

## Annual Report 2004-2005: Investors First

The SFC has published its Annual Report for the year ended 31 March 2005.

For 2004-2005, we posted a \$169 million surplus, 35% higher than the previous year. The surplus was on the back of a 13% increase in revenue to \$625 million, which in turn was mainly owing to similar percentage increases in stock market turnover and levy income.

We continued to manage our budget

responsibly. Extra spending was made only on areas considered necessary to improve market quality. Our operating expenditure increased 7% to \$456 million largely because of the variable pay awarded to performing staff and to address staff turnover.

Our reserves at the year end stood at \$860 million, equivalent to 1.7 times of the estimated expenditures for 2005-2006.

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## Cross-border co-operation enhanced

The SFC has taken several steps forward in strengthening cross-border regulatory co-operation with four regulators.

In May, we signed a Letter of Intent (LOI) with the Securities and Exchange Board of India (SEBI) to strengthen co-operation particularly in matters relating to cross-border trading and supervision of investment products.

With enhanced communication and

regulatory equivalence of the respective regulatory regimes, Hong Kong and India



SFC Chairman Mr Andrew Sheng (left) signing the LOI with SEBI Chairman Mr M. Damodaran in Mumbai.

hope to develop deeper and broader investment markets through trading in each other's markets of mutually acceptable investment products.

This LOI was signed in the spirit of mutual assistance and co-operation fostered among member regulators by the International Organization of Securities Commissions (IOSCO).

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## Revised REITs Code effective

The SFC has amended the Code on REITs to allow SFC-authorized REITs to invest in overseas properties.

The decision follows a public consultation, in which all 19 respondents supported lifting the geographical restriction.

We will also recognise the experience in managing property portfolio investments as a core competence for assessing the qualification of a REIT management company, and raise the gearing ratio to 45% of gross asset value of a REIT. Besides, we may consider on a case-by-case basis special product features, such as payment

of management fees by way of REIT units, if they are prevalent practices in established REIT markets, fair and reasonable and there are adequate safeguards to prevent conflicts of interest. Such features have to be clearly disclosed to investors.

The revised Code on REITs, including a Practice Note which serves to elaborate on the application of the Code specifically in the context of overseas investments, took effect on 17 June 2005.

For details, please see press release issued on 16 June 2005, available on the SFC website at: <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR137?openDocument>.



# Senior management interview

## Mr Stephen Birkett, Senior Director, Corporate Finance

### Please tell us your background.

I qualified as a solicitor in England and began practising commercial and corporate finance law in the mid-80s. I worked as a solicitor for about four years in England and 15 in Hong Kong. Before I joined the SFC, I was a corporate finance partner at Johnson Stokes and Master, advising on flotations, mergers and acquisitions, takeovers etc.

### Why did you quit the private sector?

I felt it was time for a change. Though my work was challenging and absorbing, the legal adviser operates within a certain spectrum. I was interested in the new role and perspective of regulatory work, such as the policy element. Also, I have been in Hong Kong for a long time, and the place and the people have been good to me—working at the SFC allows me to put something back into the community, and be involved in developing the market at its heart. The job is challenging and interesting, and my colleagues are congenial and professional.

### Is there a decision on the statutory backing of listing requirements yet?

There is consensus that we need to improve the regulation of listed companies,

with proper sanctions against corporate misconduct. However, there is more debate on the proper extent of the changes. We are working with the stock exchange and the Government on that, as we develop the conclusions from our recent public consultation exercise. I'm confident that we'll come up with the solution the market needs.

### When will the SFC consult on the prospectus regime review?

This is the third and most complex phase

of the review of the securities offering regime under the Companies Ordinance. We have prepared a draft consultation paper, after some extensive internal discussions and also soft consulting some key external parties. Those discussions are continuing. I would expect the consultation paper to come out within the next few months.

### There has been speculation about a ban on pre-deal research.

Yes, we're concerned at the leaking of pre-deal research into the newspapers. A ban on written pre-IPO research by connected analysts is one option that will be included in the consultation paper.

