Hong Kong will host the 31st Annual Conference next year, we set up an exhibition booth in the conference venue to publicise the 2006 event and invite delegates to Hong Kong.

The Colombo Annual Conference was a landmark meeting, as IOSCO adopted a timetable by which all member regulators, which are not already signatories to the MOU, will be asked to meet this benchmark by 1 January 2010. By this date, all member regulators should have applied for and been accepted as signatories under the IOSCO MOU, or have expressed a commitment to seek legal authority to enable them to become signatories.

In May, the SFC jointly organised a conference in Hong Kong with the Financial Stability Institute of the Bank for International Settlements on "What Banking Supervisors Need to Know About the Securities Industry". The conference attracted some 30 central bank officials from across the region. Senior overseas securities regulators joined SFC colleagues as speakers.

During the quarter, we welcomed officials and private sector visitors from nine Mainland delegations and one Taiwanese delegation.

### **Looking Ahead**

In June, the independent Process Review Panel (PRP) published its annual report for 2004. It reviewed 47 completed cases and procedures relating to various areas of our work. The PRP found that in general, the SFC had been adhering to its established internal procedures in its decisions and actions. The SFC welcomed the findings. We have adopted a number of specific recommendations of the PRP. Where there are difficulties in adopting or accepting in full the PRP's recommendations, we have carefully explained to the PRP the reasons for not adopting them. We look forward to continuing our co-operation with the PRP in its fifth year of work.

In May, the Financial Secretary appointed Mr Martin Wheatley, formerly Deputy Chief Executive of the London Stock Exchange, as the SFC's Executive Director (Supervision of Markets) for three years until 5 June 2008. The Financial Secretary also re-appointed Dr York Liao as a Non-Executive Director for two years to 25 May 2007. I warmly welcome Mr Wheatley and look forward to working closely with both of them.

I also welcome the appointment of Mr Henry Chan, Mr Jack Maisano, Mr Peter Sullivan, Ms Ada Tse, and



Mr Yip Lai-shing as new members of the SFC Advisory Committee for a two-year term to 31 May 2007, and thank Mr Stephen Hui, Mr Roger Luk and Dr Eden Woon, who retired in May, for their valuable contribution.

In April, the Commission Possible Volunteers Group, our voluntary team, organised a visit to the Hong Kong Heritage Museum for 15 elderly people and their family. A total of 26 volunteers, including staff's family and friends, joined the event.

Based on the current information and by managing our budget prudently, we expect a surplus in the second quarter.

Andrew Sheng  
Chairman

12 August 2005

# Securities and Futures Commission

## Consolidated Income and Expenditure Account

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	<u>Note</u>	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Income</b>			
Levies		109,665	95,807
Fees and charges		45,859	40,230
Investment income		6,890	5,164
Recoveries from Investor Compensation Fund		789	959
Other income		1,369	2,986
		<u>164,572</u>	<u>145,146</u>
		-----	-----
<b>Expenses</b>			
Staff costs and directors' emoluments		91,558	78,180
Premises			
rent		5,358	4,532
other		3,439	2,794
Other expenses		11,118	10,754
		<u>111,473</u>	<u>96,260</u>
Depreciation		<u>4,539</u>	<u>4,728</u>
		<u>116,012</u>	<u>100,988</u>
		-----	-----
<b>Surplus</b>	2	<u>48,560</u>	<u>44,158</u>

We have not prepared a separate statement of changes in equity as the surplus for the quarter would be the only component of such a statement.

The notes on pages 18 to 20 form part of the condensed consolidated financial statements.

