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*This is the Securities and Futures Commission's third 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 October to 31 December 2005

The quarter continued to be a busy period, as we made several key initiatives and took actions to raise market standards and facilitate market development. For example:

- We authorised the first REITs in Hong Kong, and announced a policy on disclosure of interests in REITs so that the market may be better informed.
- We published for consultation a six-point plan to enhance the derivative warrants market.
- Our prosecutions secured convictions of 23 persons and firms, and we disciplined 37 entities. These were higher than the figures in both the previous quarter and the same quarter in 2004. Three persons were sentenced to imprisonment for up to six months, one of which was an immediate sentence.

On the investors' front:

- We launched our Investor Education Month in January 2006. Our initiatives included new TV and radio commercials, an IE icon reinforcing the importance of "Learn before you invest", and re-branding of the Internet portal Electronic Investor Resources Centre as the InvestEd website ([www.InvestEd.hk](http://www.InvestEd.hk)).
- Investors received the good news that they are not required to pay investor compensation levies on securities and futures transactions from 19 December, following changes to the levy collection mechanism.

During the period, we also note that:

- The number of licensed persons exceeded 25,000 during the quarter, reaching 25,292 at the end of December.
- The brokerage industry also saw an increase in total shareholders' fund as trading had remained buoyant.

On SFC's finances:

- Total revenue for the third quarter dropped 3% to \$202 million from the previous quarter on lower levy income, while total expenditure remained at \$122 million.
- Total revenue for the first nine months of the fiscal year was \$575 million, with total expenditure of \$359 million.

## Review of Operations

1 October to 31 December 2005

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

### Market Overview

The US market slid during October as higher-than-expected price indices fuelled worries over inflation and further interest rate hikes. However, strong economic growth and corporate earnings, and declining oil prices, had lifted the Dow and NASDAQ to eight-month and four-year highs respectively in late November. The Dow, S&P and NASDAQ ended the quarter 1.4%, 1.6% and 2.5% higher respectively. European markets continued to outperform their US counterparts, with the DAX, FTSE and CAC rising 7.2%, 2.6% and 2.5% respectively.

The Mainland market dropped initially but rebounded. During the quarter, the Shanghai Composite Index edged up 0.5% while the Shenzhen Composite Index dropped 1.1%.

In Hong Kong, the market slid initially, after reaching a 4.5-year high in September. The HSI had dropped 6.8% within October. Following the gains of overseas markets, the market rebounded on hopes for an early completion of the rate hike cycle. The strong debut of Link Real Estate Investment Trusts (REIT) further boosted market sentiment, though profit-taking ahead of the year-end trimmed some gains. During the quarter, the HSI dropped 3.6% to 14,876 at the end of December, the H-shares index rose 2% and the red chips index declined by 4.1%.

Trading was less active than the previous quarter. The average daily turnover on the Main Board dropped 9.3% to \$18.6 billion. The average daily turnover of HSI constituent stocks declined by 11.3% to \$7 billion, while that of H-shares dropped 12.1% to \$4.2 billion. The average daily turnover of red chips was down 13.1% to \$2.4 billion.

On the Growth Enterprise Market, the S&P/HKEx GEM index closed flat at 1,007 at the end of the period. The average daily turnover on GEM was about \$88.1 million, a 23.8% decrease from the previous quarter.

IPO activities were very active during the quarter with 31 IPOs on the Main Board, including three REITs, and five on GEM, compared with a total of 10 IPOs in the previous quarter. The total amount of funds raised through IPOs was \$121.5 billion, compared with \$4.2 billion in the previous quarter.

At the end of December, the open interest of HSI futures was 98,211 contracts, 16.7% lower than the end-September level. The open interests of H-shares Index Futures and HSI Options were 35,125 contracts and 192,069 contracts respectively, 4.2% higher and 10.3% lower than the respective end-September levels.

### **Securities and Futures Ordinance (SFO)**

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

Amendments to legal definitions of certain regulated activities in Schedule 5 to the SFO to accommodate the latest market developments were gazetted on 11 November. They came into effect on 6 January.

In tandem with the Government's consultation on proposed amendments to the SFO to strengthen listing regulation, the SFC consulted the public on proposed amendments to the Securities and Futures (Stock Market Listing) Rules in January 2005. The consultation closed in March 2005. We have analysed the responses to the consultation and are discussing with the Government, HKEx and industry representatives to develop the proposed amendments required to enhance listing regulation.

Following the amendments to the Securities and Futures (Investor Compensation - Levy) Rules that came into effect on 28 October, the Government gazetted an exemption notice to declare that no person is required to pay investor compensation levies on securities and futures transactions on or after 19 December. The suspension will remain in force until the net asset value of the Investor Compensation Fund falls below \$1 billion.

Review of the disclosure of interests regime under Part XV of the SFO continued. The Working Group on Disclosure Requirements for Security Interests held the inaugural meeting on 4 October and members' comments and suggestions are being considered.

### **Raising Market Standards**

The SFC issued a consultation paper in August on possible reforms to the regime governing the public offering of shares and debentures as set out in the Companies Ordinance. Following requests from market practitioners, the SFC extended the consultation period from 30 November to 31 December. We are analysing the 26 submissions that we received.

The main revisions of the Codes on Takeovers and Mergers and Share Repurchases took effect on 1 October. The remaining revisions under Notes 1 and 2 to Rule 8 require that a copy of each document required to be displayed under Note 1 also be provided in electronic form for display on the SFC website. These revisions became effective on 1 January and will apply to transactions announced on or after that date.

