

SFC's reply to Legco Secretariat's list of follow-up actions dated 31 March 2011

- 1. In respect of the complaints against financial institutions on mis-selling of Lehman Brothers Minibonds and related structured products, information on the legal basis, mode and present position of the co-operation between SFC and the Commercial Crime Bureau of the Police in the investigation of relevant cases.**

The SFC maintains close working contact with the Commercial Crime Bureau and holds regular joint liaison meeting to discuss cases of common interests. There is a mechanism in place for mutual assistance and referral of cases between the two organisations. In the case involving Lehman Brothers Minibonds, such mechanism had been followed.

- 2. Details of the arrangements for internships, and the turnover situation of graduate interns in recent years.**

The SFC is strongly dedicated to nurturing and developing the future leaders of the organisation from within. The Graduate Trainee Programme (GTP) is our structured response to this commitment and a primary source of the young talent for our organisation. Graduate Trainees hired through the GTP are young and high-potential individuals with an exceptional drive for public service and challenge. Through our 3-year custom-designed training and development programme, we aim to developing them into more senior executives who can support and lead the Commission's future operations.

Graduate Trainees proceed through a structured curriculum of development and progression. For the first two years, they rotate through different functional attachments before settling into a specific division in their third year. Graduate Trainees who satisfactorily complete the programme by end of the 3rd year will be promoted to Assistant Manager with opportunities for further progression to other executive roles.

With a view to building a stronger management pipeline for the future, a total of 30 high calibre graduates had been recruited in 2009 and 2010.

Since inception to date, the retention rate for our Graduate Trainees is 94%.

- 3. Given the significant increases in headcounts and staff costs over the years from 2008-09 to 2011-12, information on the reasons for such marked increases, with details of the increases in workload and new initiatives in various work areas.**

Shown in the table below of the information on headcounts and staff costs:

Year 2008-09	(a)	2010-11	Changes		2011-12	Changes	
		(b)	<u>(b)-(a)</u>		(c)	<u>(c)-(a)</u>	
			(a)	%		(a)	%
Headcount	507	587	+80	15.7	648	+141	27.8
Staff cost (HK\$'M)	574	634	+60	10.5	728	+154	26.8

The increase in staff cost is mainly due to the increase in budgeted headcount, which is barely sufficient for the Commission to cope with the increase in workload arising from the continuous growth in financial markets and licensed intermediaries and to support new initiatives to strengthen the regulatory environment in response to changes in the regulatory and financial market landscape. As at 31 March 2011, while the budgeted headcount had increased by 15.7% over the past 3 years, the number of listed securities¹, number of applications to conduct new regulated activities and number of enforcement cases had increased by 51%, 19% and 259% respectively.

New initiatives introduced by the Commission over these years include:

Following the financial crisis in 2008, we introduced new measures to strengthen the regulatory regime governing the sale of investment products. These included new advertising guidelines and revised product codes for collective investment schemes, a new product code for unlisted structured investment products, new requirements for intermediaries to enhance intermediary conduct and selling practices for investment products and a new licensing regime for credit rating agency.

The number of cases handled by our Enforcement Division had increased from 112 in 2008-09 to 402 as at 31 March 2011. We commit to using all available tools to enhance investor protection and to reduce crime and market misconduct. We have for the first time obtained a high court order directing a listed company to commence civil proceedings to seek recovery of compensation for the loss and damage suffered by the company as a result of directors' misconduct. We intervened and be heard in PCCW privatisation court proceedings and applied for interim injunction to freeze assets of a listed company. We commenced for the first time criminal proceedings against individuals for market misconduct including insider dealing which resulted in first immediate jail sentence.

On regulation of listed companies, we consulted the market on the draft guidelines on disclosure of inside information which will be published when the proposed legislation on the price sensitive information disclosure is enacted. We together with the Hong Kong Exchanges and Clearing Limited (HKEx) had also conducted consultation on proposals to streamline property valuation requirements and issue of paper application form with electronic prospectuses.

¹ Data extracted from HKEx's website

On market supervision, we proposed an operating model for scripless securities and adopted a new short-position reporting regime. We worked closely with the HKEx to prepare for the listing of Renminbi (RMB) products. We are working with other stakeholders to build a regulatory regime for OTC derivatives markets.

To increase the depth and breadth of the markets and raise Hong Kong's standing as an international financial centre, we made further inroads to promote exchange-traded funds (ETFs) in Hong Kong by launching a series of China A-share ETFs and arranging with Taiwan to cross-list ETFs. We work closely with the Government and Mainland regulatory authorities to solidify Hong Kong's status as an offshore RMB centre. We authorised the first RMB-denominated fund last year. Also, the first RMB REIT will soon be listed.

The work and initiatives undertaken by the Commission over the past years as described above are not exhaustive. More information can be found in our annual reports, newsletters and press releases which are publicly accessible through our website.

4. In view of the large increase in Professional and Other Expenses, detailed information on the increase in demand for external expert services with a breakdown by the relevant work areas.

Professional and Others Expenses for 2011-12 comprise mainly legal fees (\$22 million) and external professional services (\$30.6 million). The apparent large increase in the 2011-12 budget for Professional and Other Expenses is mainly because, as explained in paragraphs 2.3.4 and 4.2.6 of the Budget Book, Professional and Others Expenses for 2010-11 were forecast to be lower than the approved budget as we had recovered significant amount of legal costs during the year. As we do not expect any significant recovery of legal costs in 2011-12, Professional and Others Expenses are consequently increased as compared with the forecast. If the same amount of legal fees recovery for 2010-11 were received in 2011-12, the increase in Professional and Other Expenses for 2011-12 would be reduced from 28.85% to 8.76%.

In 2011-12, we have budgeted for external professional services in the following work areas:

Investigation	\$13.5 million
Intermediaries supervision	\$4.5 million
Investment products	\$4.0 million
Human Resources	\$3.6 million
Takeovers panel	\$1.0 million
Others	\$4.0 million