# Securities and Futures Commission

## Consolidated Balance Sheet

At 30 June 2005

(Expressed in Hong Kong Dollars)

	Note	Unaudited At 30 Jun 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Non-current assets</b>			
Fixed assets		24,166	25,258
Held-to-maturity debt securities	3	<u>534,347</u>	<u>550,407</u>
		<u>558,513</u>	<u>575,665</u>
<b>Current assets</b>			
Held-to-maturity debt securities	3	370,944	294,398
Bank deposits		52,202	69,656
Debtors, deposits and prepayments		67,752	58,181
Cash at bank and in hand		<u>2,137</u>	<u>1,692</u>
		<u>493,035</u>	<u>423,927</u>
<b>Current liabilities</b>			
Fees received in advance		35,906	36,675
Creditors and accrued charges		<u>37,167</u>	<u>30,765</u>
		<u>73,073</u>	<u>67,440</u>
		-----	-----
<b>Net current assets</b>		<u>419,962</u>	<u>356,487</u>
		-----	-----
<b>Total assets less current liabilities</b>		978,475	932,152
<b>Non-current liabilities</b>	4	<u>69,830</u>	<u>72,067</u>
<b>Net assets</b>		<u>908,645</u>	<u>860,085</u>
		-----	-----
<b>Funding and reserves</b>			
<b>Initial funding by Government</b>		42,840	42,840
<b>Accumulated surplus</b>	2	<u>865,805</u>	<u>817,245</u>
		<u>908,645</u>	<u>860,085</u>
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The notes on pages 18 to 20 form part of the condensed consolidated financial statements.

# Securities and Futures Commission

## Balance Sheet

At 30 June 2005

(Expressed in Hong Kong Dollars)

	Note	Unaudited At 30 Jun 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Non-current assets</b>			
Fixed assets		23,976	25,012
Held-to-maturity debt securities	3	<u>534,347</u>	<u>550,407</u>
		<u>558,323</u>	<u>575,419</u>
<b>Current assets</b>			
Held-to-maturity debt securities	3	370,944	294,398
Bank deposits		52,202	69,656
Debtors, deposits and prepayments		67,344	57,845
Cash at bank and in hand		<u>1,116</u>	<u>945</u>
		<u>491,606</u>	<u>422,844</u>
<b>Current liabilities</b>			
Fees received in advance		35,906	36,675
Creditors and accrued charges		<u>35,554</u>	<u>29,451</u>
		<u>71,460</u>	<u>66,126</u>
<b>Net current assets</b>		<u>420,146</u>	<u>356,718</u>
<b>Total assets less current liabilities</b>		978,469	932,137
<b>Non-current liabilities</b>	4	<u>69,824</u>	<u>72,052</u>
<b>Net assets</b>		<u>908,645</u>	<u>860,085</u>
<b>Funding and reserves</b>			
Initial funding by Government		42,840	42,840
Accumulated surplus	2	<u>865,805</u>	<u>817,245</u>
		<u>908,645</u>	<u>860,085</u>

The notes on pages 18 to 20 form part of the condensed consolidated financial statements.

## Securities and Futures Commission

### Consolidated Cash Flow Statement For the quarter ended 30 June 2005 (Expressed in Hong Kong dollars)

	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Cash flows from operating activities</b>		
Surplus	48,560	44,158
Adjustments for :		
Depreciation	4,539	4,728
Investment income	(6,890)	(5,164)
Profit on sale of fixed assets	-	(4)
	<u>46,209</u>	<u>43,718</u>
(Increase) / decrease in debtors, deposits and prepayments	(8,049)	3,757
Increase in creditors and accrued charges	7,112	414
Decrease in fees received in advance	(769)	(4,820)
(Decrease) / increase in non-current liabilities	<u>(2,237)</u>	<u>4,638</u>
<b>Net cash generated from operating activities</b>	<u>42,266</u>	<u>47,707</u>
<b>Cash flows from investing activities</b>		
Interest received	7,655	5,667
Held-to-maturity debt securities bought	(134,377)	(177,534)
Held-to-maturity debt securities redeemed	71,604	141,500
Fixed assets bought	(4,157)	(1,734)
Fixed assets sold	-	20
<b>Net cash used in investing activities</b>	<u>(59,275)</u>	<u>(32,081)</u>
<b>Net (decrease) / increase in cash and cash equivalents</b>	(17,009)	15,626
<b>Cash and cash equivalents at beginning of the quarter</b>	<u>71,348</u>	<u>77,963</u>
<b>Cash and cash equivalents at end of the quarter</b>	<u>54,339</u>	<u>93,589</u>