We released a report entitled "A Healthy Market for Informed Investors - A Report on the Derivative Warrants Market in Hong Kong" on 25 November. The report reviewed market characteristics and practices, assessed the impact of derivative warrant activities on stock market stability and investor education needs. It also identified areas of regulation that may need reform and proposed a Six-Point Plan to improve the market. The SFC has invited the public to comment before 31 January. Responses to the proposals will be considered before formal consultation on any changes to the Listing Rules. We also briefed LegCo's Financial Affairs Panel on the matter on 5 January.

The SFC and the Insurance Authority announced on 20 December the signing of a Memorandum of Understanding (MoU) to enhance the co-operation in the regulation of insurance-related investment products, the exchange of information of persons regulated under their respective supervisory regimes and mutual assistance between the two regulators.

On 15 December, the SFC announced its policy to require that provisions substantially equivalent to those applicable to listed corporations in Part XV of the SFO be adopted in trust deeds of SFC-authorized REITs. The policy is to enhance transparency and accessibility of information regarding interests in REIT. Holders of REIT units are required to submit to the REIT manager and the HKEx notification of interests upon the attainment of the 5% disclosure threshold, and other changes in accordance with the trust deed. Such notifications will be posted on the HKEx website.

On 17 October, the Financial Secretary published the SFC's 2005 annual review on HKEx's performance in its regulation of listing matters, covering the Exchange's operation in 2004 and January 2005. The review focused on the Exchange's procedures in key listing-related functional areas. Based on our review we concluded that the Exchange's procedures in the areas examined were adequate to enable it to discharge its statutory obligation to maintain an orderly, informed and fair market. At the same time, we made recommendations to improve its procedures further.

### **Partnership with the Industry**

The number of persons licensed by or registered with the SFC increased by 2.3% from 24,722 as at 30 September to 25,292 as at 31 December. During the quarter, we granted licences to three management companies to manage The Link REIT, Prosperity REIT and GZI REIT respectively.

Mainland's further liberalisation measures concerning the financial services sector under the third phase of the Closer Economic Partnership Arrangement (CEPA III) were signed on 18 October in Hong Kong. Under CEPA III, qualified securities and futures companies in the Mainland are allowed to set up subsidiaries in Hong Kong. The SFC will co-ordinate with the China Securities Regulatory Commission (CSRC) on the implementation details.

Licensing issues commonly encountered by fund managers, including responsible officers and corporate applicants were discussed in the November/December issue of the SFC Alert in the form of FAQs.

Following the publication of our Revised Prevention of Money Laundering and Terrorist Financing Guidance Note, which will come into effect in April, the SFC held a series of seminars to assist the industry in implementing the new measures.

<b>Statistical Information and Financial Position of the Securities Industry</b>		
	<b>As at 31 Dec 2005</b>	<b>As at 31 Dec 2004</b>
Total number of securities dealers and securities margin financiers	648	663
Total number of active cash clients (Note 1)	625,775	609,281
Total number of active margin clients (Note 1)	72,290	76,546
<b>Balance Sheet (Note 2)</b>	<b>(\$ Million)</b>	<b>(\$ Million)</b>
Cash in hand and at bank (Notes 3)	121,357	110,176
Amounts receivable from margin clients (Note 4)	18,020	17,158
Amounts receivable from clients and other dealers arising from dealing in securities	103,898	65,357
Proprietary positions	98,231	77,777
Other assets	118,979	61,145
<b>Total assets</b>	<b>460,485</b>	<b>331,613</b>
Amounts payable to clients and other dealers arising from dealing in securities	174,145	124,739
Total borrowings from financial institutions	102,171	56,264
Short positions held for own account	34,480	26,552
Other liabilities	67,550	47,068
Total shareholders' fund (Note 5)	82,139	76,990
<b>Total liabilities and shareholders' fund</b>	<b>460,485</b>	<b>331,613</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 (Contract Notes, Statements of Account and Receipts) Rules.	
Note 2:	The increases in 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 \$52,434 million (31/12/2004: \$49,305 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 31 Dec 2005</u>	<u>As at 31 Dec 2004</u>
	4.3	4.6
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 SFC continued to monitor the latest developments in the Undertakings for Collective Investment in Transferable Securities (UCITS) III, the regulations issued by the European Union Commission that govern funds domiciled in the EU states, and maintain dialogue with overseas regulators and market practitioners. As of the end of December, the SFC had authorised 1,016 UCITS III funds, representing over 88% of the applications received.

Number of SFC Authorised Collective Investment Schemes			
	31 Dec 2005	30 Sep 2005	31 Dec 2004
Unit Trusts and Mutual Funds	1,964	1,997	1,933
Investment-Linked Assurance Schemes	194	187	175
Pooled Retirement Funds	37	37	38
MPF Master Trust / Industry Schemes	44	45	45
MPF Pooled Investment Funds (Note1)	277	280	255
Real Estate Investment Trusts	3	0	0
Other Schemes (Note 2)	98	94	67
<b>Total</b>	<b>2,617</b>	<b>2,640</b>	<b>2,513</b>
Note 1: There are 120 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 November, the SFC approved HKEx's proposal to launch callable bull/bear contracts. HKEx started to brief market participants and introduce the product details to issuers last December, preparing for a product launch later in the year.

We continued to work with the industry on how best to deploy XBRL (eXtensible Business Reporting Language), an evolving global standard for faster and more accurate electronic communication of business and financial data, in Hong Kong. The XBRL Preparatory Working Group held its second meeting during the quarter to update its members on the latest progress.

The SFC had worked closely with HKEx and the Police to co-ordinate the contingency measures for the markets during the Sixth Ministerial Conference (MC6) of the World Trade Organization conference, which concluded successfully in December. The SFC issued circulars to licensed corporations and associated entities to alert them about the risks and remind them to review their business continuity arrangements. The Federation of Share Registrars was also asked to advise its members to prepare for the MC6.



