





# Corporate Social Responsibility

As a statutory market regulator, the SFC's regulatory objectives are determined by the SFO. As a corporate citizen of Hong Kong we aim to pursue these objectives by following responsible policies and practices that allow us to make a positive impact on society.

To the SFC, corporate social responsibility (CSR) consists of three main areas: (a) corporate governance; (b) care for employees; and (c) care for society, including our concern for the environment and for the people around us.

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We aim to be a good corporate citizen by adopting responsible policies and practices that enable us to make a positive impact on the society in which we operate.

We believe that our role as a regulator, by its very nature, makes a positive contribution to society. However, we try hard to enhance this core contribution by also considering carefully how we carry out our duties and how we interact with the community. Whilst we believe that we already have high standards, we also recognise that improvements are possible and we are committed to doing even better.

We think about our performance on CSR issues in three main areas – Corporate Governance, Care for Employees and Care for Society.

### Corporate Governance

To maintain high corporate governance standards, we have laid down a comprehensive and cohesive corporate governance framework by making reference to best governance practices for public bodies such as those set out in “Corporate Governance for Public Bodies – A Basic Framework” published by the Hong Kong Institute of Certified Public Accountants (HKICPA).

Our governance framework comprises a clearly defined governing structure, high conduct standards, sound operational and financial control procedures and vigorous external checks and balances. This framework ensures that we practise the principles of transparency, accountability, fairness, objectivity and integrity in our work.

### Our Board (the Commission)

Our highest governance body is the Commission referred to in our name. On appointment by the HKSAR Government,

all Non-Executive Directors (NEDs) and Executive Directors (EDs) are appointed members of the Commission, who are tasked to perform duties set out in the Securities and Futures Ordinance (SFO). Within our governance structure, the terms Commission and Board are synonymous.

The Board leads the organisation in fulfilling our objectives and performing the functions set out in the SFO. The Board provides strategic guidance to senior management and provides independent oversight of executive functions.

The Board has delegated a number of regulatory powers and functions to the EDs, senior staff or committees, while retaining at Board level those functions required to perform an effective oversight role. These functions include those that could have far reaching consequences for the securities and futures markets in Hong Kong and the non-delegable functions set out in the SFO. Equally, EDs are authorised where appropriate to sub-delegate functions to their staff and committees, for the efficient discharge of their duties.

All the members of the Board are appointed by the HKSAR Chief Executive for a fixed term. The SFO requires that the majority of the members of the Board must be independent NEDs. The composition of the NEDs brings to the Board a good mix of experience and expertise and facilitates effective oversight of the executive functions. At the year-end, the Board comprised 14 members: the Chairman, seven NEDs and six EDs.

There have been a number of changes in our Board during the year. In line with good corporate governance practice, the posts of the Chairman and Chief Executive Officer (CEO) were separated by the passage of the Securities and Futures (Amendment) Ordinance 2006. The HKSAR Chief Executive subsequently appointed Mr Eddy Fong as our first non-executive Chairman for a term of three years from

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20 October 2006 and appointed Mr Martin Wheatley as our CEO for a term running from 23 June 2006 to 30 September 2008. The separation of these positions has enhanced Board level checks and balances. Under this new governance structure, the non-executive Chairman leads the Board in setting the overall direction, policies and strategy of the SFC and in monitoring the performance of the executive arm. The CEO has the executive responsibility for the day-to-day running of the SFC. He has the duty to implement the objectives set by the Board and to facilitate the effective functioning of the SFC. While the Chairman and the CEO play distinct roles, they discharge their duties in a complementary manner. The respective roles and responsibilities of the Chairman and CEO have been clearly set out and published on the SFC website for the information of our stakeholders.