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

	Unaudited At 30 Jun 2005 \$'000	Unaudited At 30 Jun 2004 \$'000
Bank deposits	52,202	91,261
Cash at bank and in hand	<u>2,137</u>	<u>2,328</u>
	<u>54,339</u>	<u>93,589</u>

# Securities and Futures Commission

## Notes to the Condensed Consolidated Financial Statements

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

### 1. BASIS OF PREPARATION

We have prepared the interim financial report in accordance with International Accounting Standard 34 "Interim financial reporting" adopted by the International Accounting Standards Board.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the SFC's statutory accounts for that financial year but is derived from those financial statements.

We consolidated the financial results of Investor Compensation Company Limited in the SFC's condensed financial statements made up to 30 June 2005. We eliminate all material intragroup balances and transactions in preparing the condensed consolidated financial statements. We have applied the same accounting policies adopted in the consolidated financial statements for the year ended 31 March 2005 to the interim financial report.

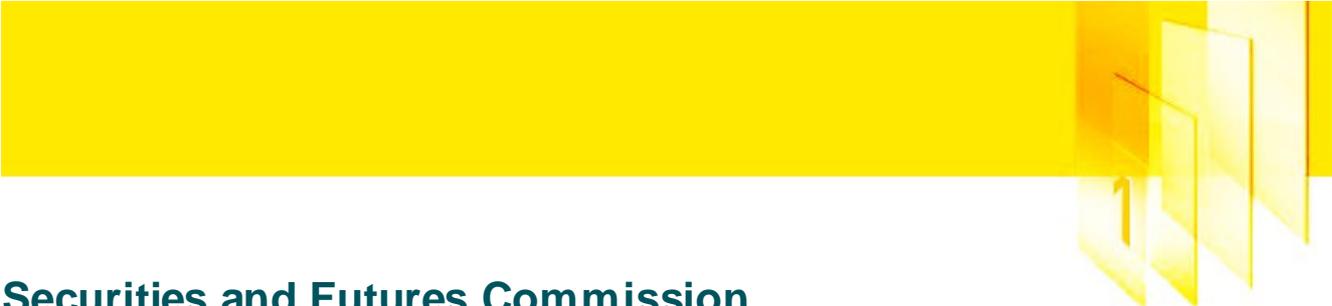
There were no significant changes in the operation of the SFC for the quarter ended 30 June 2005.

### 2. ACCUMULATED SURPLUS

#### The Group and the SFC

Movements of accumulated surplus during the quarter are as follows :

	<u>Unaudited</u> \$'000
Balance at 31 March 2005	817,245
Surplus for the quarter	48,560
	<hr/>
Balance at 30 June 2005	<u>865,805</u>



## Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

### 3. HELD-TO-MATURITY DEBT SECURITIES

#### The Group and the SFC

As of 30 June 2005, the total market value of held-to-maturity debt securities amounted to \$900,411,000 (31 March 2005 : \$837,775,000), which was below the total carrying cost of \$905,291,000 (31 March 2005 : \$844,805,000).

### 4. NON-CURRENT LIABILITIES

#### The Group and the SFC

Non-current liabilities represent deferred lease incentives and provision for premises reinstatement cost. Deferred lease incentives consist of incentives granted by our landlord in connection with the lease of our office premises. We recognise the deferred lease incentives in our income and expenditure account on a straight line basis over the lease period from 2004 to 2013 as an integral part of the lease expense.

### 5. AGEING ANALYSIS OF DEBTORS AND CREDITORS

There was no material debtor balance and creditor balance included in "debtors, deposits and prepayments" and "creditors and accrued charges" respectively as at 30 June 2005. Therefore we do not provide an ageing analysis of debtors and creditors.

### 6. EXCHANGE FLUCTUATION

All our balance sheet items are denominated in either United States dollars or Hong Kong dollars, and, as a result, we are not exposed to significant exchange rate risk.



## Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

### 7. INVESTMENTS IN SUBSIDIARIES

The SFC formed FinNet Limited (FinNet) on 6 November 2000 with an authorised share capital of \$10,000 and issued share capital of \$2 and Investor Compensation Company Limited (ICC) on 11 September 2002 with an authorised share capital of \$1,000 and issued share capital of \$0.2. Both FinNet and ICC are incorporated in Hong Kong.

The objective of FinNet is to operate an electronic network to facilitate payment and delivery transactions and interconnection of all financial institutions and financial entities in Hong Kong.

The objective of ICC is to facilitate the administration and management of the Investor Compensation Fund established under the Securities and Futures Ordinance.

Both companies are wholly owned subsidiaries of the SFC. As at 30 June 2005, the investments in subsidiaries, which is stated at cost less any impairment losses, amounted to \$2.2. The balance is too small to appear on the balance sheet which is expressed in thousands of dollars.

FinNet has not commenced operation. The balance sheet of FinNet as at 30 June 2005 and the income and expenditure account for the quarter then ended were immaterial. Therefore, we have not accounted for its result in the condensed consolidated financial statements.

The financial statements of ICC are included in the condensed consolidated financial statements.



## Investor Compensation Fund (the Fund)

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

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the quarter ended 30 June 2005.

#### 1. ESTABLISHMENT OF THE FUND

Part XII of the Securities and Futures Ordinance (Chapter 571) established the Fund on 1 April 2003.

#### 2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 22 to 26.

#### 3. MEMBERS OF THE COMMITTEE

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

Mr. Martin Wheatley	[appointed on 21 June 2005]
Mr. Peter Au-Yang	[appointed on 1 April 2005 and resigned on 20 June 2005]
Mr. Gerald Greiner	
Mrs. Alexa Lam	
Ms. Anna H.Y. Wu, SBS, JP	
Mr. Eddy Fong, SBS, JP	[appointed on 21 June 2005]

#### 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 quarter.

On behalf of the Committee

Martin Wheatley  
Chairman

4 August 2005

## Investor Compensation Fund

### Income and Expenditure Account

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Income</b>			
Net investment income		23,661	402
Levy - securities		41,004	35,892
Levy - futures / option contracts		3,559	3,422
		<u>68,224</u>	<u>39,716</u>
		-----	-----
<b>Expenses</b>			
ICC expenses	2	789	959
Auditors' remuneration		15	6
Bank charges		428	26
Professional fees		560	5
Exchange difference		3,033	5
Sundry expenses		1	1
		<u>4,826</u>	<u>1,002</u>
		-----	-----
<b>Surplus</b>		63,398	38,714
<b>Accumulated surplus brought forward</b>		353,479	154,609
		<u>416,877</u>	<u>193,323</u>
<b>Accumulated surplus carried forward</b>		<u>416,877</u>	<u>193,323</u>

The notes on page 26 form part of the condensed financial statements.

# Investor Compensation Fund

## Balance Sheet

At 30 June 2005

(Expressed in Hong Kong dollars)

	Unaudited At 30 Jun 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Current assets</b>		
Debt securities	1,272,364	1,182,665
Equity securities	124,929	122,409
Other receivable	-	384
Interest receivable	14,172	13,731
Due from ICC	1,595	1,111
Levy receivable from the SEHK	16,763	16,434
Levy receivable from the HKFE	1,259	1,283
Fixed and call deposits with banks	89,117	81,663
Cash at bank	<u>232</u>	<u>37,295</u>
	1,520,431	1,456,975
<b>Current liabilities</b>		
Accounts payable and accrued charges	<u>876</u>	<u>818</u>
<b>Net current assets</b>	<u>1,519,555</u>	<u>1,456,157</u>
<b>Net assets</b>	<u>1,519,555</u>	<u>1,456,157</u>
Representing:		
<b>Compensation fund</b>		
Contributions from UECF	994,718	994,718
Contributions from CECF	107,960	107,960
Accumulated surplus	<u>416,877</u>	<u>353,479</u>
	<u>1,519,555</u>	<u>1,456,157</u>

The notes on page 26 form part of the condensed financial statements.