## Enforcement and Regulatory Actions

During the quarter, the SFC successfully prosecuted 23 entities for market manipulation, failing to attend SFC's investigations, providing misleading information to the SFC, disclosure of interests breaches, unlicensed activities, cold calling, and making reckless and fraudulent misrepresentations. There were no acquittals and no summonses were withdrawn.

An individual convicted of market manipulation was sentenced to six months' imprisonment, suspended for 24 months, and ordered to pay investigation costs to the SFC. A District Court Judge activated another individual's suspended sentence and sentenced him to six months' imprisonment for his failure to attend SFC's interviews. A third person was sentenced to two months' imprisonment suspended for 12 months for unlicensed asset management.

During the quarter, the SFC took disciplinary action against 37 entities for various breaches:

1. *Settlement with sanctions* - Seven licensed corporations agreed to disciplinary actions, including public reprimands and fines ranging from \$75,000 to \$700,000, for: -

- breaching the Anti-Money Laundering Guidelines and the Financial Resources Rules (FRR);
- failing to detect and prevent unregistered dealing activities;
- failing to detect abusive trading activities;
- failing to establish the true and full identity of an account holder;
- failing to keep proper records of clients' orders;
- failing to safeguard client assets;
- posting misleading information on the company's website;
- re-pledging securities of margin clients to banks without authority;
- transferring interest accrued from clients' money to the company's own account without clients' consent;
- deficiencies in procedures for authenticating changes of clients' information and for monitoring clients' trades;
- inadequate monitoring of staff dealing transactions and discretionary accounts;
- inadequate supervision of staff; and
- internal control failures.

17 licensed representatives, including three responsible officers and a former dealing director, agreed to disciplinary actions (including public reprimands, making a \$60,000 voluntary payment, fines ranging from \$30,000 to \$60,000, and suspensions for five weeks to 18 months) for: -

- aiding and abetting unlicensed dealing;
- breaching the Know-Your-Client Rule;
- internal control failures;
- concealing personal trading activities from employer;

- illegal short selling;
- unregistered dealing activities;
- trading jointly with clients;
- facilitating market manipulation by executing questionable orders;
- failing to keep proper records of clients' orders;
- failing to monitor and report unregistered dealing activities to the SFC;
- creating a false market;
- posting misleading information on the company's website;
- misleading the SFC; and
- inadequate supervision of staff.

In addition, a former licensed representative was banned from re-entering the industry for five years as a result of trading in securities that were the subject matter of the research reports he prepared.

2. *Suspensions* - The Securities and Futures Appeals Tribunal (SFAT) upheld the SFC's decision to suspend an individual for one month for failing to account for client assets and to keep proper account of compensation. A responsible officer was suspended for nine months for failing to detect and inquire into clients' suspicious trades. Another responsible officer was suspended for six months for failing to inform a client of the irregularities of his transactions and to verify the identity of the person who placed orders on the client's behalf. A former responsible officer was suspended for 20 months for lying to the SFC and lending his account to a third party for personal use. A licensed representative was suspended for six months for failing to report clients' suspicious trades to his supervisor.
3. *Reprimands and fines* - A licensed corporation and its responsible officer were reprimanded and fined for FRR breaches, internal control weaknesses and inadequate supervision of staff.
4. *Reprimands* - Three licensed corporations were reprimanded for supervisory failures, failing to monitor manipulative trades and ensure sound advice be given to clients. A licensed representative was reprimanded for conducting discretionary trading without proper written authorisation from the client and failing to record clients' orders properly.

#### Statistics of Enforcement Actions

	Oct - Dec 2005	Jul - Sep 2005	Oct - Dec 2004
Successful prosecutions	23	15	21
Entities disciplined (including settlement cases) (Note 1)	37	29	25
Warning letters issued (Note 2)	48	30	82
Cases under investigation (Notes 3 and 4)	457	494	523
Disciplinary inquiries in progress (Note 4)	114	109	122

Note 1: The number includes currently and previously licensed entities.

Note 2: The decrease from the same quarter last year was mainly owing to disclosure of interests breaches.

Note 3: Some cases are ongoing investigations from the previous quarter.

Note 4: Number of cases as at end of quarters.

During the quarter, we received 23 complaints in relation to boiler room operations and acted upon five of them. Liaison work with other domestic and overseas enforcement bodies in this regard has continued.

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

We have designated January 2006 as the Investor Education Month to draw the public's attention to the importance of investor education. The launch ceremony was officiated by Mr Frederick Ma, Secretary for Financial Services and the Treasury on 10 January, with the theme "Before you invest, ask the right questions". Our investor education initiatives included new TV and radio commercials, a new investor education icon, the re-branding of the portal previously called Electronic Investor Resources Centre as "InvestEd" (URL changed to [www.InvestEd.hk](http://www.InvestEd.hk)) and the addition of flash animation videos to complement our educational information on the portal.

The SFC organised in November an open competition "My Investment Story" with The Salvation Army and the Radio Television Hong Kong to invite the public to share their personal experiences in investing.

We started a new weekly column on derivative warrants in the Money Times magazine of Hong Kong Economic Times in October. We also introduced new games on our portal and more numeric examples in our article series to enhance the public's understanding of warrants.

We continued to increase collaboration with universities during the quarter. We partnered with The Open University of Hong Kong to organise 13 free investor education seminars and workshops for the public in November and December. They covered topics on personal financial planning, investment psychology, stock analysis, new investment products and stock transaction flow from execution to settlement. Over 1,800 individuals attended these workshops. More sessions took place in January.