Two new NEDs were appointed during the year: Mrs Angelina Lee and Mr Shengman Zhang were appointed for a term of two years, from 1 August 2006 and 1 January 2007 respectively. Mr Kenneth Kwok and Professor Liu Pak Wai were re-appointed NEDs for a term of two years from 1 January 2007. There were also four new appointments of EDs: Mr Brian Ho and Mr Keith Lui were appointed for a term of three years from 28 August 2006; while Mr Mark Steward and Mr Paul Kennedy were appointed also for three years from 25 September 2006 and 16 October 2006 respectively. Former EDs, Mr Alan Linning and Mr Peter Au-Yang, left the SFC, and former NED Mr Raymond Kwok stepped down during the year.

The Board meets regularly every month and holds additional meetings as necessary. In addition to the matters requiring Board approval under the SFO, all important policies and decisions are discussed and approved by the Board. Members are also briefed on certain key operational issues and provided with financial statements on a monthly basis. Divisional staff also attend Board meetings as necessary to brief members on specific policy proposals, operational matters and regulatory issues. The Chief Counsel also attends Board meetings to advise on legal issues.

### Attendance of Directors at Commission meetings in 2006-07

Number of meetings	18	
<b>Attendance of individual Directors</b>		
Eddy C Fong <sup>1</sup>	15	83%
Martin Wheatley	17	94%
Peter Au-Yang <sup>2</sup>	2	100%
Brian Ho <sup>3</sup>	8	100%
Paul Kennedy <sup>4</sup>	6	100%
Alexa Lam	16	89%
Alan Linning <sup>5</sup>	1	25%
Keith Lui <sup>6</sup>	8	100%
Mark Steward <sup>7</sup>	7	100%
Christopher W C Cheng	13	72%
Kenneth H W Kwok	11	61%
Raymond P L Kwok <sup>8</sup>	5	63%
Angelina Lee <sup>9</sup>	8	89%
York Liao	13	72%
Liu Pak Wai	15	83%
Jasper Y S Tsang	14	78%
Shengman Zhang <sup>10</sup>	4	100%
<b>Average attendance of meetings</b>	<b>80%</b>	

The individual attendance rates are based on the respective number of meetings members were expected to attend during their terms. For details of their terms, please see chapter on Directors of the Commission.

<sup>1</sup> Membership from 20.10.06

<sup>2</sup> Membership until 25.5.06

<sup>3</sup> Membership from 28.8.06

<sup>4</sup> Membership from 16.10.06

<sup>5</sup> Membership until 6.6.06

<sup>6</sup> Membership from 28.8.06

<sup>7</sup> Membership from 25.9.06

<sup>8</sup> Membership until 31.7.06

<sup>9</sup> Membership from 1.8.06

<sup>10</sup> Membership from 1.1.07

Board members have separate and independent access to senior management and divisional staff for any additional information they feel that they require about any policy proposal. They also have access to the Commission Secretary, who is responsible for ensuring the procedures of the SFC are complied with. Board members and the Board committees may also seek independent professional advice, at the expense of the SFC, should they consider this necessary.

Board members receive timely and adequate information to enable them to consider issues to be discussed at Board meetings. Minutes of the Board meetings are kept in safe custody by the Commission Secretary, and are open for inspection by Board members.

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All newly appointed Board members receive briefings on the work of the SFC and are provided with relevant SFC documents including a copy of the Code of Conduct, which sets out the legal obligations and the SFC's requirements on confidentiality, conflict of interests and personal investment. The most important statutory obligations are those relating to the preservation of secrecy and avoidance of conflict of interests. All Board members are required to disclose their investment portfolio upon appointment and to report any subsequent changes.

NEDs bring an independent and informed perspective to matters discussed and deliberated at the Board and play an important role in ensuring that the Board is accountable and transparent. NEDs also chair and participate in various statutory committees established by the Board which each have written terms of reference. All Board committees circulate their minutes and report important issues to the Board regularly.

### Internal committees

The **Audit Committee** comprises only NEDs. Mrs Angelina Lee is the Chairman. Senior personnel including the Chief Operating Officer and the Director of Finance and Administration are invited to attend meetings where necessary.

