

## **NOTE FOR FINANCE COMMITTEE**

### **The Budget of the Securities and Futures Commission for the Financial Year 2014-15**

#### **PURPOSE**

In accordance with the consultation procedures agreed with the Legislative Council (LegCo) when the Securities and Futures Commission (SFC) was established<sup>1</sup>, this note briefs Members on the main features of the budget of SFC for 2014-15<sup>2</sup>.

#### **BACKGROUND**

2. Section 13(2) of the Securities and Futures Ordinance (Cap. 571) (SFO) requires SFC to submit estimates of its income and expenditure (the budget) for each financial year to the Chief Executive for approval. The Chief Executive has delegated the authority to the Financial Secretary (FS). In accordance with section 13(3) of SFO, FS shall cause the budget to be laid on the table of LegCo. On 7 February 2014, this Bureau and SFC briefed the Panel on Financial Affairs (FA Panel) on SFC's proposed budget for 2014-15. A copy of the budget for 2014-15 is at Enclosure.

Encl.

#### **FUNDING OF SFC**

3. Section 14 of SFO provides that the Government shall provide funding to SFC as appropriated by LegCo. In practice, SFC has not requested appropriation from LegCo since 1993-94. The funding of SFC comes from the market in the form of transaction levies, and fees and charges on services rendered to market operators and participants.

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<sup>1</sup> Members may refer to FCR(89-90)12 for details.

<sup>2</sup> The financial year of SFC starts on 1 April 2014 and ends on 31 March 2015.

4. Over the years, levies on securities transactions and futures/options contracts trading have been the main source of income for SFC. The current rate of levy<sup>3</sup> on securities transactions is 0.0030% while that on futures/options contracts is \$0.60 or \$0.12 per leviable transaction, depending on the type of contracts.

## BUDGET FOR 2014-15

5. SFC has projected a budget deficit of \$508.68 million for 2014-15. As in past years, SFC does not request any appropriation from LegCo for the 2014-15 budget. The main features of the 2014-15 budget are set out in paragraphs 6 to 15 below.

### Income

6. The estimated income for 2014-15 is \$1,161.79 million, which is \$37.52 million (3.3%) above the forecast income for 2013-14 (\$1,124.27 million). SFC has adopted the following assumptions in projecting the estimated income –

- (a) the average securities market turnover will be \$65 billion per day and the average futures/options market turnover will be 270 000 contracts per day;
- (b) the levy rate will be reduced by 10% tentatively with effect from October 2014 (from 0.0030% to 0.0027% for securities transactions and from \$0.60 or \$0.12 per contract to \$0.54 or \$0.108 per contract for futures/options contracts, depending on the type of contracts); and
- (c) the annual licensing fee holiday will be extended for another period of two years, with effect from 1 April 2014.

### Expenditure

7. The estimated expenditure for 2014-15 is \$1,670.47 million, which is \$245.49 million (17.2%) above the forecast expenditure for 2013-14 (\$1,424.98 million). The increase is mainly attributable to –

- (a) increase in staff cost by \$161.66 million (17.8%) arising mainly from –

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<sup>3</sup> Under section 394 of SFO, the Chief Executive in Council may specify the rates of levy for sale and purchase of securities recorded on a recognised securities market or futures contracts traded on a recognised futures market.

- (i) a provision of \$66 million for 51 new headcounts for four principal areas where the regulatory and supervisory framework needs to be strengthened, namely regulation and supervision of markets, listed companies and intermediaries; cooperation with Mainland China; compliance with new international standards on financial market infrastructures; and enhancing litigation capacity for the enforcement of securities regulation. Details are set out in paragraph 8;
  - (ii) a provision of \$49.01 million for annual pay adjustment, i.e. an amount approximately equivalent to 5.5% of personnel costs; and
  - (iii) a provision of \$13.16 million for 36 position upgrades for different divisions and departments;
- (b) increase in funding to external parties by \$34.7 million (55.3%). This includes an increase in provision from \$3.37 million to \$20 million for providing financial support to training initiatives offered by the Hong Kong Securities and Investment Institute (HKSI) and other institutions. These training initiatives are for intermediaries, particularly small and medium-sized firms, to meet the challenges arising from a changing market landscape;
- (c) increase in expenses on professional and others by \$13.91 million (14.8%) as the demand for external legal and expert services remains high, especially in the areas of investigation, supervision of intermediaries and authorization of new products; and
- (d) increase in expenses on information and systems services by \$10.16 million (23.0%) due to higher software and hardware maintenance costs after the lapse of warranty periods and increases in subscriptions for market data to support enforcement and supervision activities. New systems are required by the operating divisions to manage their caseloads and to enhance their investigatory and supervisory capabilities.

### Manpower Plan

8. In addition to the originally proposed 47 headcount increase for 2013-14, SFC added 11 posts as interim headcount addition during the year to support the work resulting from the expansion of its regulatory remit and the additional regulatory and oversight responsibilities. With this interim headcount addition, SFC now has a total headcount of 794<sup>4</sup>. SFC proposes another 51 new posts in the budget of 2014-15, and the total headcount will be 845<sup>4</sup>. The new

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<sup>4</sup> Not including seven posts in the Investor Education Centre, which is a wholly-owned subsidiary of SFC.

positions are required mainly to cope with the increase in workload in the following areas –

- (a) **Intermediaries Division** (13 posts) – to keep pace with the anticipated increase in the number of licensed corporations and to maintain the cycle of on-site inspections, to cater for the expansion of the anti-money laundering team, to assist in general policy development and devise new supervisory approaches for the licensing and supervision of intermediaries, to support specific policy work, and to deal with the marked and steady increase in licensing applications;
- (b) **Supervision of Markets Division** (nine posts) – to enhance the supervisory approach to the Hong Kong Exchanges and Clearing Limited, to handle initiatives including over-the-counter derivatives regulation and uncertificated securities market, and to cater for growing volume of policy work arising from SFC's active involvement in global regulatory developments and interactions with peer regulators;
- (c) **Corporate Finance Division** (eight posts) – to support work resulting from the expansion of SFC's regulatory remit and the additional regulatory and oversight responsibilities, in particular the creation of a new corporate regulation team which aims to provide SFC with a broader and more proactive oversight of listed companies;
- (d) **Legal Services Division** (eight posts) – to enhance SFC's litigation capacity to provide in-house legal advice for supporting investigations and litigation cases requiring priority treatment;
- (e) **Enforcement Division** (six posts) – to address the need for more staff to provide support for resource intensive work resulting from the increasing number and complexity of investigations undertaken by the division;
- (f) **Investment Products Division** (five posts) – to support work relating to Mainland-Hong Kong fund mutual recognition, implementation of product design measures, and heightened monitoring of SFC-authorized funds and suspected collective investment schemes; and
- (g) **Corporate Affairs Division** (two posts) – to cater for increase in workload arising from the appointment of external fund managers for the day-to-day monitoring of SFC's investment portfolio and to meet the anticipated increase in administrative workload.

9. In addition, SFC stresses that given the highly uncertain environment in which they currently operate, there is a need to recognize the possibility of unanticipated additional resource requirements closer to the time of the implementation of new initiatives (e.g. the development of Shanghai-Hong Kong Stock Connect), as well as new or expanded regulatory mandates. Should any such matters arise, they will be dealt with through a separate interim budget request.

### **Capital Expenditure**

10. The total capital expenditure proposed for 2014-15 is \$63.56 million, which is \$14.49 million (29.5%) above the forecast expenditure for 2013-14 (\$49.07 million). Provisions for major capital items include the following and a 10% contingency –

- (a) computer systems development – for “front-end” technology to upgrade market surveillance capabilities, improve access and exchange of information between stakeholders and SFC, and enhance various IT systems (\$33.81 million);
- (b) office equipment and vehicle – for replacement of obsolete office equipment and vehicle due to normal wear and tear and for investment in storage technology and data base capacity plus costs relating to the normal replacement of obsolete servers and computer equipment for the additional headcount (\$16.37 million); and
- (c) office furniture and fixtures – for leasing additional office space to meet growth in headcount and for replacement of obsolete furniture due to normal wear and tear (\$7.6 million).