We also gave lectures at The Hong Kong University of Science and Technology and Hong Kong Baptist University and met various student societies. In addition, we spoke to secondary school students and civil servants on market operations, financial products and prudent retirement investment.

We gave out six Smart Investor Awards in December to the public for reporting boiler rooms and Internet financial scams. We also made the Alert List on the InvestEd more user-friendly by adding search functions.

During the quarter, Dr Wise's column discussed financial advisers and investment product recommendations, change of control of listed companies and disclosure of interests.

We published the second Quarterly Report for the financial year 2005 - 2006 in mid-November on our operations and financial position in July - September.

We also continued to publish the bi-monthly newsletter SFC Alert, the monthly SFC Enforcement Reporter, and the Autumn issue of Quarterly Bulletin to communicate with the public on our work and enforcement actions and to educate the investing public. All these publications are available on the SFC website.

Statistics of Investor Enquiries and Public Complaints			
	Oct - Dec 2005	Jul - Sep 2005	Oct - Dec 2004
Enquiries	1,218	1,205	1,219
Complaints	257	252	306

### International Co-operation and External Relations

During the quarter, the SFC received 11 requests from overseas regulators, eight seeking non-public information and the rest seeking public information, investigatory and other assistance. Responses were provided to five requests and the remainders were being processed. During this period, we made three requests to overseas regulators for investigatory assistance.

We visited the CSRC in Beijing on 26 and 27 October. We met CSRC Chairman, Mr Shang Fulin, and other senior CSRC officials and had useful discussions on Mainland's state-owned shares reform, Hong Kong's role in the development of the PRC capital market, and other issues.

We welcomed one local delegation, visitors from Korea, a Hong Kong Government-sponsored Thai newspaper editor and three Mainland delegations during the quarter.

### Financial Review<sup>1</sup>

The SFC's financial position remained healthy during the quarter.

Total revenue for October - December decreased 3% from \$208 million in the previous quarter to \$202 million. Levy income decreased 7% to \$141 million from \$151 million as the average daily stock market turnover dropped from \$22 billion to \$21 billion<sup>2</sup>. Total expenditure (including depreciation) was \$122 million, remaining at the same level of last quarter. As a result, the SFC recorded a surplus of \$80 million for the quarter, compared with the \$87 million recorded for July to September.

By the end of December, total revenue for the first nine months of the financial year was \$575 million. Levy income comprised \$401 million as the average daily stock market turnover increased to \$20 billion from \$16 billion. Fees and charges income was \$144 million.

<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.

Total expenditure (including depreciation) for the nine months was \$359 million. The total number of staff at the end of December was 433, comprising 387 regular staff and 46 temporary staff.

Overall, the Commission recorded a surplus of \$215 million for the first three quarters, compared to the \$122 million surplus recorded in the same period last year.

At the end of December, our reserves stood at \$1.08 billion.

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

### **Corporate Affairs**

The SFC received several awards during the quarter. In November, the SFC's Annual Report 2004-2005 took the Gold Award in the public organisation category in the Hong Kong Management Association's Best Annual Reports Awards. It was also the winner of the Award for Citation for Achievement in Corporate Governance Disclosure. The Report was highly commended for its professional set of accounts, the provision of information relation to Corporate Governance, discussion on employee relations and development, description of activities, performance, and future plans, and overall understandability. The Annual Report was also given the Platinum Award in the Public Sector/Not-for-profit Organisations Category in the Hong Kong Institute of Certified Public Accountants' Best Corporate Governance Disclosure Awards 2005.

In October, the SFC corporate website at [www.sfc.hk](http://www.sfc.hk) was named one of the Gold Award recipients in the Web Care Award 2005, which was organised by the Internet Professional Association to promote no-barrier websites for all users including people with disabilities.

The Commission Possible Volunteers Group, the SFC's volunteers group, organised a Christmas party for 45 children and parents in Tai Kok Tsui in December.

### **Looking Ahead**

The Hong Kong market has made considerable gains in the past year and the financial industry has benefitted from the increase in business. Inevitably, as the economic conditions improve, we have seen increased levels of staff turnover.

We believe it is a compliment to our staff that the private sector sees the SFC as a good recruitment ground for high quality people. We are also pleased that staff may put to good use their regulatory experience acquired during their service here.

The SFC can only effectively discharge its regulatory functions properly with a competent staff. Hence, hiring and retaining the right people remains a priority. We review staff remuneration regularly to ensure that the packages are commensurate with the market level, making adjustments where necessary. We will continue to work closely with the Government to ensure that we are given the adequate support and properly resourced to keep good people. We are also working on some staff retention proposals.

We are pleased that the SFC was rated as one of the top 10 companies in Hong Kong that undergraduates would like to work for, in a survey conducted by a leading journal last December. We are confident that with sound and comprehensive people management policies and practices, we will continue to attract both young talent and experienced practitioners to join the SFC.