## Investor Compensation Fund

### Statement of Changes in Equity

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

	Unaudited Quarter Ended <u>30 Jun 2005</u> \$'000	Unaudited Quarter Ended <u>30 Jun 2004</u> \$'000
Compensation fund balance as at 1 April	1,456,157	962,209
Surplus for the quarter	63,398	38,714
Contributions from UECF	-	121,683
Compensation fund balance as at 30 June	<u>1,519,555</u>	<u>1,122,606</u>

The notes on page 26 form part of the condensed financial statements.

## Investor Compensation Fund

### Cash Flow Statement

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Cash flows from operating activities</b>		
Surplus for the quarter	63,398	38,714
Net investment income	(23,661)	(402)
Exchange difference	3,033	-
(Increase) / decrease in levies receivable	(305)	5,028
Increase in accounts receivable	(484)	(140)
Increase / (decrease) in accounts payable and accrued charges	<u>59</u>	<u>(49)</u>
<b>Net cash generated from operating activities</b>	<u>42,040</u>	<u>43,151</u>
<b>Cash flows from investing activities</b>		
Purchase of debt securities	(979,836)	-
Sale or maturity of debt securities	895,124	51,500
Sale of equity securities	153	-
Interest received	<u>12,910</u>	<u>2,172</u>
<b>Net cash (used in) / generated from investing activities</b>	<u>(71,649)</u>	<u>53,672</u>
<b>Cash flows from financing activities</b>		
Contributions received from UECF	<u>-</u>	<u>121,683</u>
<b>Net cash generated from financing activities</b>	<u>-</u>	<u>121,683</u>
<b>Net (decrease) / increase in cash and cash equivalents</b>	(29,609)	218,506
<b>Cash and cash equivalents at beginning of the quarter</b>	<u>118,958</u>	<u>766,977</u>
<b>Cash and cash equivalents at end of the quarter</b>	<u>89,349</u>	<u>985,483</u>
<b>Analysis of the balance of cash and cash equivalents:</b>		
	Unaudited At 30 Jun 2005 \$'000	Unaudited At 30 Jun 2004 \$'000
Cash at bank	232	100,044
Fixed and call deposits with banks	<u>89,117</u>	<u>885,439</u>
	<u>89,349</u>	<u>985,483</u>



# Investor Compensation Fund

## Notes to the Condensed Financial Statements

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

### 1. BASIS OF PREPARATION

The Fund prepares the interim financial report in accordance with International Accounting Standard 34 "Interim financial reporting" adopted by the International Accounting Standards Board.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2005 to the interim financial report.

### 2. ICC EXPENSES

The SFC formed the Investor Compensation Company Limited (ICC) in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the Securities and Futures Ordinance (SFO). The Fund is responsible for funding the establishment and operation of ICC. For the quarter ended 30 June 2005, ICC incurred \$789,000 for its operation (For the quarter ended 30 June 2004 : \$959,000).

### 3. CONTINGENT LIABILITIES

As at the date of this report, the Fund has received claims against two intermediaries. 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 \$300,000 (As at 31 March 2005 : \$900,000).

# 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 quarter ended 30 June 2005.

### 1. ESTABLISHMENT OF THE FUND

Part X of the repealed Securities Ordinance (Chapter 333) established the Fund. However, when the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single investor compensation fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. After reserving sufficient money in the Fund to meet claims against it and its other liabilities, the SFC will eventually transfer the remaining balance of the Fund to the ICF.

Part X of the repealed Securities Ordinance remains effective in respect of the operation of the Fund to the extent described in Section 74 of Schedule 10 of the SFO.