### **Reserves**

11. SFC has estimated that by 31 March 2014, the reserves will reach \$7,154.92 million, which is 5.02 times of its projected operating expenditure for 2013-14 (\$1,424.98 million).

12. According to section 396 of SFO, SFC may, after consultation with FS, recommend to the CE-in-Council that the rate or amount of levy be reduced if the reserves of SFC are more than twice its estimated operating expenses for that financial year. As stated in paragraph 6(b) above, SFC proposes to reduce the levy rate for transactions of securities and futures/options contracts. The proposed

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reduction is targeted to take effect in the fourth quarter of 2014<sup>5</sup>. This will involve revenue foregone estimated at \$52.38 million for 2014-15. SFC effected a levy reduction of 20% in December 2006 and a further 25% in October 2010.

13. SFC also proposes to extend the annual licensing fee holiday for another period of two years with effect from 1 April 2014 (paragraph 6(c) above). The proposal will involve revenue foregone estimated at \$340 million for the two years. SFC offered an annual licensing fee holiday for one year effective on 1 April 2009, and for two years effective on 1 April 2012.

14. Taking into account the proposed levy reduction and the annual licensing fee holiday, the reserves of SFC are expected to reduce from \$7,154.92 million by the end of 2013-14 to \$6,646.24 million by the end of 2014-15.

15. In proposing the levy reduction, SFC has pointed out that given the uncertainty in local market turnover level and the expected increase in regulatory costs, it will continue to incur an operating deficit in future. Unless stock market turnover substantially increases, this further reduction in the levy rate will aggravate SFC's projected operating deficits in future years. To ensure that SFC is financially sustainable, the levy rate may need to be increased if the reserves are depleted to the level of two times the annual operating expenditure.

## **COMPARISON OF THE ORIGINAL BUDGET WITH THE FORECAST BUDGET FOR 2013-14**

### **Income**

16. The forecast income for 2013-14 is \$1,124.27 million, which is \$55.14 million (5.2%) more than the original budget of \$1,069.13 million. The higher income is mainly due to higher actual market turnover in the first six months of 2013-14<sup>6</sup>.

### **/Expenditure .....**

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<sup>5</sup> As the rate of a levy is provided in the Securities and Futures (Levy) Order (Cap. 571, sub. leg. Z), amendments have to be made to this Order before the transaction levies could be reduced.

<sup>6</sup> The revised income for 2013-14 is projected based on the prevailing market performance and the assumption that the average daily turnover of securities transactions and futures/options contracts transactions is \$60 billion per day and 250 000 for the remainder of 2013-14. The original budget is made based on assumptions of \$54 billion per day and 238 000 per day.

## **Expenditure**

17. The forecast expenditure is \$1,424.98 million, which is \$79.31 million (5.3%) below the original budget of \$1,504.29 million. The underspending is mainly due to time lag experienced in filling vacancies, lower-than-expected increase in management fees for premises and information and systems services, savings in general office and insurance expenses and overseas travelling, and deferment of some training and development activities, etc.

## **Capital Expenditure**

18. The forecast capital expenditure is \$49.07 million, which is \$13.18 million (21.2%) below the original budget of \$62.25 million, as a result of savings in fitting-out work, which is partially offset by the renovation costs for new office space to cater for the new corporate regulation team.

## **PUBLIC CONSULTATION**

19. The Administration and SFC briefed FA Panel on SFC's 2014-15 budget on 7 February 2014. Members generally welcomed the budget.

## **ADMINISTRATION'S VIEWS**

20. The Administration has examined the budget of SFC for 2014-15. We note that SFC has proposed to reduce its levy rate by 10% and extended the annual licensing fee holiday for two years with effect from 1 April 2014, and will continue to provide financial support for training initiatives offered by the HKSI and other institutions. SFC has projected a deficit in its budget, and as in the past years, it has not requested appropriation from LegCo.

21. We note that SFC has pointed out that it is projecting an operating deficit in the next few years, and that it would need to consider increasing the levy rate if its reserves are depleted substantially (paragraph 15 above). Having regard to the need for SFC to maintain a healthy financial position on the one hand, and the benefit the reduction will bring to the general investing public and the financial industry on the other, we consider the proposed levy reduction reasonable.

22. We have proposed to SFC to consider setting aside part of its reserves for acquisition of office premises as a long-term measure to enhance stability and certainty in the delivery of its services through economic cycles.

23. It is a public commitment of SFC, as a publicly funded organization, to deploy its resources and control its expenditures in a prudent manner. In this regard, we note SFC's increase in staff establishment to cope with new and increasing regulated activities over the years. We look forward to SFC's continued effort in redeploying existing resources to deal with extra workload and new regulatory initiatives.

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Financial Services and the Treasury Bureau  
May 2014





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

**Enclosure to FCRI(2014-15)1**

**Securities and Futures Commission**  
**Budget of Income and Expenditure**  
**for the financial year 2014/2015**

24 December 2013



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## 1. Executive summary

1.1 Each year the budget is prepared based on a policy of tightly controlling all expenditures, as befits a publicly funded organization. Prior year expenditure levels are used as a benchmark except in areas where additional resources have been identified as necessary to meet our regulatory obligations and objectives or to support new initiatives and regulatory development. Strict controls are applied to ensure that costs stay within budget commitments.

1.2 Set out below is a summary of the Commission's forecast for 2013/14 and proposed budget for 2014/15. This summary is intended to give an overview of our proposed budget. For more detailed explanations, reference should be made to sections 4 and 5 of this budget book.

	2014/15	2013/14	Variance	
	Proposed Budget (a) HK\$m	Forecast (b) HK\$m	Proposed Budget vs. Forecast (c) = (a-b) HK\$m	(c/b) %
<b>Income</b>	<b>1,161.79</b>	1,124.27	37.52	3.3%
<b>Recurrent expenditure</b>				
Staff cost	1,070.32	908.66	161.66	17.8%
Premises expenses	227.79	216.66	11.13	5.1%
Other recurrent expenses	274.86	236.86	38.00	16.0%
Total recurrent expenditure	1,572.97	1,362.18	210.79	15.5%
<b>Funding to external parties</b>	<b>97.50</b>	62.80	34.70	55.3%
Total expenditure	1,670.47	1,424.98	245.49	17.2%
<b>Deficit for the year</b>	<b>(508.68)</b>	(300.71)	(207.97)	69.2%

1.3 For 2014/15 we project that income will increase by \$37.52 million (3.3%) over the 2013/14 Forecast as a result of higher assumed securities market turnover, higher fees and charges and investment income.

1.4 We have carefully considered the issue of whether we should reduce the levy in light of the level of our reserves. Having taken into consideration prevailing market conditions, the size of our reserves, our expected resource requirements and medium-term financial projections, we propose to reduce the Commission's transaction levy by 10% in 2014/15. It should however be noted that unless the stock market turnover substantially increases, the reduction in levy rate will aggravate the Commission's projected operating deficits in future years. To ensure that the Commission is financially sustainable, we would need to increase the levy rate if our reserves are depleted to the level of two times our annual operating expenditure.

1.5 We are mindful that market participants have been operating in a stressed environment amid high levels of volatility, uncertainty over the global economy and sluggish turnover in recent months. We therefore propose extending our fee holiday for another two years for all annual license fees payable during the two-year period commencing 1 April 2014. The annual licence fee holiday will provide a degree of financial relief for licensed intermediaries, particularly smaller firms.