Martin Wheatley  
Chairman

14 February 2006

## Securities and Futures Commission

### Consolidated Income and Expenditure Account

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited Three Months Ended		Unaudited Nine Months Ended	
		31 Dec 2005	31 Dec 2004	31 Dec 2005	31 Dec 2004
		\$'000	\$'000	\$'000	\$'000
<b>Income</b>					
Levies		140,572	127,165	401,210	313,966
Fees and charges		50,155	41,635	144,138	119,618
Investment income		9,837	5,786	24,887	15,942
Recoveries from Investor					
Compensation Fund		941	956	2,499	2,784
Other income		255	404	1,850	3,831
		<u>201,760</u>	<u>175,946</u>	<u>574,584</u>	<u>456,141</u>
<b>Expenses</b>					
Staff costs		92,672	105,913	278,414	261,552
Premises					
- rent		5,358	5,358	16,074	15,215
- other		3,408	3,397	10,277	9,528
Other expenses		14,910	10,839	39,430	31,659
		<u>116,348</u>	<u>125,507</u>	<u>344,195</u>	<u>317,954</u>
Depreciation		5,590	5,934	15,084	16,388
		<u>121,938</u>	<u>131,441</u>	<u>359,279</u>	<u>334,342</u>
<b>Surplus</b>	2	<u>79,822</u>	<u>44,505</u>	<u>215,305</u>	<u>121,799</u>

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

The notes on pages 17 to 19 form part of the condensed consolidated financial statements.

## Securities and Futures Commission

### Consolidated Balance Sheet

At 31 December 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited At 31 Dec 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Non-current assets</b>			
Fixed assets		20,417	25,258
Held-to-maturity debt securities	3	667,696	550,407
		<u>688,113</u>	<u>575,665</u>
<b>Current assets</b>			
Held-to-maturity debt securities	3	387,007	294,398
Bank deposits		96,848	69,656
Debtors, deposits and prepayments		64,393	58,181
Cash at bank and in hand		2,975	1,692
		<u>551,223</u>	<u>423,927</u>
<b>Current liabilities</b>			
Fees received in advance		43,775	36,675
Creditors and accrued charges		54,803	30,765
		<u>98,578</u>	<u>67,440</u>
<b>Net current assets</b>		<u>452,645</u>	<u>356,487</u>
<b>Total assets less current liabilities</b>		1,140,758	932,152
<b>Non-current liabilities</b>	4	65,368	72,067
<b>Net assets</b>		<u>1,075,390</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	1,032,550	817,245
		<u>1,075,390</u>	<u>860,085</u>

The notes on pages 17 to 19 form part of the condensed consolidated financial statements.



## Securities and Futures Commission

### Balance Sheet

At 31 December 2005

(Expressed in Hong Kong dollars)

	<u>Note</u>	<u>Unaudited</u> <u>At 31 Dec 2005</u> \$'000	<u>Audited</u> <u>At 31 Mar 2005</u> \$'000
<b>Non-current assets</b>			
Fixed assets		20,311	25,012
Held-to-maturity debt securities	3	667,696	550,407
		<u>688,007</u>	<u>575,419</u>
<b>Current assets</b>			
Held-to-maturity debt securities	3	387,007	294,398
Bank deposits		96,848	69,656
Debtors, deposits and prepayments		63,934	57,845
Cash at bank and in hand		978	945
		<u>548,767</u>	<u>422,844</u>
<b>Current liabilities</b>			
Fees received in advance		43,775	36,675
Creditors and accrued charges		52,241	29,451
		<u>96,016</u>	<u>66,126</u>
<b>Net current assets</b>		<u>452,751</u>	<u>356,718</u>
<b>Total assets less current liabilities</b>		1,140,758	932,137
<b>Non-current liabilities</b>	4	65,368	72,052
<b>Net assets</b>		<u>1,075,390</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	1,032,550	817,245
		<u>1,075,390</u>	<u>860,085</u>

The notes on pages 17 to 19 form part of the condensed consolidated financial statements.

## Securities and Futures Commission

Consolidated Cash Flow Statement  
For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Unaudited Nine months ended 31 Dec 2005 \$'000	Unaudited Nine months ended 31 Dec 2004 \$'000
<b>Cash flows from operating activities</b>		
Surplus	215,305	121,799
Adjustments for:		
Depreciation	15,084	16,388
Investment income	(24,887)	(15,942)
Profit on sale of fixed assets	(11)	(27)
	<u>205,491</u>	<u>122,218</u>
Increase in debtors, deposits and prepayments	(3,157)	(8,750)
Increase in creditors and accrued charges	24,249	34,400
Increase / (decrease) in fees received in advance	7,100	(1,043)
(Decrease) / increase in non-current liabilities	(6,684)	6,196
	<u>226,999</u>	<u>153,021</u>
<b>Net cash generated from operating activities</b>	-----	-----
<b>Cash flows from investing activities</b>		
Interest received	25,405	28,107
Held-to-maturity debt securities bought	(502,988)	(543,212)
Held-to-maturity debt securities redeemed	289,517	356,500
Fixed assets bought	(10,469)	(10,900)
Fixed assets sold	11	43
	<u>(198,524)</u>	<u>(169,462)</u>
<b>Net cash used in investing activities</b>	-----	-----
<b>Net increase / (decrease) in cash and cash equivalents</b>	28,475	(16,441)
<b>Cash and cash equivalents at beginning of the nine months</b>	<u>71,348</u>	<u>77,963</u>
<b>Cash and cash equivalents at end of the nine months</b>	<u>99,823</u>	<u>61,522</u>
<b>Analysis of the balance of cash and cash equivalents :</b>		
	Unaudited At 31 Dec 2005 \$'000	Unaudited At 31 Dec 2004 \$'000
Bank deposits	96,848	59,678
Cash at bank and in hand	2,975	1,844
	<u>99,823</u>	<u>61,522</u>

## Securities and Futures Commission

### Notes to the Condensed Consolidated Financial Statements

For the nine months ended 31 December 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 financial statements 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 31 December 2005. We eliminated 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 nine months ended 31 December 2005.