#### Attendance of Directors at Audit Committee meetings in 2006-07

Number of meetings	4	
<i>Attendance of individual Directors</i>		
Eddy C Fong (Chairman) <sup>1</sup>	3	100%
Angelina Lee (Chairman) <sup>2</sup>	3	100%
Kenneth H W Kwok (Deputy Chairman) <sup>3</sup>	4	100%
Raymond P L Kwok (Deputy Chairman) <sup>4</sup>	1	100%
Liu Pak Wai <sup>5</sup>	3	100%
Shengman Zhang <sup>6</sup>	N/A	N/A
<b>Average attendance of meetings</b>	<b>100%</b>	

<sup>1</sup> Membership until 15.1.07

<sup>2</sup> Appointed as Chairman on 15.1.07

<sup>3</sup> Appointed as Deputy Chairman on 17.7.06

<sup>4</sup> Membership until 31.7.06

<sup>5</sup> Membership from 17.7.06

<sup>6</sup> Membership from 15.1.07

The Audit Committee holds meetings on a quarterly basis. It reviews the annual financial statements before their submission to the Board for approval and recommends the appointment of external auditors for the Board's approval. It considers the scope and planning of the external audit, reviews any audit findings set out in the external auditors' management letters and monitors the implementation of agreed improvements.

The Audit Committee also examines management's procedures to monitor the effectiveness of the systems of financial and internal control. It considers and approves our annual internal control review programme.

All non-audit services conducted by external auditors are considered critically by the Audit Committee, which considers each engagement on a merit basis. To ensure independence and objectivity of the annual audit, different external auditors are appointed to perform the annual internal control review of the SFC.

During the year, we paid KPMG, our external auditor, \$275,000 for audit-related services and \$2,800,000 for non-audit related activity involving circularisation of client accounts of selected brokers.

KPMG was also engaged as the external auditor of compensation funds which are directly or indirectly under the supervision of the SFC as required by the law. In total, they paid KPMG \$206,000 for annual audits and half-yearly interim reviews.

Apart from performing audit-related and internal control functions, the Audit Committee also plays an important role in the handling of complaints against SFC staff, cases of staff grievances, public interest grievances, and complaints of discrimination. If a case involves staff at ED level, the Audit Committee will normally handle the case itself. For other cases, a quarterly report is made to the Audit Committee providing information on the complaints or grievances raised and decisions taken. We are pleased to report that we did not have any substantiated cases during the past year.

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The **Remuneration Committee** comprises only NEDs. Dr York Liao is the Chairman. Senior staff including EDs are invited to attend the meetings where necessary to brief the committee members on matters under consideration.

### Attendance of Directors at Remuneration Committee meetings in 2006-07

Number of meetings	3	
Attendance of individual Directors		
York Liao (Chairman)	3	100%
Christopher W C Cheng (Deputy Chairman)	3	67%
Eddy C Fong	2	67%
Kenneth H W Kwok	2	67%
Raymond P L Kwok <sup>1</sup>	0	0%
Angelina Lee <sup>2</sup>	2	100%
Liu Pak Wai	2	67%
Jasper Y S Tsang	2	67%
Shengman Zhang <sup>3</sup>	1	100%
<b>Average attendance of meetings</b>	<b>76%</b>	

<sup>1</sup> Membership until 31.7.06

<sup>2</sup> Membership from 1.8.06

<sup>3</sup> Membership from 1.1.07

The goal of our remuneration policy is to ensure that overall remuneration levels, including benefits, are effective in attracting, retaining and motivating appropriate levels of competent staff such that we can effectively execute our statutory responsibilities. The Remuneration Committee reviews policy on both the structure and level of staff remuneration and makes recommendations to the Board. It reviews reports on trends in salary and benefits and recommends to the Board any periodic adjustment. It is also consulted on the appointment of EDs and makes recommendations to the Government on appropriate remuneration levels.