- 1.6 Expenditure for 2014/15 is expected to increase by \$245.49 million (17.2%) over the 2013/14 Forecast. The increase is mainly attributable to increases in staff costs (\$161.66 million), funding to external parties (\$34.70 million) and other recurrent expenses (\$38 million).
- 1.7 As set out in Section 3, the Commission's budget for 2014/15 is premised on the need to ensure that the Commission is adequately resourced to effectively and efficiently carry out its responsibilities amid an increasingly demanding local and global regulatory environment.
- 1.8 Specific initiatives such as enhanced supervision of the Hong Kong Exchanges and Clearing Limited (HKEx) and the expansion of the Commission's role in the area of corporate regulation will inevitably require more resources in the coming year.
- 1.9 Having critically reviewed the manpower needs of the Commission's operating divisions and departments for 2014/15, a net increase of 51 full time posts (6.4%) over the Commission approved headcount of 2013/14 has been included in the budget. 5 of these posts are reserved for existing graduate trainees (GTs) to progress upon completion of three rotations within the first two years of the Graduate Trainee Programme. Apart from this, 36 position upgrades are requested to reflect the expansion in scope and complexity of our work.
- 1.10 Given the highly uncertain environment in which we currently operate, there is a need to recognize the possibility of unanticipated additional resource requirements closer to the time of the implementation of new or expanded regulatory mandates. Should any such matters arise, they will be dealt with through a separate interim budget request.
- 1.11 The Commission has attempted, wherever possible, to redeploy existing resources to deal with extra workload or new regulatory initiatives anticipated in the next budget year. For initiatives that are currently in a consultative or preliminary stage, existing resources will be deployed to the extent possible. Please refer to Section 4 for more detailed information about the Commission's 2014/15 manpower plan.
- 1.12 Whilst there are segments within the Hong Kong financial services market that have been subject to downsizing, streamlining and/or offshoring, the demand for compliance and risk focused specialists remains high. The elevated demand for these professionals is due to the shortage of suitably qualified people in these areas and the growing regulatory demands placed upon institutions as a result of ongoing global regulatory reform. This has implication for recruitment and retention at the Commission.
- 1.13 Other recurrent expenses for 2014/15 are expected to increase by \$38 million over the 2013/14 Forecast. This increase is mainly due to higher professional and other similar expenses (\$13.91 million), information and systems services expenses (\$10.16 million) and depreciation expenses (\$8.5 million).
- 1.14 We have set aside \$20 million in our 2014/15 budget for funding training initiatives for intermediaries, particularly small and medium-sized firms, to meet the challenges arising from a changing market landscape.
- 1.15 A deficit of approximately \$508.68 million is expected in 2014/15 leaving our overall reserves at \$6.6 billion at the end of that financial year, approximately 4 times our annual costs including depreciation and funding to various external parties.



## 2. Assumptions

### 2.1 Investor levy rates

2.1.1 We have included a 10% cut in the levy rate with effect from mid 2014/15, tentatively 1 October 2014, for budget purposes, i.e.

(a) Investor Levy Rate – Securities will be reduced from 0.003% to 0.0027%; and

(b) Investor Levy Rate - Future/Options contracts will be reduced from \$0.6/\$0.12 per contract to \$0.54/\$0.108 per contract, depending on the type of contract.

### 2.2 Market turnover

#### 2.2.1 Equity market

Based on the prevailing market performance, the average securities market turnover is assumed to be \$60 billion/day for the remainder of 2013/14 and \$65 billion/day for 2014/15.

#### 2.2.2 Futures and Options market

Based on the transaction volumes for the first six month of 2013/14 (Apr – Sep 2013), the futures/options market turnover is assumed to be an average of 250,000 contracts per day for the rest of 2013/14. For forecasting purposes we have assumed that volumes will increase in line with the estimated increase in the securities market turnover. On this basis, the futures/options market turnover is assumed to be an average of 270,000 contracts per day in 2014/15.

### 2.3 Fees and charges

2.3.1 We propose to extend the two-year annual fee waiver for licensees for 2014/15 and 2015/16. This will apply to all annual fees payable during the two-year period commencing 1 April 2014 on terms that will be announced during March 2014. The underlying rates of fees and charges, which will continue to apply to all new license applications, are assumed to remain unchanged.

### 2.4 Rate of return

2.4.1 The average gross return on investment of our reserve funds before investment management fees is assumed to be 1.5% p.a. for the year 2014/15.

### 2.5 Remuneration adjustment

2.5.1 A provision of 5.5% of personnel costs has been included as salary adjustments for staff (see also 5.4.2 (c)).



2.5.2 In arriving at the provision, the Commission has considered a number of factors including but not limited to, macro-economic factors (projected CPI & GDP), relevant industry remuneration trends for 2014/15, the labour market demand for the type of expertise required by the Commission as well as merit adjustments.

## 2.6 Inflation

2.6.1 Where an estimate of general price level increases is required we have assumed 4%<sup>1</sup> when we do not have specific data and/or quotes on which to estimate our future costs.

## 2.7 Capital expenditure

2.7.1 Capital expenditure is budgeted based on the level of expenditure which will be 'committed to' within a financial year. However, actual expenditure incurred will differ from this and the approved estimates of capital expenditure for different capital projects will, as previously, be carried forward until the completion of the projects.

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<sup>1</sup> Based on the latest statistics released by the Census and Statistics Department in October 2013, the year-on-year rate of increase in the Composite CPI after netting out of the effects of all Government's one-off relief measures, was 4%.



### **3. Global and domestic regulatory challenges**

#### **3.1 Key challenges faced by the Commission are:**

##### **3.1.1 Increasing market complexity**

- (a) The sophistication and complexity of the securities and futures market, and its participants, has increased as (i) the Hong Kong market continues to evolve and expand; and (ii) Hong Kong responds to post-financial crisis global regulatory reforms and responses. For example, on-site inspection work (with increased use of new supervisory tools such as thematic inspections and surveys) and off-site inspection monitoring has become more complex.
- (b) The unique nature of the Hong Kong market, with a continued large and diverse number of small to medium size intermediaries, with significant retail penetration, requires a resource intensive supervisory approach.
- (c) Market participants are increasingly becoming more sophisticated. The growth of particular segments of the market (e.g. asset management), and increasing automation of trading and operations, as well as the international nature of many licensed corporations (LCs) all have resource implications for the Commission.
- (d) Credible enforcement of our laws and regulations is crucial to Hong Kong's status as an international financial centre. Our enforcement strategy will continue to focus on remedial and punitive outcomes, using the disciplinary provisions of the Securities and Futures Ordinance, the civil courts, criminal prosecutions and the Market Misconduct Tribunal (MMT).
- (e) HKEx is transitioning into a vertically-integrated multi-asset class exchange. HKEx is also looking to deepen relationships with Mainland exchanges and clearing houses. In view of these developments, the Commission is developing a new supervisory approach for HKEx, including regular on-site reviews of HKEx operations.
- (f) Following a recent reform to strengthen the regulation of listed companies (such as the new inside information regime) and IPO sponsors, the Commission has decided to use its existing powers under the SFO to pursue a more structured and active role as a regulator of listed company conduct. This does not require new legislation but, rather, its purpose is to bring together the relevant elements of the SFO under a new staffing structure and strategy which transforms Commission into a proactive corporate regulator involving surveillance, analysis and enforcement against misconduct. This will enhance Commission's role in promoting a quality listed market.



- (g) Changes are also significant in the development and regulation of funds, asset managers and investment products; the Commission will continue to be involved in the development of new initiatives for Hong Kong domiciled funds as well as mechanisms for cross-border access. It will also pursue ways to better protect investors, including regulatory expectations of financial institutions which manufacture products for retail. This reflects a greater focus by international regulators in this area.