#### 2. Accumulated surplus

Movements of accumulated surplus during the nine months ended 31 December 2005 are as follows :

	<u>Unaudited</u> \$'000
Balance at 31 March 2005	817,245
Surplus	215,305
	<hr/>
Balance at 31 December 2005	<u>1,032,550</u>

#### 3. Held-to-maturity debt securities

As of 31 December 2005, the total market value of held-to-maturity debt securities amounted to \$1,046,467,000 (31 March 2005 : \$837,775,000), which was below the total carrying cost of \$1,054,703,000 (31 March 2005 : \$844,805,000).

## Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

### 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 31 December 2005. Therefore we do not provide an ageing analysis on 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.

### 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.

## Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the nine months ended 31 December 2005

*(Expressed in Hong Kong dollars)*

### 7. Investments in subsidiaries - Cont'd

Both companies are wholly owned subsidiaries of the SFC. As at 31 December 2005, the investment in subsidiaries, which is stated at cost less any impairment losses, amounted to \$2.2. The balance was too small to appear on the balance sheet which is expressed in thousands of dollars.

FinNet has not commenced operations. The balance sheet of FinNet as at 31 December 2005 and the income and expenditure account for the period 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.

### 8. Related party transactions

We have related party relationships with the Unified Exchange Compensation Fund, the Commodity Exchange Compensation Fund, the Investor Compensation Fund, the Securities Ordinance (Chapter 333) - Dealers' Deposits Fund, the Commodities Trading Ordinance (Chapter 250) - Dealers' Deposits Fund and the Securities Ordinance (Chapter 333) - Securities Margin Financiers' Security Fund. During the period, we received reimbursement from the Investor Compensation Fund for all the ICC's expenses, which is in accordance with section 242(1) of the Securities and Futures Ordinance.

# 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 nine months ended 31 December 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 21 to 25.

### 3. MEMBERS OF THE COMMITTEE

The members of the Committee during the nine months ended 31 December 2005 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 Fong, SBS, JP	[appointed on 21 June 2005]
Mr Gerald Greiner	
Mrs Alexa Lam	
Ms Anna HY Wu, SBS, JP	

### 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 nine months.

On behalf of the Committee

Martin Wheatley  
Chairman

27 January 2006

## Investor Compensation Fund

### Income and Expenditure Account

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited Three Months Ended		Unaudited Nine Months Ended	
		31 Dec 2005	31 Dec 2004	31 Dec 2005	31 Dec 2004
		\$'000	\$'000	\$'000	\$'000
<b>Income</b>					
Net investment income		19,850	23,117	55,355	34,708
Transaction levy from the SEHK		46,911	48,348	144,814	118,079
Contract levy from the HKFE		3,540	3,179	11,465	9,835
		<u>70,301</u>	<u>74,644</u>	<u>211,634</u>	<u>162,622</u>
<b>Expenses</b>					
ICC expenses	2	941	956	2,499	2,784
Auditors' remuneration		80	11	110	29
Bank charges		172	226	944	638
Professional fees		610	514	1,771	997
Exchange difference		521	3,677	5,503	4,032
Sundry expenses		-	-	1	1
		<u>2,324</u>	<u>5,384</u>	<u>10,828</u>	<u>8,481</u>
<b>Surplus</b>		67,977	69,260	200,806	154,141
<b>Accumulated surplus brought forward</b>		<u>486,308</u>	<u>239,490</u>	<u>353,479</u>	<u>154,609</u>
<b>Accumulated surplus carried forward</b>		<u>554,285</u>	<u>308,750</u>	<u>554,285</u>	<u>308,750</u>

The notes on page 25 form part of the condensed financial statements.

## Investor Compensation Fund

### Balance Sheet

At 31 December 2005

(Expressed in Hong Kong dollars)

	Unaudited At 31 Dec 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Current assets</b>		
Debt securities	1,297,770	1,182,665
Equity securities	137,355	122,409
Other receivable	-	384
Interest receivable	17,893	13,731
Due from ICC	2,490	1,111
Levy receivable from the SEHK	10,524	16,434
Levy receivable from the HKFE	657	1,283
Fixed and call deposits with banks	134,266	81,663
Cash at bank	56,721	37,295
	<u>1,657,676</u>	<u>1,456,975</u>
<b>Current liabilities</b>		
Accounts payable and accrued charges	713	818
	<u>713</u>	<u>818</u>
<b>Net current assets</b>	<u>1,656,963</u>	<u>1,456,157</u>
<b>Net assets</b>	<u>1,656,963</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	554,285	353,479
	<u>1,656,963</u>	<u>1,456,157</u>

The notes on page 25 form part of the condensed financial statements.



**Investor Compensation Fund**  
**Statement of Changes in Equity**  
**For the nine months ended 31 December 2005**  
*(Expressed in Hong Kong dollars)*

	Unaudited Nine Months Ended <u>31 Dec 2005</u> \$'000	Unaudited Nine Months Ended <u>31 Dec 2004</u> \$'000
<b>Compensation Fund balance as at 1 April</b>	1,456,157	962,209
<b>Surplus for the period</b>	200,806	154,141
<b>Contributions from UECF</b>	-	295,078
<b>Compensation Fund balance as at 31 December</b>	<u>1,656,963</u>	<u>1,411,428</u>

The notes on page 25 form part of the condensed financial statements.

