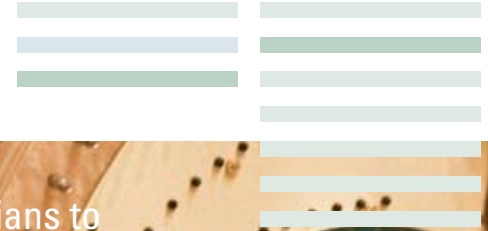
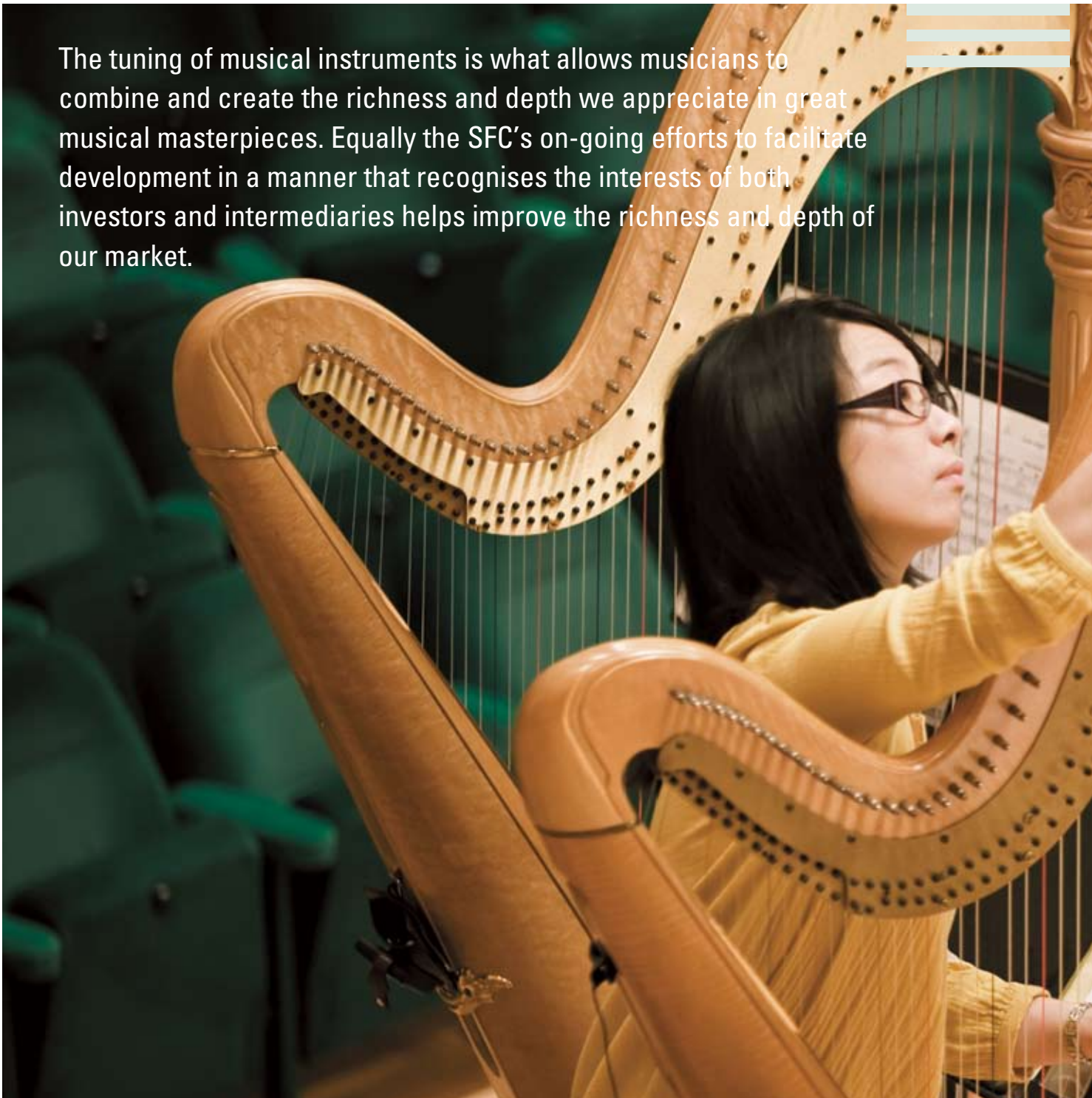


# Facilitation



The tuning of musical instruments is what allows musicians to combine and create the richness and depth we appreciate in great musical masterpieces. Equally the SFC's on-going efforts to facilitate development in a manner that recognises the interests of both investors and intermediaries helps improve the richness and depth of our market.