### 3.1.2 Relationships with Mainland China

- (a) Hong Kong is a hub for international capital flows between the Mainland and the rest of the world. Continued capital market opening together with a broader range of RMB products will enhance Hong Kong's position as a gateway for accessing Mainland capital and wealth, and provide more channels for investing in the Mainland market.
- (b) At the same time, it is vital that our ability to protect investors and enforce effectively is maintained. The Commission will closely monitor financial stability risks and financial conduct risks as the two markets become more inter-connected.

### 3.1.3 International regulatory developments

- (a) International financial regulators and standard setters such as the Financial Stability Board (FSB) and International Organizations of Securities Commissions (IOSCO) are all committed to a fundamental reform of the financial system to correct the fault lines that led to the global financial crisis and to rebuild a safer, more resilient financial system that better serves real economies. These reforms are essential components of the G20's primary objective of strong, sustainable and balanced growth.
- (b) A major area of reform is to make OTC derivatives markets safer by introducing requirements for reporting of all OTC derivatives trades to trade repositories, adopting rules for central clearing and trading on organised platforms, where appropriate, and adopting resolution regimes for systemically important financial institutions and financial market infrastructures (FMIs) such as central counterparties (CCP). The Commission and HKMA have worked jointly on a Bill, which is now before the legislature, to introduce a new regulatory regime for OTC derivatives markets in Hong Kong.
- (c) The global financial crisis has caused government and regulators to focus on "systemically important financial institutions" (SIFIs), which has led to a number of initiatives to address "too-big-to-fail". The term "resolution regime" encompasses measures to stabilise a SIFI as well as measures to handle a non-viable SIFI with the least disruption. It was also recognised that the services provided by individual FMIs have a critical role in supporting activity in the financial markets as well as individual financial institutions (FIs). Failure of an FMI may disrupt these activities resulting in uncertainty and losses for FIs and





may thus have an adverse impact on financial stability. The Commission is currently working with the Government and other regulators to develop a statutory resolution regime that provides for additional resolution powers via a common framework that is applicable to firms in different financial sectors and to FMIIs.

- (d) The G20 is committed to enhancing cross-border co-operation. The FSB notes that this can be achieved in some areas by market regulators establishing agreements for deferring to each other's rules when these produce similar outcomes. The application of consistent rules across jurisdictions in a non-discriminatory way is essential for today's global markets, and is an area of work in which the Commission is closely involved.
- (e) The Commission, in June 2013, took up chairmanship of the newly created IOSCO Task Force on Cross-Border Regulation, which has the ambitious mandate to address challenges in regulating cross-border activities in securities markets. To galvanize the "Asia voice" in the formulation of international regulatory standards, the Commission is the current chair of the IOSCO Asia-Pacific Regional Committee (APRC). The Commission believes that greater regional collaboration amongst Asian jurisdictions on matters of common interest enables Asia to influence global policy making and to ensure it takes account of different types of markets and aspirations in the region. We always ensure that our involvement in international policy work is fully aligned with Hong Kong's interest as a leading financial centre.



## 4. Manpower plan

### 4.1 Proposed headcount changes 2014/15 vs 2013/14

Division	Headcount					
	Commission Approved 2013/14	Proposed 2014/15	Net Change	Executive Posts	Non-Executive Posts	Para /ref
Centralised Services <sup>Note 1</sup>	31	31	-	-	-	-
Corporate Finance	74	82	+8	8	-	4.3.3-4.3.4
Enforcement	172	178	+6	1	5	4.3.5-4.3.8
Intermediaries <sup>Note 2</sup>	230	243	+13	8	5	4.3.9
Legal Services	36	44	+8	6	2	4.3.10-4.3.12
Investment Products <sup>Note 3</sup>	106	111	+5	4	1	4.3.13-4.3.15
Supervision of Markets	40	49	+9	7	2	4.3.16-4.3.19
Corporate Affairs	105	107	+2	1	1	4.3.20-4.3.21
<b>TOTAL</b> <sup>Note 6</sup>	<b>794</b> <sup>Note 4</sup>	<b>845</b>	<b>51</b> <sup>Note 5</sup>	<b>35</b>	<b>16</b>	

Note 1 : Include CEO's Office, Risk and Strategy Unit, International & China Unit, Secretariat and Press Office.

Note 2 : Following the appointment of a new Executive Director in June 2013, the Intermediaries Supervision Department and the Licensing Department were combined under a single Division referred to as the Intermediaries Division. One headcount from CEOO was transferred to Intermediaries Division in June 2013.

Note 3 : In February 2013, 6 posts were transferred from the Policy, China & Investment Products Division to the International & China Unit of CEOO. The division was subsequently renamed Investment Products Division.

Note 4 : The Commission approved headcount includes 11 interim headcount.

Note 5 : Including 5 posts for the placement of graduate trainees.

Note 6 : The Commission has proposed 36 post upgrades for 2014/15 (including one upgrade for the CEOO)

#### 4.1.1 Implications of the global and domestic regulatory challenges on Commission's manpower resources:

- (a) The evolving regulatory landscape, marked by an increased interconnection with the Mainland, global financial reforms, an active presence of international players and increased regional competition to Hong Kong's position as an international financial center necessitated the Commission to respond to these challenges through new approaches, while optimizing its capacity to deliver its increasing responsibilities in an effective and efficient manner.
- (b) In arriving at the manpower plan for 2014/15, the Commission has undertaken a comprehensive assessment of our manpower needs by considering various factors such as anticipated workload, future challenges, headcount prioritisation and retraining and redeployment of current resources.
- (c) The unpredictable outlook for economic conditions and financial markets, coupled with the regulatory reforms and initiatives as set out



in paragraph 4.3, may however result in the need for additional resources later in the year.

#### 4.1.2 Key focus areas

- (a) The 2014/15 manpower requests reflect four principal areas where the regulatory and supervisory framework needs to be strengthened in the short-term :
  - (i) **Regulation and supervision of markets, listed companies and intermediaries** – this concerns the rapid and ambitious evolution of the business model of the HKEx, the introduction of a regime for the regulation of OTC derivatives in Hong Kong, the expanded role of the Commission as a regulator of listed companies and new approaches to driving a compliance culture within licensed intermediaries;
  - (ii) **Integration with Mainland China** – the risks and opportunities for the Hong Kong SAR in response to closer linkages with Mainland China;
  - (iii) **Compliance with new international standards on financial market infrastructures (FMIs)** - including the oversight and supervision of FMIs and to comply with the new Principles for Financial Market Infrastructures (PFMIs); and
  - (iv) **Enhancing the Commission’s litigation capacity for the enforcement of securities regulation** – the need to significantly step up manpower resources in the Commission’s Legal Services Division in order to deliver in-house legal advice to support the efficient completion of “high priority” investigations and litigation cases.

#### 4.1.3 The external employment market

- (a) Although there are segments within the Hong Kong financial services market that have been subject to downsizing, streamlining and/or off-shoring, the demand for compliance and risk-focused professionals remains high. This is due to the shortage of suitably qualified candidates within these areas in Hong Kong and the growing regulatory demand placed on financial institutions as a result of ongoing global regulatory reforms.
- (b) The increased demand for legal and compliance talent continues to present the Commission with challenges in its attempts to recruit more senior external candidates.

#### 4.1.4 The Graduate Trainee Programme

- (a) Recognising the importance of nurturing a strong, committed and diverse workforce, the Commission continues to develop its talent pipeline through the Commission’s Graduate Trainee Programme (GTP). The Programme is a three-year structured programme.



During the first two years, all Graduates Trainees under a fixed-term contract move through three rotations of eight month segments by being attached to various functional areas. In the third year, Graduate Trainees will be converted to a permanent role in a particular division. Graduate Trainees will be promoted to the Assistant Manager grade upon satisfactory completion of the 3-year programme. The primary objective of the GTP is to develop young graduates by giving them exposure to a wide range of the Commission's work before moving into specific roles.