## Investor Compensation Fund

### Cash Flow Statement

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Unaudited Nine Months Ended 31 Dec 2005 \$'000	Unaudited Nine Months Ended 31 Dec 2004 \$'000
<b>Cash flows from operating activities</b>		
Surplus for the period	200,806	154,141
Net investment income	(55,355)	(34,708)
Exchange difference	5,503	3,702
Decrease/ (increase) in levies receivable	6,536	(791)
Increase in amount due from ICC	(1,379)	(364)
(Decrease) / increase in accounts payable and accrued charges	(105)	689
<b>Net cash generated from operating activities</b>	156,006	122,669
<b>Cash flows from investing activities</b>		
Purchase of debt securities	(2,534,660)	(2,033,676)
Purchase of equity securities	-	(99,990)
Sale or maturity of debt securities	2,413,729	983,263
Sale of equity securities	472	136
Interest received	36,482	8,442
<b>Net cash used in investing activities</b>	(83,977)	(1,141,825)
<b>Cash flows from financing activities</b>		
Contributions received from UECF	-	295,078
<b>Net cash generated from financing activities</b>	-	295,078
<b>Net increase / (decrease) in cash and cash equivalents</b>	72,029	(724,078)
<b>Cash and cash equivalents at beginning of the nine months</b>	118,958	766,977
<b>Cash and cash equivalents at end of the nine months</b>	190,987	42,899
<b>Analysis of the balance of cash and cash equivalents:</b>		
	Unaudited At 31 Dec 2005 \$'000	Unaudited At 31 Dec 2004 \$'000
Cash at bank	56,721	356
Fixed and call deposits with banks	134,266	42,543
	190,987	42,899

**Investor Compensation Fund**  
**Notes to the Condensed Financial Statements**  
**For the nine months ended 31 December 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 nine months ended 31 December 2005, ICC incurred \$2,499,000 for its operation (For the nine months ended 31 December 2004 : \$2,784,000).

**3. CONTINGENT LIABILITIES**

As at the date of this report, the Fund has four outstanding claims against three 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 \$600,000 (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 nine months ended 31 December 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 27 to 32.

### 3. MEMBERS OF THE COMMITTEE

The members of the Committee during the nine months ended 31 December 2005 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 nine months.

On behalf of the Committee

Martin Wheatley  
Chairman

27 January 2006

## Unified Exchange Compensation Fund

### Income and Expenditure Account

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited Three Months Ended		Unaudited Nine Months Ended	
		31 Dec 2005 \$'000	31 Dec 2004 \$'000	31 Dec 2005 \$'000	31 Dec 2004 \$'000
<b>Income</b>					
Net investment income		548	87	1,252	853
Recoveries	2	1,405	4,236	2,295	15,007
Replenishments from SEHK	3	-	-	1	-
Provision for compensation reversed		121	1,232	106	4,763
		<u>2,074</u>	<u>5,555</u>	<u>3,654</u>	<u>20,623</u>
<b>Expenses</b>					
Auditors' remuneration		9	10	28	28
Bank charges		1	-	1	29
Professional fees		-	-	10	23
Sundry expenses		-	-	1	1
		<u>10</u>	<u>10</u>	<u>40</u>	<u>81</u>
<b>Surplus</b>		2,064	5,545	3,614	20,542
<b>Accumulated surplus / (deficit) brought forward</b>		<u>9,005</u>	<u>1,713</u>	<u>7,455</u>	<u>(13,284)</u>
<b>Accumulated surplus carried forward</b>		<u>11,069</u>	<u>7,258</u>	<u>11,069</u>	<u>7,258</u>

The notes on pages 31 and 32 form part of the condensed financial statements.

## Unified Exchange Compensation Fund

### Balance Sheet

At 31 December 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited At 31 Dec 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Current assets</b>			
Equity securities received under subrogation	2	632	7,793
Interest receivable		104	36
Fixed and call deposits with banks		56,681	47,028
Cash at bank		14	52
		57,431	54,909
		57,431	54,909
<b>Current liabilities</b>			
Accounts payable and accrued charges		4,251	4,291
Provision for compensation	4	440	1,492
		4,691	5,783
		4,691	5,783
<b>Net current assets</b>		52,740	49,126
<b>Net assets</b>		52,740	49,126
Representing:			
<b>Compensation fund</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		11,069	7,455
		1,047,458	1,043,844
Contributions to Investor Compensation Fund		(994,718)	(994,718)
		52,740	49,126

The notes on pages 31 and 32 form part of the condensed financial statements.

**Unified Exchange Compensation Fund**  
**Statement of Changes in Equity**  
**For the nine months ended 31 December 2005**  
*(Expressed in Hong Kong dollars)*

	Unaudited Nine Months Ended <u>31 Dec 2005</u> \$'000	Unaudited Nine Months Ended <u>31 Dec 2004</u> \$'000
Compensation Fund balance as at 1 April	49,126	323,815
Surplus for the period	3,614	20,542
Contributions refunded to the SEHK	-	(250)
Contributions to Investor Compensation Fund	-	(295,078)
Compensation Fund balance as at 31 December	<u>52,740</u>	<u>49,029</u>

The notes on pages 31 and 32 form part of the condensed financial statements.

**Unified Exchange Compensation Fund**  
**Cash Flow Statement**  
**For the nine months ended 31 December 2005**  
*(Expressed in Hong Kong dollars)*