### 2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 28 to 33.

### 3. MEMBERS OF THE COMMITTEE

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

Mr. Martin Wheatley	[appointed on 21 June 2005]
Mr. Peter Au-Yang	[appointed on 1 April 2005 and resigned on 20 June 2005]
Mr. Eddy C. Fong, SBS, JP	[appointed on 1 April 2005]
Mr. Gerald Greiner	[appointed on 1 April 2005]
Mrs. Alexa Lam	
Mr. David M. Roberts	

### 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 quarter.

On behalf of the Committee

Martin Wheatley  
Chairman

25 July 2005

## Unified Exchange Compensation Fund

### Income and Expenditure Account

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	<u>Note</u>	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Income</b>			
Net investment income		292	(978)
Recoveries	2	164	10,033
Replenishments from SEHK	3	1	-
Provision for compensation reversed		-	923
		<u>457</u>	<u>9,978</u>
		-----	-----
<b>Expenses</b>			
Provision for compensation made		876	-
Auditors' remuneration		9	9
Bank charges		1	16
Professional fees		-	13
Sundry expenses		1	1
		<u>887</u>	<u>39</u>
		-----	-----
<b>(Deficit) / Surplus</b>		(430)	9,939
<b>Accumulated surplus / (deficit) brought forward</b>		<u>7,455</u>	<u>(13,284)</u>
<b>Accumulated surplus / (deficit) carried forward</b>		<u><u>7,025</u></u>	<u><u>(3,345)</u></u>

The notes on pages 32 and 33 form part of the condensed financial statements.

# Unified Exchange Compensation Fund

## Balance Sheet

At 30 June 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited At 30 Jun 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Current assets</b>			
Equity securities received under subrogation	2	5,443	7,793
Interest receivable		48	36
Fixed and call deposits with banks		48,928	47,028
Cash at bank		145	52
		<u>54,564</u>	<u>54,909</u>
<b>Current liabilities</b>			
Accounts payable and accrued charges		4,291	4,291
Provision for compensation	4	1,577	1,492
		<u>5,868</u>	<u>5,783</u>
<b>Net current assets</b>		<u>48,696</u>	<u>49,126</u>
<b>Net assets</b>		<u>48,696</u>	<u>49,126</u>
Representing:			
<b><u>Compensation fund</u></b>			
Contributions from the SEHK		46,100	46,100
Excess transaction levy from the SEHK		353,787	353,787
Special contribution		3,500	3,500
Additional contribution from the SEHK		300,000	300,000
Additional contribution from the SFC		330,000	330,000
Special levy surplus		3,002	3,002
Accumulated surplus		7,025	7,455
		1,043,414	1,043,844
Contributions to Investor Compensation Fund		<u>(994,718)</u>	<u>(994,718)</u>
		<u>48,696</u>	<u>49,126</u>

The notes on pages 32 and 33 form part of the condensed financial statements.

## Unified Exchange Compensation Fund

### Statement of Changes in Equity

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

	Unaudited Quarter Ended <u>30 Jun 2005</u> \$'000	Unaudited Quarter Ended <u>30 Jun 2004</u> \$'000
Compensation fund balance as at 1 April	49,126	323,815
(Deficit) / surplus for the quarter	(430)	9,939
Contributions refunded to the SEHK	-	(250)
Contributions to Investor Compensation Fund	-	(121,683)
Compensation fund balance as at 30 June	<u>48,696</u>	<u>211,821</u>

The notes on pages 32 and 33 form part of the condensed financial statements.

# Unified Exchange Compensation Fund

## Cash Flow Statement

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Cash flows from operating activities</b>		
(Deficit) / surplus for the quarter	(430)	9,939
Net investment income	(292)	978
Decrease in equity securities received under subrogation	2,350	1,121
Increase /(decrease) in provision for compensation	85	(2,434)
Decrease in accounts payable and accrued charges	-	(177)
<b>Net cash generated from operating activities</b>	<u>1,713</u>	<u>9,427</u>
<b>Cash flows from investing activities</b>		
Debt securities redeemed	-	21,500
Interest received	280	2,880
<b>Net cash generated from investing activities</b>	<u>280</u>	<u>24,380</u>
<b>Cash flows from financing activities</b>		
Contribution refunded to the SEHK	-	(250)
Contributions to Investor Compensation Fund	-	(121,683)
<b>Net cash used in financing activities</b>	<u>-</u>	<u>(121,933)</u>
<b>Net increase / (decrease) in cash and cash equivalents</b>	1,993	(88,126)
<b>Cash and cash equivalents at beginning of the quarter</b>	<u>47,080</u>	<u>167,622</u>
<b>Cash and cash equivalents at end of the quarter</b>	<u>49,073</u>	<u>79,496</u>
<b>Analysis of the balance of cash and cash equivalents:</b>		
	Unaudited At 30 Jun 2005 \$'000	Unaudited At 30 Jun 2004 \$'000
Cash at bank	145	157
Fixed and call deposits with banks	<u>48,928</u>	<u>79,339</u>
	<u>49,073</u>	<u>79,496</u>