- (b) Since the inception of the GTP in 2009, we have a total of 75 graduates who were recruited of which 15 have been appointed by the Commission in July 2013 as junior professionals based on their own merits. Currently, 15 graduate trainees are under Year 1 rotation and 13 are under Year 2 rotation and will be converted to permanent roles in 2014/15 subject to the satisfactory completion of their three rotations. The Commission has earmarked in the 2014/15 budget a total of 5 junior posts for the placement of graduate trainees to support the Commission's long-term talent strategy while the other 8 graduate trainees will be placed into existing vacancies.

#### 4.1.5 "The right place for people with a purpose"

The Commission abides by its core values of being proactive and professional and regards its employees as its most valuable assets. To deliver our employer brand promise, we will continue to nurture a favourable working environment and engage our employees via the provision of meaningful work, practical training programmes, personalised career planning, open communication and effective work life balance.

## 4.2 Interim headcount – 2013/14

4.2.1 During 2013/14, the Commission approved an interim request of 11 additional posts to support work resulting from the expansion of the Commission's regulatory remit and the additional regulatory and oversight responsibilities. The initiatives are comprised of:

- (a) The formation of a new listed corporate regulation team
  - (i) The corporate regulation team within the Corporate Finance Division (CFD) aims to provide the Commission with a broader and more proactive oversight of listed companies.
  - (ii) The team will review corporate and financial information and make appropriate enquiries at an early stage to facilitate timely disclosure or other remedial action by listed companies and to identify misconduct for enforcement action. These enquires will serve to educate companies and their directors to better comply with relevant rules and regulations thereby promoting good corporate behaviour.



- (iii) The Commission has approved the first phase of headcount increase for this team comprising 8 posts. The remaining 19 posts earmarked for the second phase are subject to the headcount approval procedures for the 2014/15 budget.
- (b) Enhancement of the supervisory approach to the HKEx
  - (i) The Supervision of Markets Division (SOM) will enhance its supervisory approach to the HKEx in response to the significant evolution in its business model, strategy, and range of activities.
  - (ii) The Commission has approved the first phase of headcount increase for this initiative comprising 3 posts. The remaining 9 posts in the second phase are to support increased supervisory intensity and engagement and are subject to the approval procedures for the 2014/15 budget.

#### 4.3 New headcount requests – 2014/15

4.3.1 Having taken into consideration the approved interim headcount, the Commission has undertaken a comprehensive workload analysis for 2014/15. It should be noted that a critical assessment of areas for potential re-training and redeployment of staff and process re-engineering or streamlining has been undertaken. Consequently, a net increase of 51 full time posts (of which 5 posts are for the placement of graduate trainees) has been included within this budget.

4.3.2 Approximately 69% of the proposed new headcount relates to executive grade positions with the remaining 31% being non-executive grade<sup>2</sup>. The need for executive grade staff reflects the Commission's assessment of the increasing complexity of the regulatory environment and the size of the market it regulates

##### **Corporate Finance Division**

4.3.3 The 8 posts proposed by the Corporate Finance Division (CFD), comprising 8 executive posts, form part of the second phase of planned headcount for the new corporate regulation team (paragraph 4.2.1(a)).

4.3.4 In addition to the 8 posts approved within the 2013/14 financial year, 8 of the remaining 19 posts earmarked for the second phase are proposed in 2014/15 budget. The remaining 11 posts will be deferred to 2015/16, subject to a further manpower review.

##### **Enforcement Division**

4.3.5 The Enforcement Division (ENF) plays a critical role in a robust supervisory regime, allowing the Commission to send the right signals to the market as

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<sup>2</sup> Executive grade refers to positions from Manager grade and above, while non-executive refers to positions below Manager grade



to the practices that are not tolerated and are detrimental to the development of a healthy securities and futures market in Hong Kong.

- 4.3.6 1 executive post is proposed by ENF to lead teams of more junior staff to handle an increasing number of investigations. The division has seen a growth in larger investigations, which has resulted in an increase in material that needs to be assessed. The size and complexity of these cases have made routine evaluations more resource intensive and require the input of more seasoned professionals.
- 4.3.7 5 non-executive posts are proposed to provide the necessary support structure for the investigations undertaken by ENF. In 2013/14, the shortage of non-executive staff resulted in the need for professional staff to undertake resource intensive work in addition to their investigative roles. This is not an ideal operational arrangement and the new non-executive headcount requests seek to remedy this situation.
- 4.3.8 The 4 upgrades proposed are part of a progression path for high performing graduate trainees to take up junior professional roles.

#### **Intermediaries Division**

- 4.3.9 The Intermediaries Division (INT) proposes 13 new posts for the new unit which now combines the Licensing and Intermediaries Supervision departments. The headcount requests for INT is detailed below:
- (a) Strategic planning
- 1 executive post is proposed to assist in general policy development and to devise new supervisory approaches for the licensing and supervision of intermediaries.
- (b) Intermediaries Supervision Department, Intermediaries
- (i) 5 new executive posts and 2 new non-executive posts are proposed to keep pace with the anticipated increase in the number of Licensed Corporations (LCs) and to maintain the cycle of on-site inspections. Increased supervisory intensity (in line with global trends and expectations) will require more proactive inspections of LCs as well as more detailed 'offsite' monitoring work. Increasing complexity of LCs' business models, and increasing automation of trading and operations, will require the breadth and depth of our inspections to be adjusted so as to properly address the risks involved.
- (ii) Anti-Money Laundering (AML)
- 1 executive post is required for the expansion of the AML team to enhance the Commission's supervisory programme for AML compliance by LCs and to handle AML-related tasks.



- Specifically, the team will assist in the money laundering and terrorist financing national risk assessment for the securities sector, participate in the amendment review of the AMLO, a joint review of the uniform AML Guideline together with the other financial regulators, and other supervisory initiatives in preparation for the upcoming FATF Mutual Evaluation of Hong Kong's AML regime which is due to commence in 2015/16.
- (iii) 1 additional executive post is required to support specific policy work which includes, but is not limited to:
  - The development of regulatory requirements for the new OTC derivatives regime including reviewing and amending FRR, Keeping of Records Rules, Client Money Rules, Client Securities Rules, Code of Conduct, client clearing documentation of HKEX's OTC Clear, as well as to work with IP on new policy initiatives in relation to open-ended fund companies; and
  - The development of detailed requirements of the local resolution regime which is expected to be completed by 2014;
- (iv) 6 executive and 4 non-executive upgrades are proposed to reflect the increased sophistication and range of supervisory work as described above.
- (c) Licensing Department, Intermediaries
  - (i) 3 non-executive posts are proposed by the Licensing Department (LIC – INT) to deal with the marked and steady increase in applications that LIC INT is experiencing. The focus on non-executive posts reflects the need for junior staff to deal with the more routine aspects of license and related applications.
  - (ii) 2 executive and 2 non-executive upgrades are proposed to promote and retain high quality staff within the department.

### **Legal Services Division**

- 4.3.10 The Legal Services Division (LSD) proposed 6 executive posts and 2 non-executive posts to establish a new litigation team to take on a mix of civil and criminal litigation work. The requirement for a new team reflects the increasing number of complex High Court litigation cases undertaken by the Commission as well as preparation of proceedings before the MMT.
- 4.3.11 LSD has in the past faced severe resourcing issues which have in turn created a backlog of cases; this new team will provide much needed resources to alleviate this. In practical terms, the new team will allow LSD to provide advice more quickly and to position LSD to take on additional work which is expected to be created by the increased number of investigators in ENF and the newly expanded listed corporate regulator team within CFD.



- 4.3.12 The 3 non-executive upgrades are proposed to reflect the changed nature of the clerical roles from administration to office management type of work.