## Facilitation

The SFC’s responsibilities include facilitating the development of the securities market to help Hong Kong maintain its reputation as the leading international financial centre in Asia. In discharging all of our regulatory responsibilities, we aim to maintain an orderly and fair market but in a manner that does not impose undue burdens or restrictions on industry participants. We believe that a balanced approach to regulation has helped, and will continue to help, attract quality investors and intermediaries to our markets.



CEO Mr Martin Wheatley delivers a speech at the Hong Kong Institute of Chartered Secretaries.

Global products are becoming ever more sophisticated and technically complex, requiring world-class markets to be flexible and innovative. It is vital that our regulatory regime can accommodate this dynamic environment and be responsive to evolving market needs, while still maintaining appropriate regulatory standards.

During the year we worked on several fronts to boost the market’s attractiveness and adaptability. This included measures to streamline and speed up existing regulatory processes, to reduce costs to market players and to broaden product choice.

We have taken some positive steps to make our licensing process more efficient and market-friendly as part of a longer term exercise which will see us re-engineer and automate all of our processes in this area.

We are also responsive to innovation and on a case-by-case basis, have accommodated a number of intermediaries with unique business models by granting specific exemptions or modifications to the Financial Resources Rules requirements where there are no investor protection concerns. This year

this approach has allowed seven intermediaries to operate more effectively in our market when otherwise the Financial Resources Rules constraints would have made this extremely difficult or impractical.

We continued our focus on the Mainland as a crucial partner in the development of Hong Kong's market and built on the strong foundation laid down in previous years. In particular we facilitated the implementation of the QDII scheme and helped pave the way for Mainland asset managers setting up operations under Supplement IV to CEPA.

On the international front we remain active in all five Standing Committees of IOSCO which deal with many aspects of securities regulation and industry issues relevant to securities markets, on which global regulators seek to co-operate and to develop common standards. We also hosted two IOSCO standing committee meetings in November 2007 dealing with issues on accounting and auditing as well as investment management.

### Hong Kong as a fund innovator

Hong Kong's asset management business enjoyed significant growth over the past year with buoyant markets attracting more investors to fund products. We have worked hard to encourage the development of the industry – both new asset managers and new funds – as part of the deepening of the Hong Kong market, and also to increase the number and range of SFC-authorized funds available to investors.

281 new retail funds were authorised during the year and by the year end there were 2,123 SFC-authorized funds (an increase of 7 per cent over the previous year) with an aggregate net asset value of more than US\$1 trillion.

Hong Kong is now the largest exchange traded fund (ETF) market in Asia ex-Japan, with 17 SFC-authorized ETFs with a combined market capitalisation of US\$12 billion. As at end-March 2008, there were 244 SFC-authorized UCITS III funds which utilise financial derivative instruments for investment purposes.



Regular publications enhance understanding of our work.

In terms of product authorisation, there were a number of notable firsts during the year:

- The first commodities futures ETF, which was listed in April 2007
- The first actively managed closed-end fund investing primarily in the A-share market, which was listed in July 2007
- The first retail 130/30 UCITS III fund, which was authorised in July 2007
- The first UCITS III fund that has significant exposure to hedge fund indices, which was authorised in November 2007
- The first retail Islamic fund, which was authorised in November 2007
- The first Real Estate Investment Trust (REIT) managed by an international REIT manager, which is also the second REIT with cross-border investment property in the Mainland

## Facilitation



The SFC issued 8,615 licences, up 44% over the previous year.

We also enhanced the efficiency of our review and approval processes by giving practical and proactive guidance in relation to the conduct of substantial transactions by REITs, such as the first acquisition of Mainland property by a listed REIT in Hong Kong announced in January 2008.

### Enhanced flexibility

During the year, we approved more than 8,600 new items of marketing material and 3,700 revisions to existing scheme documents and related notices of our authorised products. While we turn around applications for approval on a timely basis, there are inevitable time and cost implications for issuers. We have therefore undertaken a review of this process and proposed changes to streamline the review of marketing materials and notices for investment products, moving from a pre-vetting to a post-vetting and monitoring regime. This change would bring us in line with international standards and practices with regard to the approval of marketing material for authorised products. A public consultation was commenced in February 2008 and the comments received were generally supportive of our proposals. We will publish our consultation conclusions later this year.