# Unified Exchange Compensation Fund

## Notes to the Condensed Financial Statements

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

### 1. BASIS OF PREPARATION

The Fund prepares the interim financial report in accordance with International Accounting Standard 34 "Interim financial reporting" adopted by the International Accounting Standards Board. As the Fund will eventually cease operation as a result of the Securities and Futures Ordinance (SFO) which came into effect from 1 April 2003, the Fund prepares the interim financial report on a break-up basis with assets stated at recoverable amounts.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2005 to the interim financial report.

### 2. EQUITY SECURITIES AND RECOVERIES

In relation to the share distribution from C.A. Pacific Securities Ltd. and C.A. Pacific Finance Ltd., the liquidators had advised the Securities and Futures Commission (SFC) that shares were allocated to the Fund under its subrogation rights, subject to paying a processing fee to the liquidators. The Fund recognised as recoveries the sale proceeds and the remaining shares at market value as of 30 June 2005 after deducting relevant processing fees and charges for collecting and selling the securities received.

### 3. REPLENISHMENTS FROM THE SEHK

Under Section 107 of the Securities Ordinance, the SFC may require the SEHK to replenish the Fund with an amount that is equal to that paid in connection with the satisfaction of the claim (limited to \$8,000,000 per each defaulted case) after the SFC has exhausted all relevant rights of action and other legal remedies against the defaulter. During the quarter, the Fund received replenishments of \$883 from the SEHK in respect of one defaulted case.

# Unified Exchange Compensation Fund

## Notes to the Condensed Financial Statements

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

### 4. PROVISION FOR COMPENSATION

	Unaudited \$'000
Balance as at 1 April 2004	9,545
Less: amount paid during the year ended 31 March 2005	(2,851)
unused provision reversed during the year ended 31 March 2005	<u>(5,202)</u>
Balance as at 31 March 2005	1,492
Less: amount paid during the quarter ended 30 June 2005	(791)
Add: provision made during the quarter ended 30 June 2005	<u>876</u>
Balance as at 30 June 2005	<u><u>1,577</u></u>

We made provision for claims in respect of three SEHK exchange participants for which the SEHK has published a notice calling for claims. The maximum liabilities of the Fund in respect of these three default cases can exceed the normal \$8 million limit.

### 5. CONTINGENT LIABILITIES

As at the date of this report, the SEHK has received claims against seven exchange participants. They are subject to the normal \$8 million ceiling pursuant to Section 109 of the repealed 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 \$56 million (As at 31 March 2005 : \$56 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 quarter ended 30 June 2005.

### 1. ESTABLISHMENT OF THE FUND

Part VIII of the repealed Commodities Trading Ordinance (Chapter 250) established the Fund. However, when the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single investor compensation fund (ICF) was formed to ultimately replace the Fund and the Unified Exchange Compensation Fund. After reserving sufficient money in the Fund to meet claims against it and its other liabilities, the SFC will eventually transfer the remaining balance of the Fund to the ICF.

Part VIII of the repealed Commodities Trading Ordinance remains effective in respect of the operation of the Fund to the extent described in Section 75 of Schedule 10 of the SFO.