#### **Investment Product Division**

- 4.3.13 The Investment Product Division (IP) proposes a total of 4 executive and 1 non-executive post as detailed below:

- (a) Mainland-Hong Kong fund mutual recognition
  - (i) The Commission is in the final stage of negotiation with the Mainland authorities regarding the Mainland-Hong Kong mutual recognition of funds (MRF) initiative. It is expected that the MoU with CSRC will be concluded by end of 2013 or early 2014.
  - (ii) This MRF initiative will be a significant milestone for Hong Kong asset management industry, and is a crucial part of developing Hong Kong as an international asset management centre and offshore RMB hub. This is expected to bring about fundamental changes to the types of funds seeking Commission's authorisation once the implementation phase commences in 2014/15.
  - (iii) It is estimated that over 500 Mainland funds will qualify under this MRF initiative. The Commission anticipates there will also be an increase in number of applications for new Hong Kong-domiciled funds to make use of this new MRF initiative. Considerable changes in the product nature and strategies of these funds are also expected to meet the needs of target investors in the Mainland.
  - (iv) Further, close interaction and extensive ongoing dialogue with the CSRC, SAFE and other Mainland authorities will be required.
  - (v) 2 executive posts and 1 non-executive post are therefore proposed to handle the new applications and associated work as a result of the implementation of the MRF initiative.
- (b) Implementation of product design measures
  - 1 executive post is proposed for IP to implement new product design measures in 2014/15 and to critically assess product applications. Given the wide coverage of investment products affected and anticipated practical implementation issues, a special task force is needed, which will also deal with ILAS issues.
- (c) Heightened monitoring of Commission authorised funds and suspected Collective Investment Schemes (CIS)
  - 1 executive post is proposed for IP to take up a new mandate concerning the surveillance of suspected CIS advertisements and to more intensively monitor the substantial pool of existing





Commission-authorized products. This requires experienced senior staff to conduct the relevant analysis and put forward any relevant cases for enforcement action.

- 4.3.14 In addition, 5 executive upgrades are requested by IP to handle work of increasing complexity including the implementation of mutual recognition of funds with the Mainland and product design measures.
- 4.3.15 The above headcount request follows the redeployment of existing staff in a more efficient manner and streamlining existing processes so as to ensure optimal utilisation of available staff resources. For example, IP has deployed existing resources to handle the additional workload required for a major policy project to introduce an open-ended fund companies framework in Hong Kong. The Commission working group chaired by IP has recently made key technical proposals to the Government. Following public consultation to be conducted by early 2014, IP will assist the Government in the consultation conclusions, legislative and regulation drafting phases during 2014/15.

### **Supervision of Markets Division**

- 4.3.16 The Supervision of Markets Division (SOM) plays a pivotal role in the oversight and supervision of the financial market infrastructure which underpins Hong Kong's position as an international financial centre.
- 4.3.17 The 9 new posts proposed by SOM, comprising 6 executive posts and 2 non-executive posts, form the second phase of headcount requests in relation the vital enhancement of the supervisory approach to the HKEx (para 4.2.1 (b)) and to handle other existing and new initiatives. These include:

(a) OTC derivatives regulation

The Commission is currently in the process of making legislative amendments to introduce a regime for the regulation of OTC derivatives market in Hong Kong. It is anticipated that an implementation stage will follow the completion of the legislative amendments in 2014, which will, among other things, require the Commission to review applications from overseas CCPs to provide clearing services for OTC derivatives products in Hong Kong.

(b) Uncertificated securities market

The Government is planning to introduce legislative amendments in relation to uncertificated securities market to the LegCo in the first half of 2014. We expect that a significant amount of preparatory work will be required to resolve various operational issues and to consult the market on different aspects of the new proposed framework.



(c) HKEx's new business model

HKEx has initiated a number of strategic initiatives including the acquisition of LME. The development of LME Clear and expansion of products into other asset classes including fixed income, currencies and commodities requires effective supervision.

- 4.3.18 1 executive post is proposed by the Research team of SOM due to the growing volume of policy work arising from the Commission's involvement in global regulatory developments and interactions with peer regulators.
- 4.3.19 Lastly, 2 upgrades comprising 1 executive and 1 non-executive posts are to deal with the changing nature and increasing complexity of work in supervising HKEx and monitoring the dynamics of the overall market.

**Corporate Affairs Division**

- 4.3.20 For Corporate Affairs Division (CA), 1 new executive headcount is proposed by the Finance and Administration Department (F&A). This is in response to the increase in workload which will arise from the appointment of external fund managers for the day-to-day monitoring of the Commission's investment portfolio. Additionally, 1 non-executive support headcount and 1 non-executive support upgrade are requested by F&A in order to meet the anticipated increase in administrative workload.
- 4.3.21 The remaining 6 upgrades comprising 3 in External Relations Department (ER), 1 in Human Resources (HR) and 2 in the Information Technology Department (IT) are required to align the CA structure with those of the operating divisions to ensure continued efficiency in service delivery.



## 5. Financials

### 5.1 Income and expenditure statement

Para. Ref.	(a) Proposed Budget For Year 2014/15 HK\$'000	(b) Forecast For Year 2013/14 HK\$'000	(c) Approved Budget For Year 2013/14 HK\$'000	Proposed Budget (a)		Forecast (b) over/(under) Approved Budget (c)		
				Over/(under) Forecast (b) HK\$'000	%	over/(under) Approved Budget (c) HK\$'000	%	
<b><u>Income</u></b>								
Investor Levy	5.3.2							
Securities		918,840	895,465	803,520	23,375	2.6%	91,945	11.4%
Futures/Options Contracts		76,334	74,733	70,829	1,601	2.1%	3,904	5.5%
Hong Kong Mercantile Exchange		-	36	2,336	(36)	N/A	(2,300)	N/A
Fees & Charges	5.3.3	89,700	83,000	93,700	6,700	8.1%	(10,700)	-11.4%
Investment Income	5.3.4	68,236	62,354	93,000	5,882	9.4%	(30,646)	-33.0%
Other Income	5.3.5	8,680	8,680	5,748	-	0.0%	2,932	51.0%
<b>Total</b>		<b>1,161,790</b>	<b>1,124,268</b>	<b>1,069,133</b>	<b>37,522</b>	<b>3.3%</b>	<b>55,135</b>	<b>5.2%</b>
<b><u>Recurrent expenditure</u></b>								
Premises	5.4.1	227,791	216,656	220,104	11,135	5.1%	(3,448)	-1.6%
Staff cost	5.4.2	1,070,316	908,663	955,230	161,653	17.8%	(46,567)	-4.9%
Info. & Sys. Services	5.4.3	54,388	44,231	50,757	10,157	23.0%	(6,526)	-12.9%
General Office & Insurance	5.4.4	8,697	7,365	9,154	1,332	18.1%	(1,789)	-19.5%
Training & Development	5.4.5	9,950	9,000	10,820	950	10.6%	(1,820)	-16.8%
Professional & Others	5.4.6	107,908	94,000	89,805	13,908	14.8%	4,195	4.7%
External Relations	5.4.7	15,456	13,849	21,500	1,607	11.6%	(7,651)	-35.6%
Internship Programme	5.4.8	9,461	8,910	9,720	551	6.2%	(810)	-8.3%
Contingency	5.4.9	4,000	3,000	3,000	1,000	33.3%	-	0.0%
Depreciation	5.4.10	65,000	56,500	70,000	8,500	15.0%	(13,500)	-19.3%
<b>Total (1)</b>		<b>1,572,967</b>	<b>1,362,174</b>	<b>1,440,090</b>	<b>210,793</b>	<b>15.5%</b>	<b>(77,916)</b>	<b>-5.4%</b>
<b><u>Funding to external parties</u></b>								
Funding to FRC	5.5.1	5,106	4,863	4,863	243	5.0%	-	0.0%
Funding to IFRS Foundation	5.5.2	390	389	390	1	0.3%	(1)	-0.3%
Funding to IEC	5.5.3-4	60,506	50,678	54,448	9,828	19.4%	(3,770)	-6.9%
Funding to FDRC	5.5.5	10,500	3,500	3,500	7,000	200.0%	-	0.0%
Funding to HKSI and other training initiatives	5.5.6-7	20,000	3,370	-	16,630	493.5%	3,370	N/A
Funding for the establishment of the HK XBRL Taxonomy	5.5.8	1,000	-	1,000	1,000	N/A	(1,000)	N/A
<b>Total (2)</b>		<b>97,502</b>	<b>62,800</b>	<b>64,201</b>	<b>34,702</b>	<b>55.3%</b>	<b>(1,401)</b>	<b>-2.2%</b>
<b>Total expenditure (1)+(2)</b>		<b>1,670,469</b>	<b>1,424,974</b>	<b>1,504,291</b>	<b>245,495</b>	<b>17.2%</b>	<b>(79,317)</b>	<b>-5.3%</b>
<b>Deficit for the year</b>		<b>(508,679)</b>	<b>(300,706)</b>	<b>(435,158)</b>	<b>(207,973)</b>	<b>69.2%</b>	<b>134,452</b>	<b>-30.90%</b>
Reserves brought forward		7,154,923	7,455,629	7,237,595	(300,706)	-4.0%	218,034	3.0%
<b>Reserves carried forward</b>		<b>6,646,244</b>	<b>7,154,923</b>	<b>6,802,437</b>	<b>(508,679)</b>	<b>-7.1%</b>	<b>352,486</b>	<b>5.2%</b>