The investment management operations of SFC-authorised funds must be based in an Acceptable Inspection Regime (AIR) unless otherwise approved by the SFC. Starting in October 2007, managers of SFC-authorised funds were granted greater flexibility in delegating investment management functions to their affiliated companies located in overseas jurisdictions beyond those on the AIR list. We now have funds managed in AIR jurisdictions such as the UK and the US, as well as non-AIR jurisdictions including Belgium, Bermuda, Brazil, Japan, the Netherlands, Singapore and Switzerland.

In order to improve efficiency and accuracy we have proposed measures for all licensed corporations to submit financial returns electronically, extending the current voluntary regime. A new submissions platform is now being created, including high levels of security, which will be provided to intermediaries, together with training, during 2008. With the new electronic submission facilities, licensed corporations will be able to flexibly prepare and amend their

returns electronically at any time before the submission deadline and built-in arithmetic checks will help reduce clerical and data entry errors.

### Streamlined processes

The hedge fund industry benefited from a streamlining of their licensing process that we introduced in 2007, with the average processing time for managers cut by 45 per cent. The average period taken by us to approve in principle the licence applications for hedge fund managers is now nine weeks, with well prepared applications taking as little as four weeks to approve in some instances.

For the whole year, we approved 53 licence applications from hedge fund managers, a 47 per cent increase from last year. At year end, the total number of licensed hedge fund managers topped 200, compared with 154 in the previous year.

Under our streamlined process, persons nominated to be the Responsible Officers (ROs) of hedge fund managers can be exempted from the local regulatory examination if they fulfil certain specified criteria. Under the new procedures we recognise a broader range of past industry experience for RO qualification. Policies concerning office premises and the need for ROs to be physically present in Hong Kong have also been clarified.

Our Takeovers team has also streamlined and refined procedure for applications for exempt fund manager and exempt principal trader status.

### Measures involving listed companies and the exchanges

We continue to enhance and develop our relationship with the Stock Exchange, in order to facilitate and encourage new entrants to the securities market, without reducing regulatory standards, with a focus on making it quicker and easier for them to start their businesses.

#### The principal measures and improvements achieved during the year were:

- Working on a framework for the listing of overseas companies in Hong Kong by way of depositary receipts.

Existing shareholder protection in the Listing Rules will apply to depositary receipt issuers following amendments to the rules.

- Steps were taken to improve transparency of takeovers proceedings by opening disciplinary hearings before the Takeovers and Mergers Panel and Takeovers Appeal Committee to the public with effect from 1 April 2008.
- The market was consulted on proposed amendments to the Takeovers Code relating to dealings by connected discretionary fund managers and principal traders before and during an offer period, transactions involving the disposal by a company of its assets or operations and the possibility of delisting of the trading in the shares of that company and securities borrowing and lending. The proposed amendments will provide the market with greater clarity. The SFC is currently considering the public comments received.
- The SFC sought to improve timely publication of disclosure of interests information through mandatory electronic submission of these notices. The market was consulted on the proposed changes and the overall response received was positive. It is hoped to implement the proposal as soon as practicable.
- In November 2007 the SFC approved an HKEx proposal to allow Exchange Participants (EPs) to transfer their clearing and settlement obligations in the Central Clearing And Settlement System to another clearing participant. Third party clearing provides EPs with more flexibility in managing their business operations. We are also discussing with HKEx its proposal to admit overseas companies as Remote Exchange Participants. This would give more choice to overseas market participants and improve efficiency.
- We oversaw HKEx's upgrading of the trading, clearing and network systems to cope with increases in market activities. The SFC also administered Part III of the SFO in relation to the authorisation and on-going reporting of the Automated Trading Services. Two new authorisations were granted in 2007.
- Further flexibility in the position limits regime was achieved by enabling, in appropriate circumstances and with SFC approval, EPs or their affiliates to exceed the statutory limits for Hang Seng Index and Hang Seng

## Facilitation

China Enterprises Index futures and options contracts by up to 50 per cent. This follows an earlier relaxation of position limits for the Hang Seng China Enterprises Index futures and options contracts effective from 30 March 2007.

### Other products

Action was taken during the year to facilitate the introduction of more innovative products, as well as reducing the compliance burden and costs faced by intermediaries.

In particular, on 7 December 2007 we announced that waivers from certain disclosure obligations by issuers of listed structured products may be applied for on an annual basis rather than in respect of each product listed.