The HKSAR Chief Executive (or the Financial Secretary under delegated authority) determines the remuneration packages of EDs, taking into consideration recommendations by the Remuneration Committee. Details of the EDs' remuneration on an individual named basis are set out on page 67. The EDs' remuneration packages comprise annual fixed pay and performance-related variable pay. The Chairman and NEDs receive a fixed sum honorarium every year.

The **Budget Committee** comprises both NEDs and EDs.

NED Mr Christopher Cheng is the Chairman. It examines and approves the parameters and basis used in the preparation of the annual budget, which will then be submitted to the Board for approval. It reviews performance against the approved annual budget half-yearly and makes recommendation to the Board regarding any revisions or actions that may be required.

### Attendance of Directors at Budget Committee meetings in 2006-07

Number of meetings	1	
Attendance of individual Directors		
Christopher W C Cheng (Chairman) <sup>1</sup>	1	100%
Raymond P L Kwok (Chairman) <sup>2</sup>	N/A	N/A
Liu Pak Wai (Deputy Chairman) <sup>3</sup>	1	100%
Peter Au-Yang <sup>4</sup>	N/A	N/A
Paul Kennedy <sup>5</sup>	1	100%
Alexa Lam	1	100%
Angelina Lee <sup>6</sup>	1	100%
Martin Wheatley	1	100%
<b>Average attendance of meetings</b>	<b>100%</b>	

<sup>1</sup> Appointed as Chairman on 17.7.06

<sup>2</sup> Membership until 31.7.06

<sup>3</sup> Appointed as Deputy Chairman on 17.7.06

<sup>4</sup> Membership until 25.5.06

<sup>5</sup> Membership from 28.11.06

<sup>6</sup> Membership from 1.8.06

The **Executive Committee** comprises all EDs and the Chief Counsel. Mr Martin Wheatley, CEO, is the Chairman. This committee was formed during the year, with Board approval, to enhance the efficiency and effectiveness of the executive decision-making process. It performs administrative, financial and management functions as delegated by the Board and considers policy issues for recommendation to the Board. The Executive Committee also coordinates and oversees the exercise of functions that have been delegated to individual EDs. The Management Committee, which previously performed certain administrative, financial and management functions, was absorbed into the new Executive Committee. Minutes of the Executive Committee are provided to the Board on a regular basis.

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### Conduct standards

The SFC requires the highest standards of integrity and conduct from its staff and is conscious of the role this has in promoting and maintaining public confidence in the SFC. Our requirements and the relevant legal obligations in respect of confidentiality, conflict of interests and personal investment etc are set out in our Code of Conduct which all staff must formally acknowledge. Disciplinary action is considered against any staff who do not comply with the Code. In addition to disciplinary action, the staff concerned may be subject to penalties specified by law.

We encourage open communications within the SFC and seek to handle grievances and complaints in an efficient and open manner. We have established standard procedures for handling grievances concerning the employment of individual employees, grievances concerning the public interest and complaints in relation to equal employment opportunities. We have published the procedures for public interest grievances on our website to assist those who believe that they have discovered improper practices or misconduct relating to the running of the SFC or work-related activities of SFC employees, to report these to the SFC in a constructive and confidential manner. The procedures enable the following persons to report confidentially: any person who has an employment contract with the SFC, is on secondment to the SFC, is engaged as an independent consultant by the SFC or is a contractor or supplier of services to the SFC.

We take seriously any dissatisfaction regarding the way in which SFC staff have carried out or failed to carry out their duties. The Procedures for Handling Complaints against SFC Staff ensures prompt handling of any complaints from members of the public against our staff and facilitates effective follow-up action. We have published the procedures on our website to enhance transparency and provide clear guidance to the public in making such complaints.

### Accountability, transparency and internal control

We strive to act firmly, fairly and in a transparent and accountable manner in exercising our powers and carrying out our duties. To achieve this aim, individual divisions and departments of the SFC follow established procedures and guidelines in making decisions and taking actions.

To ensure proper use and management of financial resources, we have established detailed policies and procedures for

financial control. The financial control procedures set out levels of authority and delegation of functions for administration, financial and management functions. Matters such as the appointment of consultants, collection of fees, investment, and purchasing or disposal of fixed assets etc are all clearly set out in the financial control procedures.