	Unaudited Nine Months Ended <u>31 Dec 2005</u> \$'000	Unaudited Nine Months Ended <u>31 Dec 2004</u> \$'000
<b>Cash flows from operating activities</b>		
Surplus for the period	3,614	20,542
Net investment income	(1,252)	(853)
Decrease / (increase) in equity securities received under subrogation	7,161	(881)
Decrease in provision for compensation	(1,052)	(7,269)
Decrease in accounts payable and accrued charges	(40)	(261)
<b>Net cash generated from operating activities</b>	<u>8,431</u>	<u>11,278</u>
<b>Cash flows from investing activities</b>		
Debt securities redeemed	-	90,500
Debt securities sold	-	67,763
Interest received	1,184	5,595
<b>Net cash generated from investing activities</b>	<u>1,184</u>	<u>163,858</u>
<b>Cash flows from financing activities</b>		
Contributions refunded to the SEHK	-	(250)
Contributions to Investor Compensation Fund	-	(295,078)
<b>Net cash used in financing activities</b>	<u>-</u>	<u>(295,328)</u>
<b>Net increase / (decrease) in cash and cash equivalents</b>	9,615	(120,192)
<b>Cash and cash equivalents at beginning of the nine months</b>	47,080	167,622
<b>Cash and cash equivalents at end of the nine months</b>	<u>56,695</u>	<u>47,430</u>
<b>Analysis of the balance of cash and cash equivalents:</b>		
	Unaudited <u>At 31 Dec 2005</u> \$'000	Unaudited <u>At 31 Dec 2004</u> \$'000
Cash at bank	14	83
Fixed and call deposits with banks	56,681	47,347
	<u>56,695</u>	<u>47,430</u>



**Unified Exchange Compensation Fund**  
**Notes to the Condensed Financial Statements**  
**For the nine months ended 31 December 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 31 December 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 repealed 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 period, 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 nine months ended 31 December 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)
Less: 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 nine months ended 31 December 2005	(946)
Less: provision reversed during the nine months ended 31 December 2005	<u>(106)</u>
Balance as at 31 December 2005	<u><u>440</u></u>

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

**5. CONTINGENT LIABILITIES**

As at the date of this report, the SEHK has received claims against three 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 \$24 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 nine months ended 31 December 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 34 to 38.

### 3. MEMBERS OF THE COMMITTEE

The members of the Committee during the nine months ended 31 December 2005 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 nine months.

On behalf of the Committee

Martin Wheatley  
Chairman

## Commodity Exchange Compensation Fund

### Income and Expenditure Account

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Unaudited Three Months Ended		Unaudited Nine Months Ended	
	31 Dec 2005	31 Dec 2004	31 Dec 2005	31 Dec 2004
	\$'000	\$'000	\$'000	\$'000
<b>Income</b>				
Net investment income	4	1	10	1
	-----	-----	-----	-----
<b>Expenses</b>				
Auditors' remuneration	6	10	19	28
Bank charges	-	1	-	1
Professional fees	-	-	9	9
Sundry expenses	-	-	1	1
	-----	-----	-----	-----
	6	11	29	39
	-----	-----	-----	-----
<b>Deficit</b>	(2)	(10)	(19)	(38)
<b>Accumulated surplus brought forward</b>	108,211	108,234	108,228	108,262
	-----	-----	-----	-----
<b>Accumulated surplus carried forward</b>	<u>108,209</u>	<u>108,224</u>	<u>108,209</u>	<u>108,224</u>

The note on page 38 forms part of the condensed financial statements.

## Commodity Exchange Compensation Fund

### Balance Sheet

At 31 December 2005

(Expressed in Hong Kong dollars)

	Unaudited At 31 Dec 2005 \$'000	Audited At 31 Mar 2005 \$'000
<b>Current assets</b>		
Interest receivable	1	-
Fixed and call deposits with banks	456	488
Cash at bank	1	4
	458	492
<b>Current liabilities</b>		
Accounts payable and accrued charges	209	224
	249	268
<b>Net current assets</b>	249	268
<b>Net assets</b>	249	268
Representing:		
<b><u>Compensation fund</u></b>		
Accumulated surplus	108,209	108,228
Contributions to Investor Compensation Fund	(107,960)	(107,960)
	249	268

The note on page 38 forms part of the condensed financial statements.

**Commodity Exchange Compensation Fund**  
**Statement of Changes in Equity**  
**For the nine months ended 31 December 2005**  
*(Expressed in Hong Kong dollars)*

	Unaudited Nine Months Ended <u>31 Dec 2005</u> \$'000	Unaudited Nine Months Ended <u>31 Dec 2004</u> \$'000
Compensation Fund balance as at 1 April	268	302
Deficit for the period	(19)	(38)
	<hr/>	<hr/>
Compensation Fund balance as at 31 December	<u>249</u>	<u>264</u>

The note on page 38 forms part of the condensed financial statements.

## Commodity Exchange Compensation Fund

### Cash Flow Statement

For the nine months ended 31 December 2005

(Expressed in Hong Kong dollars)

	Unaudited Nine Months Ended 31 Dec 2005 \$'000	Unaudited Nine Months Ended 31 Dec 2004 \$'000
<b>Cash flows from operating activities</b>		
Deficit for the period	(19)	(38)
Net investment income	(10)	-
Decrease in accounts payable and accrued charges	(15)	-
	<hr/>	<hr/>
<b>Net cash used in operating activities</b>	<u>(44)</u>	<u>(38)</u>
<b>Cash flows from investing activities</b>		
Interest received	9	-
	<hr/>	<hr/>
<b>Net cash generated from investing activities</b>	<u>9</u>	<u>-</u>
<b>Net decrease in cash and cash equivalents</b>	(35)	(38)
<b>Cash and cash equivalents at beginning of the nine months</b>	492	529
	<hr/>	<hr/>
<b>Cash and cash equivalents at end of the nine months</b>	<u>457</u>	<u>491</u>
<b>Analysis of the balance of cash and cash equivalents:</b>		
	Unaudited At 31 Dec 2005 \$'000	Unaudited At 31 Dec 2004 \$'000
Cash at bank	1	4
Fixed and call deposits with banks	456	487
	<hr/>	<hr/>
	<u>457</u>	<u>491</u>

## Commodity Exchange Compensation Fund

### Notes to the Condensed Financial Statements

For the nine months ended 31 December 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 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.