## 5.2 Capital expenditure statement

<u>Para.</u> <u>Ref.</u>	(a)	(b)	(c)	Proposed		Forecast (b)	
	<b>Budget For Year 2014/15</b>	Forecast For Year 2013/14	Approved Budget For Year 2013/14	Budget (a) Over/(under) Forecast (b)	%	over/(under) Approved Budget (c)	%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000		HK\$'000	
<b>Capital expenditure</b>							
		5.6					
Furniture & Fixtures	<b>7,600</b>	3,450	10,000	4,150	120.3%	(6,550)	-65.5%
Office Equipment	<b>15,170</b>	18,610	17,090	(3,440)	-18.5%	1,520	8.9%
Vehicles	<b>1,200</b>	0	0	1,200	N/A	-	N/A
Computer Sys. Development	<b>33,810</b>	22,550	29,500	11,260	49.9%	(6,950)	-23.6%
Sub-total	<b>57,780</b>	44,610	56,590	13,170	29.5%	(11,980)	-21.2%
Contingency	<b>5,780</b>	4,460	5,659	1,320	29.6%	(1,199)	-21.2%
<b>Total</b>	<b>63,560</b>	<b>49,070</b>	<b>62,249</b>	<b>14,490</b>	29.5%	<b>(13,179)</b>	-21.2%



## 5.3 Income

### 5.3.1 Annual grant from government

S.14 of the Securities and Futures Ordinance provides that: “For each financial year of the Commission, the Government shall pay to the Commission out of the general revenue the moneys appropriated by the Legislative Council for that purpose.” As in previous years, the Commission proposes that the Government does not request any appropriation from the Legislative Council for the financial year 2014/15. The Commission’s decision is made without prejudice to the funding principles established when the Commission was formed, and has no implications for requests for appropriations in future years.

### 5.3.2 Investor levy

- (a) While it is projected that the Commission will continue to incur an operating deficit in future, having taken into consideration the level of our reserves and the longer term financial stability of the Commission, we recommend a 10% reduction in the levy rate in 2014/15. Given the time required to amend the Securities and Futures (Levy) Order, for budgetary purposes, we have budgeted for the reduction in both the securities and futures levy rates with effect from 1 October 2014.
- (b) The following turnover and levy rate assumptions have been used in preparing levy income estimates:

	2013/14		2014/15	
	Budget	Forecast	Budget Apr - Sep	Budget Oct - Mar
<b>Securities</b>				
Daily turnover (billion/day)	\$54.0	\$60.0	\$65.0	\$65.0
Levy rate	0.003%	0.003%	0.003%	0.0027%
<b>Futures/Options Contracts</b>				
Daily turnover (contracts)	238,000	250,000	270,000	270,000
Levy rate	\$0.6	\$0.6	\$0.6	\$0.54

- (c) The 2013/14 Forecast of Investor Levy – Securities is higher than the Approved Budget by 11.4% (\$91.95 million) whereas Investor levy – Futures and Options is above the Approved Budget by 5.5% (\$3.90 million). These variations reflect the higher actual market turnover in the first six months of 2013/14 when compared to the estimates underlying the Approved Budget.
- (d) Based on estimates made by our research team on a basis consistent with prior years, we project that the average securities market turnover for 2014/15 will be 8% higher than that of 2013/14.



### 5.3.3 Fees and charges

- (a) The Forecast aggregate fees and charges income for 2013/14 is 11.4% (\$10.7 million) lower than the Approved Budget as fees from Licensing and Investment Products are lower than expected.
- (b) The 2014/15 Budget shows an increase in fee income of 8.1% (\$6.7 million) against the Forecast for 2013/14. This increase arises mainly from a projected increase in licensing application fees, including application fees for the new regime in respect of the regulation of OTC derivatives, which is expected to be implemented in 2014/15.

### 5.3.4 Investment income

- (a) Investment income for 2013/14 is forecasted to be \$62.35 million, 33% (\$30.65 million) lower than the Approved Budget as we have revised downward the average rate of return from 1.5% to 1% p.a., based on the actual return earned during the first six months of the year.
- (b) 2014/15 investment income is budgeted to be \$68.24 million, 9.4% (\$5.88 million) higher than the 2013/14 Forecast. We plan to engage external investment managers in 2014 to manage our investment portfolio. The rate of return depends primarily on market performance and the investment strategy to be adopted.

### 5.3.5 Other income

Other income for 2013/14 and 2014/15 represents license fees and service fees received from IEC and ICC for providing office space, accountancy, human resources and IT support services, recoveries from enforcement cases and sale of Commission publications.

## 5.4 Recurrent expenditure

### 5.4.1 Premises

- (a) Forecast premises expenses for 2013/14 are expected to be lower than the approved budget by \$3.45 million (1.6%) primarily due to a lower than expected increase in management fees. We have entered into a new lease for around 3,000 sq. ft. of office space from November 2013 for the additional headcount required for the CFD corporate regulation team. This is a new initiative not included in our Approved Budget.
- (b) Expenses for 2014/15 are budgeted to be \$11.14 million (5.1%) higher than our 2013/14 Forecast. This is mainly due to the full year effect of the lease of new office mentioned in (a) above and provision for additional office space in the second half of the year 2014/15 to cater for the headcount for the new financial year.



#### 5.4.2 Staff cost

- (a) The overall staff cost for 2013/14 is forecasted to be lower than the 2013/14 budget by 4.9% (\$46.57 million). This is principally due to the time lag experienced in filling vacancies and a number of positions being under-filled at lower grades.
- (b) The projected headcount at 31 March 2015 is 845, a net increase of 51 (6.4%) over the 2013/14 Commission approved headcount. Please see section 4 for detailed explanations. The projected staff cost for 2014/15 is 17.8% (\$161.65 million) higher than the 2013/14 Forecast and 12.1% (\$115.09 million) higher than the 2013/14 budget.
- (c) The 2014/15 budget includes provision for an average 5.5% pay increase for Commission staff. This is based on preliminary market information from external parties including pay consultants and professional associations (as at 1 November 2013). Detailed proposals for the actual pay increase will be formulated in Q1, 2014.
- (d) The management will determine the detailed pay policy and present this to the Remuneration Committee for discussion and to the Commission for approval.