### Any other important projects?

We have recently completed the annual audit of the stock exchange's listing functions and procedures. We are also assisting the Government in the creation of the Financial Reporting Council. It will be partially funded by the SFC, and is aimed at enhancing the quality of financial reporting and regulation of auditors.



## Personal bio

- Joined the SFC in January 2005.
- M.A. (Modern Languages), Cambridge; CPE & Law Society Finals, Bristol.
- Previously commercial and corporate finance lawyer with Slaughter and May, Coudert Brothers, and Johnson Stokes and Master.
- Interests: Church life, family, hockey, Royal Geographical Society HK, Putonghua and music.

## Appointments

- The Financial Secretary has appointed **Mr Martin Wheatley** as the Executive Director (Supervision of Markets) for three years from 6 June 2005 to 5 June 2008. Mr Wheatley is formerly Deputy Chief Executive of the London Stock Exchange.
- The Financial Secretary has re-appointed **Dr York Liao** as a Non-Executive Director of the SFC for two years from 26 May 2005 to 25 May 2007.
- The Financial Secretary has appointed **Mr Henry Chan, Mr Jack Maisano, Mr Peter Sullivan, Ms Ada Tse** and **Mr Yip Lai-shing** and re-appointed **Mr Thaddeus Beczak, Mr Ambrose Cheung, Mr Paul Chow, Mr Paul Fan, Ms Christine Loh, Mr Samuel Poon** and **Mr Blair Pickerell** as members of the SFC Advisory Committee for two years from 1 June 2005 to 31 May 2007. The SFC thanks **Mr Stephen Hui, Mr Roger Luk** and **Dr Eden Woon**, who have retired from the Advisory Committee, for their valuable contribution.

# Review of Hedge Funds Guidelines

In view of the rapid development in the hedge funds industry, the SFC has proposed to enhance the regulatory regime for SFC-authorized hedge funds.

To strike the right balance between market facilitation and investor protection, we have proposed revisions to the Hedge Funds Guidelines to serve three key objectives.

We aim to

- strengthen the assessment criteria of managers of SFC-authorized hedge funds and provide greater flexibility in recognising the experience of fund managers' key personnel;
- enhance the measures for safeguarding investors' interest and the level of transparency; and
- codify our existing practices in authorising hedge funds and provide additional guidance to the interpretation of the provisions in the Guidelines.

Under the proposals for public consultation, a manager must have two key personnel with the requisite experience which is at least two years' specific hedge funds investment management

experience out of five years' experience. The manager as a firm must have the necessary internal systems, resources and risk management process in place.

We propose that additional information including the calculation of performance fees, the risk management process and the relationship between a fund and its prime brokers be disclosed. We also propose to make it mandatory for all SFC-authorized hedge funds to have independent valuation.

We also invite comments on two specific proposals to revise the Guidelines: (1) lowering of the current minimum subscription level for SFC-authorized single hedge funds from US\$50,000 to US\$30,000; and (2) the review of the current restriction imposed on the level of collateralisation to prime brokers for SFC-authorized hedge funds.

The consultation will end on 30 June 2005.

*For details, please see press release issued on 26 May 2005, available on the SFC website at: <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR126?openDocument>.*

## Annual Report 2004-2005

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The Annual Report details the SFC's achievements during last year and our work in progress.

It also has an analysis of the significant increase of our workload over the past decade and a comparison with international regulators which show our staff and expenditures have increased only moderately.

### Investors First:

As a regulator, the SFC does its utmost to educate the public and enable investors to protect their own interests. We see the well-being of the investors as key to the healthy development of the capital markets. The Chinese character 「健」, as in "Healthy" - 「健康」 and "Steady" - 「穩健」, is made up of 「人」 - "People" and 「建」 - "Develop" or "Establish". The Annual Report delivers a concise message that we put the interests of investors first, through "Regulation" 「規」, "Enforcement" 「行」, and "Education" 「信」.