We have certain statutory obligations in terms of financial control and reporting such as keeping proper accounts and records of transactions. We are also required by law to prepare financial statements to give a true and fair view of the state of affairs of the SFC as at the end of the financial year and of the results of its operations and cash flows in the financial year. These financial statements are subject to an annual independent audit, approved by the Board and signed by the Chairman and the CEO. Each year, the revised and proposed budgets are submitted to the Financial Secretary for approval and laid before the Legislative Council after consideration by the Board. The Director of Audit may also examine any books, accounts, vouchers, records or documents that we keep.

We are committed to open communication with our stakeholders and the public. We discuss our operations and activities through our Quarterly Reports which are published voluntarily, Annual Report, press conferences and other publications. We also maintain a user-friendly website to provide the public with comprehensive and updated information about us including contact details for enquiries and complaints. Last year, we conducted the second periodic survey to obtain the views of our stakeholders about our work, our effectiveness as a regulator, and the areas where we should apply more focus. The results of this survey were communicated to the public through a press release and are available on our website.

We have the power to make rules under various provisions of the SFO. It is a statutory requirement that we consult the public on any rule changes and subsequently publish a document setting out in general terms the public's representations on the draft rules, our response to the representations, and details of any major modifications to the draft rules. Although we are only required to consult the public on rule changes, we consistently exceed statutory requirements by also consulting on proposed non-statutory codes and guidelines, and amendments to them.

We have appointed an external audit firm, PricewaterhouseCoopers, to conduct annual internal control reviews for us. The focus

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of this review is approved annually by the Audit Committee and forms part of the SFC's overall annual internal control review programme.

The purpose of the internal control review is to assess whether the systems of internal control as set out in the various SFC's manuals are adhered to, to evaluate the adequacy of the controls in place, and to identify enhancements to current procedures and controls to improve operating efficiency. The internal controls are designed to provide reasonable, but not absolute, assurance that errors and irregularities will not occur, and that procedures are performed in accordance with management's intentions.

We have an internal contingency plan to deal with emergency situations that may affect the SFC's operations, such as fire, flooding and other natural or man-made disasters. The plan details the contingency measures for all operational and support functions in recovering and resuming their business during and after any emergency.

We have developed an information security policy and established an information security unit. We have established an information security framework to manage our IT environment and all staff are required to attend mandatory information security awareness training.

### Independent checks and balances

The SFC is subject to various external checks and balances designed to ensure fairness and observance of due process, and to prevent misuse of regulatory powers.

The Process Review Panel (PRP) for the SFC is an independent, non-statutory panel, established by the HKSAR Chief Executive in November 2000, to review and advise upon the adequacy of the SFC's internal procedures governing the operational decisions and actions. The SFC is the first securities regulator in the world to introduce such an external review system of its internal operations. The PRP has the power to review files of any completed or discontinued cases to verify that we have followed the procedures that govern our operational decisions and actions. The PRP currently comprises 10 members, including eight members from the financial sector, academia and the legal and accountancy professions, and two ex-officio members, the representative of the Secretary for Justice and the Chairman of the SFC. In July 2006, the PRP published its annual report on its 2005 review. It concluded that, in general, the SFC had been

adhering to established internal procedures in its decisions and actions. In 2006, the PRP reviewed 40 completed cases. These cases covered: licensing and inspection of intermediaries, authorisation of collective investment schemes, handling of complaints, and enforcement actions including settlement and fining.

A wide range of the regulatory decisions of the SFC are subject to a full merits review by the Securities and Futures Appeals Tribunal (SFAT), which is chaired by a High Court judge and comprises two other members appointed by the Secretary for Financial Services and the Treasury. The SFAT has the power to call new evidence, stay any of the proceedings in the review, confirm, vary or set aside SFC decisions. There were 10 applications for review lodged with the SFAT during the year: one was determined, four were withdrawn and five are in progress. In addition, 11 cases were carried forward from 2005-06, of which three were determined, five were withdrawn and three are in progress.