### 2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 35 to 39.

### 3. MEMBERS OF THE COMMITTEE

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

Mr. Martin Wheatley	[appointed on 21 June 2005]
Mr. Peter Au-Yang	[appointed on 1 April 2005 and resigned on 20 June 2005]
Mr. Eddy C. Fong, SBS, JP	[appointed on 1 April 2005]
Mr. Gerald Greiner	
Mrs. Alexa Lam	
Mr. Calvin Tai	

### 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 quarter.

On behalf of the Committee

Martin Wheatley  
Chairman

25 July 2005

## Commodity Exchange Compensation Fund

### Income and Expenditure Account

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Income</b>		
Net investment income	2	-
	<hr/>	<hr/>
<b>Expenses</b>		
Auditors' remuneration	6	9
Bank charges	-	-
Professional fees	-	-
Sundry expenses	1	1
	<hr/>	<hr/>
	7	10
	<hr/>	<hr/>
<b>Deficit</b>	(5)	(10)
<b>Accumulated surplus brought forward</b>	108,228	108,262
	<hr/>	<hr/>
<b>Accumulated surplus carried forward</b>	108,223	108,252
	<hr/>	<hr/>

The note on page 39 form part of the condensed financial statements.

# Commodity Exchange Compensation Fund

## Balance Sheet

At 30 June 2005

(Expressed in Hong Kong dollars)

	Unaudited At 30 Jun 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Current assets</b>		
Interest receivable	1	-
Fixed and call deposits with banks	483	488
Cash at bank	1	4
	<u>485</u>	<u>492</u>
<b>Current liabilities</b>		
Accounts payable and accrued charges	<u>222</u>	<u>224</u>
<b>Net current assets</b>	<u>263</u>	<u>268</u>
<b>Net assets</b>	<u>263</u>	<u>268</u>
Representing:		
<b><u>Compensation fund</u></b>		
Accumulated surplus	108,223	108,228
Contributions to Investor Compensation Fund	<u>(107,960)</u>	<u>(107,960)</u>
	<u>263</u>	<u>268</u>

The note on page 39 form part of the condensed financial statements.

## Commodity Exchange Compensation Fund

### Statement of Changes in Equity

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

	Unaudited Quarter Ended <u>30 Jun 2005</u> \$'000	Unaudited Quarter Ended <u>30 Jun 2004</u> \$'000
Compensation fund balance as at 1 April	268	302
Deficit for the quarter	<u>(5)</u>	<u>(10)</u>
Compensation fund balance as at 30 June	<u><u>263</u></u>	<u><u>292</u></u>

The note on page 39 form part of the condensed financial statements.

# Commodity Exchange Compensation Fund

## Cash Flow Statement

For the quarter ended 30 June 2005

(Expressed in Hong Kong dollars)

	Unaudited Quarter Ended 30 Jun 2005 \$'000	Unaudited Quarter Ended 30 Jun 2004 \$'000
<b>Cash flows from operating activities</b>		
Deficit for the quarter	(5)	(10)
Net investment income	(2)	-
Decrease in accounts payable and accrued charges	<u>(2)</u>	<u>(27)</u>
<b>Net cash used in operating activities</b>	<u>(9)</u>	<u>(37)</u>
<b>Cash flows from investing activities</b>		
Interest received	<u>1</u>	<u>-</u>
<b>Net cash generated from investing activities</b>	<u>1</u>	<u>-</u>
<b>Net decrease in cash and cash equivalents</b>	(8)	(37)
<b>Cash and cash equivalents at beginning of the quarter</b>	<u>492</u>	<u>529</u>
<b>Cash and cash equivalents at end of the quarter</b>	<u>484</u>	<u>492</u>
<b>Analysis of the balance of cash and cash equivalents:</b>		
	Unaudited At 30 Jun 2005 \$'000	Unaudited At 30 Jun 2004 \$'000
Cash at bank	1	5
Fixed and call deposits with banks	<u>483</u>	<u>487</u>
	<u>484</u>	<u>492</u>



# Commodity Exchange Compensation Fund

Notes to the Condensed Financial Statements

For the quarter ended 30 June 2005

*(Expressed in Hong Kong dollars)*

## 1. BASIS OF PREPARATION

The Fund prepares the interim financial report in accordance with International Accounting Standard 34 "Interim financial reporting" adopted by the International Accounting Standards Board. As the Fund will eventually cease operation as a result of the Securities and Futures Ordinance (SFO) which came into effect from 1 April 2003, the Fund prepares the interim financial report on a break-up basis with assets stated at recoverable amounts.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2005 to the interim financial report.