#### 5.4.3 Information and systems services

- (a) The information and systems services expenses forecast for 2013/14 is 12.9% (\$6.53 million) lower than the approved budget due to lower than expected information services and systems contract services required and lower hardware and software maintenance costs. Some subscriptions for market data services have been deferred to 2014/15.
- (b) For 2014/15, we project a 23.0% (\$10.16 million) increase due to higher software and hardware maintenance costs after the lapse of warranty periods and increases in subscriptions for market data to support enforcement and supervision activities. New systems are required by our operating divisions to manage their caseloads and to enhance their investigatory and supervisory capabilities.

#### 5.4.4 General office and insurance

- (a) The general office and insurance expenses forecast for 2013/14 is 19.5% (\$1.79 million) lower than the approved budget mainly due to savings in repairs and maintenance, printing, professional indemnity insurance premiums and vehicle expenses.
- (b) Expenses for 2014/15 are expected to be higher than 2013/14 Forecast by 18.1% (\$1.33 million) due to higher printing and stationery and office services expenses.



#### 5.4.5 Training and development

- (a) Forecast training related expenses for 2013/14 are 16.8% (\$1.82 million) lower than the approved budget. This is mainly due to the change of project priorities and thus deferral of some development activities to 2014/15.
- (b) Training and development expenses for 2014/15 are comparable to the 2013/14 Forecast. We are working to streamline various management training programmes to make them more cost-effective. Sourcing complimentary technical training from market practitioners should lead to further cost savings. In addition, staff development activities for next year will be rationalised to maximize the value of our training budget.

#### 5.4.6 Professional and others

- (a) Forecast professional and others expenses for 2013/14 are 4.7% (\$4.20 million) above the approved budget mainly due to higher legal costs in relation to current cases.
- (b) Professional and others expenses for 2014/15 are expected to increase by 14.8% (\$13.91 million) as the demand for external legal and expert services remains high, especially in the areas of investigation, supervision of intermediaries and authorization of new products.

#### 5.4.7 External relations

- (a) Forecast external relations expenses for 2013/14 are lower than the approved budget by 35.6% (\$7.65 million) due to savings in overseas travelling and publications expenses.
- (b) The 2014/15 budget is \$1.61 million (11.6%) higher than the 2013/14 Forecast owing to a projected increase in expenses relating to the Commission's international work and other regulatory activity.

#### 5.4.8 Internship programme

This represents the salary cost of hiring university graduates in support of the Government's internship for university graduates programme and for the Commission to develop a pipeline of talent for the future. Our proposed expenditure for 2014/15 to recruit and retain these individuals represents an increase of \$0.55 million (6.2%) over the 2013/14 Forecast.

#### 5.4.9 Contingency

A contingency of \$3 million and \$4 million is provided for the remainder of 2013/14 and the full year of 2014/15 respectively to cover unforeseen expenses arising from changes in the operating environment or unforeseen special requirements.





#### 5.4.10 Depreciation

- (a) Forecast depreciation expenses for 2013/14 are expected to be 19.3% (\$13.5 million) lower than budget because of lower than expected capital expenditure actually incurred in the current year.
- (b) Depreciation expenses for 2014/15 will be 15% (\$8.5 million) higher than the 2013/14 Forecast as we expect that “unspent” capital expenditure in 2013/14 will be carried forward and expended in 2014/15.

#### 5.5 Funding to external parties

- 5.5.1 To continue our support for the work of the Financial Reporting Council, the Commission will provide annual funding of \$5.11 million in 2014/15.
- 5.5.2 To continue our support for the work of the International Financial Reporting Standards Foundation, the Commission will again provide funding of US\$50,000 (or HK\$390,000).
- 5.5.3 We have reduced our funding to Investor Education Centre (IEC) from \$54.45 million to \$50.68 million in 2013/14 based on the latest forecast prepared by IEC. In 2014/15, IEC proposed total expenditure of \$60.51 million. A budget summary is provided below:

	Budget 2014/15	Forecast 2013/14	Budget 2013/14
	\$'m	\$'m	\$'m
Education programmes	23.45	19.89	19.00
Staff costs	22.69	17.74	21.52
Premises costs	3.36	2.93	3.33
Professional & other services	4.99	4.31	3.93
Publicity & external relations	2.57	2.23	2.12
General office & others	1.95	1.97	1.98
Contingency	1.50	1.61	2.57
Total	<u>60.51</u>	<u>50.68</u>	<u>54.45</u>

- 5.5.4 IEC projects higher expenditure for 2014/15 based on experience of the actual costs of its key operations in 2013/14 (e.g. website maintenance and development, conducting high quality and rigorous research etc) as well as proposals for projects in 2014/15 to increase the awareness, effectiveness and reach of education work.
- 5.5.5 The Commission will continue to share 1/4 of the Financial Dispute Resolution Centre’s (FDRC) annual operating costs in 2014/15. According to the Memorandum of Understanding signed between Commission and the other parties, the amount of funding for 2014/15 is \$10.5 million.
- 5.5.6 In 2013/14 Forecast, we have included funding of \$3.37 million to Hong Kong Securities and Investment Institute (HKSI) for developing new study manuals and additional licensing examination questions in anticipation of



the introduction of the OTC derivatives and the enhanced sponsor IPO regulatory regimes.

5.5.7 We have included \$20 million in 2014/15 budget for funding training initiatives for intermediaries, particularly small and medium-sized firms, to meet the challenges arising from the changing market landscape.

5.5.8 The project on the development of a Hong Kong XBRL<sup>3</sup> taxonomy<sup>4</sup> for financial reporting by Hong Kong listed companies is deferred to 2014/15. To support the development of the project, we have provided \$1 million in our 2014/15 budget.

## 5.6 Capital expenditure

5.6.1 The total capital expenditure forecast for 2013/14 has been trimmed from \$62.25 million to \$49.07 million. Savings in our fit-out work is partially offset by the renovation costs for our 36/F office, which was leased in November 2013 (see also para 5.4.1(a)).

5.6.2 The total capital expenditure budget for 2014/15 is \$63.56 million, 29.5% (\$14.49 million) higher than the 2013/14 Forecast. This is the combined effect of the estimated renovation costs for the additional lease of office space (see also para 5.4.1 (b)) and the replacement of a Commission car. The planned capital expenditure commitment for 2014/15 comprises the following:

Capital expenditure	Amount HK\$ m	Note
Office furniture & fixtures	7.60	(a)
Office equipment	15.17	(b)
Vehicles	1.20	(c)
Computer systems development	33.81	(d)
Contingency (10%)	<u>5.78</u>	(e)
Total	<u>63.56</u>	

Notes :-

(a) for office furniture and fixtures:

In view of the growth in headcount, we plan to lease additional office space in mid-2014. The projected renovation cost is about \$6.6 million. We have also provided \$1 million for replacement of obsolete furniture due to normal wear and tear.

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<sup>3</sup> XBRL (Extensible Business Reporting Language) is an open standard that is developed and maintained by XBRL International, a global non-profit consortium of over 650 major companies, organisations and government agencies from 30 countries, including China, UK and the US. It aims at standardizing financial reporting in order to promote transparency and improve quality and comparability of business information.

<sup>4</sup> XBRL taxonomies are the dictionaries which the computer languages use. They define the specific tags for individual items of financial data. Due to the differences in accounting regulations, each jurisdiction may have its own taxonomy for financial reporting.



- (b) for office equipment:
  - (i) \$1 million for replacement of obsolete office equipment due to normal wear and tear; and
  - (ii) \$14.17 million for investment in storage technology and data base capacity plus costs relating to the normal replacement of obsolete servers and computer equipment for the additional headcount.
- (c) for the replacement of one of the existing Commission cars.
- (d) for “front-end” technology to upgrade our market surveillance capabilities, improve access and exchange of information between stakeholders and the Commission and enhance various IT systems (including Intermediaries and market surveillance systems).
- (e) as in the prior year, contingency is set at 10% of the aggregate budgeted capital expenditure.