The Independent Commission Against Corruption (ICAC) has conducted periodic corruption prevention reviews on the procedures and practices of the SFC since 1990. The ICAC conducted a review on the work of the Licensing Department in 2006 with no adverse findings.

Members of the public can complain to the Ombudsman against the SFC regarding the actions taken by the SFC and its staff in the discharge of their functions and powers. During the year, there were eight complaints. The Ombudsman found six of the cases not substantiated and is still dealing with the remaining two cases.

Anyone who is dissatisfied with the SFC's performance of its functions may take civil action in the Courts, by either applying for judicial review of the SFC's decisions or seeking remedies. There were two applications for judicial review against the SFC last year. The applicant in one of the cases was not granted leave by the court to proceed with the judicial review. The applicant's subsequent appeal to the Court of Appeal was dismissed. The other case of judicial review is in progress.

Although, the SFC is an independent regulatory body, it reports regularly and furnishes information to the Financial Secretary, the Secretary for Financial Services and the Treasury, and the Financial Services and the Treasury Bureau regarding important regulatory or market issues. We are also required to consult the Financial Secretary before exercising certain powers.

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### Performance pledges

In discharging our regulatory duties, we pledge to be responsive to the general public, market participants, and intermediaries

under our supervision. The following table shows how we met our pledges last year.

Performance pledges			% of cases meeting the pledge in 2006-07
Investor enquiries			
■ Preliminary response to telephone enquiries	4 business days		100%
■ Preliminary response to written enquiries	2 weeks		100%
General enquiries			
■ Preliminary response to enquiries via enquiry@sfc.hk	4 business days		99.7% <sup>1</sup>
Public complaints			
■ Preliminary response to verbal & written complaints	2 weeks		99.8% <sup>2</sup>
Processing of licensing applications <sup>3</sup>			
■ Representatives (provisional licence)	7 business days		90%
■ Representatives (normal licence)	8 weeks		65% <sup>4</sup>
■ Representatives (responsible officers)	10 weeks		90%
■ Corporations	15 weeks		97%
■ Transfer of accreditation	7 business days		87%
Modification/waiver and subordinated loan applications			
■ Acknowledgement of receipt upon receiving any application	2 business days		100%
Investment products authorisation			
■ Take-up of applications upon receipt	2 business days		100%
■ Preliminary response to applicants after take-up for unit trusts, mutual funds, investment-linked assurance schemes and Mandatory Provident Fund pooled investment funds	7 business days		100%
■ Preliminary response to applications after take-up for other schemes	14 business days		100%

<sup>1</sup> Some cases failed to meet the pledge due to the exceptionally heavy workload when the enquiries were received.

<sup>2</sup> Two cases failed to meet the pledge due to its complexity. More time was needed to collect information to facilitate assessment.

<sup>3</sup> Performance pledges only applied to cases where the applicants had supplied all the required documentation in their applications and satisfied all regulatory requirements.

<sup>4</sup> The percentage has fallen (87% in 2005-06) due to the high staff turnover, additional work load (13% increase in the number of licensees compared to the year before) and having had to divert resources to process corporate applications. Nevertheless, the majority of the applications were approved within one to two weeks after the pledge.

### Care for Employees

The SFC considers its staff its greatest asset and treating them well is fundamental to the development of our organisation. We aim to be an employer of choice by providing appropriate and comprehensive remuneration and benefits, personal development opportunities, a healthy and safe environment and a family-friendly workplace. We are pleased to have been able to adopt a five-day week this year which has considerably improved the overall working circumstances of our staff.

As at 31 March 2007, there were 443 staff (2005-06: 441), comprising 402 permanent and 41 temporary staff. At the end of March 2007, 197 (44%) of our staff held professional qualifications. We also employed 69 undergraduates from local and overseas universities as part time interns for periods of several weeks each.