We approved the launch by HKEx of other initiatives including the new Hang Seng China H-Financials Index futures contract, the Mini H-shares Index futures contract and Market Access Products.

The SFC also authorised the issue of offering and marketing materials to facilitate three public offerings of unlisted RMB bonds which had a total retail issue size of around RMB 3 billion.

### Co-operation with Mainland authorities

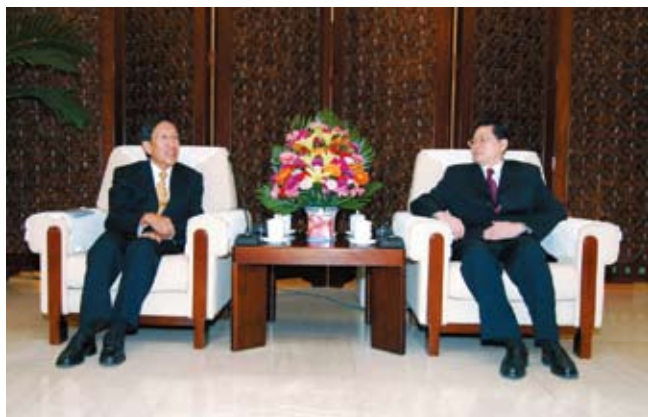
2007 saw the implementation of the Mainland's QDII scheme, reinforcing Hong Kong's role as a capital raising centre for Mainland enterprises. The SFC continues to work closely with its Mainland regulatory counterparts to

ensure that Hong Kong is the platform of choice for the implementation of the scheme. Some important milestones during the year were as follows:

- In April 2007, we signed an MOU with the CBRC for Hong Kong to become the first overseas jurisdiction that Mainland commercial banks could invest in. Hong Kong was the first market to benefit from the expansion of the investment scope of Mainland bank QDII.
- In June 2007, the CSRC announced provisional rules for QDII funds investing in overseas markets. The first QDII fund was launched in September 2007. Up to 40 per cent of the fund's assets are allocated to the Hong Kong market.
- In March 2008, a Regulatory Co-operation Agreement of Understanding was signed with the CIRC, which is the first agreement on regulatory co-operation and information exchange on the use of Mainland insurance funds outside the Mainland.

A senior SFC representative sits on the CSRC's QDII expert committee which approves QDII funds. During the year, our staff attended 14 committee meetings.

We continue to conduct regular exchanges of staff with the CSRC. We welcomed 24 individuals on secondment from the CSRC in 2007. In turn, 18 of our staff were seconded to the CSRC.



The SFC maintains close ties with the Mainland authorities.



Our publications facilitate the investing public in understanding our role and functions.

We encourage Mainland asset managers to set up business operations in Hong Kong which is permitted under Supplement IV to CEPA signed on 29 June 2007. To facilitate the establishment of these businesses, the SFC sponsored a high level seminar organised by the Hong Kong Investment Funds Association for a delegation of the Mainland's largest fund management and securities companies to visit Hong Kong in September 2007.

### Communication with the market

Keeping stakeholders and investors abreast of our activities is a top priority and we aim to achieve this through a variety of means. In our publications, the 'Enforcement Reporter' gives up-to-date information on recent cases. Over the past year we have given it a fresher look and included new sections to share changes in our thinking and approach with the market.

The 'Takeovers Bulletin' is a new publication this year. This is a periodic newsletter designed to provide practice notes and informal guidance to the industry as well as articles and information on takeovers.

Our Research team continues to issue analysis and commentary on matters relevant to Hong Kong's financial

markets, including this year a report on the stock options market which helped identify Hong Kong as the most active stock options market in Asia.

We gather information about the funds market and annually publish the Fund Management Activities Survey, the last one being in July 2007.

Our Annual Report was recognised for its clarity and scope, taking the Gold Award in the non-profit making and charitable organisations category of the Hong Kong Management Association's Best Annual Reports Awards 2007, and won the Citation for Achievement in Corporate Governance Disclosure. The report also received a Platinum Award in the Public Sector / Not-for-profit Organisations category in the HKICPA's Best Corporate Governance Disclosure Awards 2007.

During the year, 2,540 enquiries were received from our stakeholders. In addition, we received 835 enquiries from the media in addition to holding press conferences and briefings to keep members of the press up to date on topical issues and areas of concern.



Our Annual Report wins top awards.