*The Annual Report is available on the SFC website at: <http://www.sfc.hk/sfc/html/EN/speeches/public/annual/annual.html>.*

The photograph shows (from left) Executive Directors Mr Peter Au-Yang, Mrs Alexa Lam, Mr Andrew Sheng (Chairman) and Mr Alan Linning introducing the Annual Report at a press conference on 12 May.



## FAQs

**Q: How is the offer price in a general offer made to shareholders determined?**

**A:** Basically, the offer price in an offer for minority shareholders' shares is a commercial decision of the offeror. The SFC's Code on Takeovers and Mergers provides that the offer price should not be less than the highest price at which the offeror or persons acting in concert with the offeror bought the shares of the target company within the six-month period immediately before the announcement of the offer and during the offer period. As shareholders, you may accept or reject an offer after considering its terms.

## Fine-tuning of disclosure regime

The SFC has received general support for its proposals to make the disclosure of interests regime more user-friendly.

A total of 34 respondents commented on a public consultation paper released in January. They are generally supportive of the recommendations to fine-tune and rationalise the regime.

A number of the recommended changes are to make the regime more user-friendly. For example, we will change the disclosure forms so that they are easier to fill in and to understand; clearly define triggering disclosure events for "change in nature of an interest"; synchronise dates for reporting sales and purchases; and simplify the *de minimis* exemption regime. There are also changes proposed in specialist areas to better take account of business practices.

There is no consensus yet in the important area of disclosure of security interests. A working group comprising investors and practitioners will be set up to consider in depth if there are better alternatives.

Responding to market requests, we have published a note outlining our policy on investigation of suspected breaches in four areas: late disclosures; failing to complete the disclosure form in accordance with the directions and instructions; including in the form information which is false or misleading; and failure to make a disclosure of a notifiable event.

*For details, please see press release issued on 31 May 2005, available on the SFC website at: <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR131?openDocument>.*

## Cross-border co-operation enhanced

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The SFC in June signed a similar LOI with Guernsey's Financial Services Commission (GFSC).

The LOI was the fifth signed by the SFC, following those with our counterparts in Indonesia, Thailand, Sri Lanka and India. The LOI marks a progression in our initiative to dismantle unnecessary barriers to the cross-border trading of investment products by extending the SFC's intention to forge a more cohesive Asian market for investment products to promote the distribution of Hong Kong investment products in Europe and vice versa.

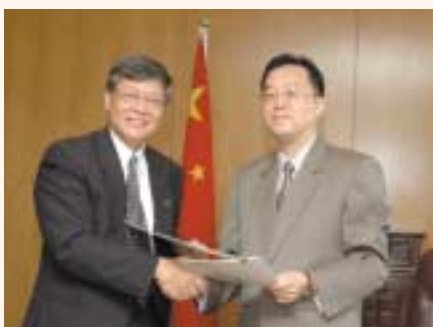
The GFSC is the SFC's first non-Asian partner in this endeavour. Given its strategic role in the European investment products market, Guernsey is ideally placed to explore with the SFC the means of achieving cross-border trading.



Senior Vice Minister for Financial Services of Japan Mr Akira Shichijo exchanging the signed SOI with Mr Sheng at the SFC's office in Hong Kong.

With regard to cross-border co-operation to enforce compliance with securities laws and regulations, the SFC signed a Statement of Intent (SOI) concerning co-operation and the exchange of information with Japan's Financial Services Agency in May.

The SOI establishes a framework for mutual assistance and facilitates information exchange to enable better enforcement of the securities laws and regulations of Hong Kong and Japan.



Mr Sheng exchanging the Side Letters with AMCM Chairman Mr Anselmo Teng in Macau.

Also in May, the SFC exchanged Side Letters with the Monetary Authority of Macau (AMCM) under the existing Memorandum of Understanding (MOU) concerning cross-border co-operation and the exchange of information.

The Side Letters explain how the SFC's and the AMCM's requests for information will be handled by each other subject to the MOU that was signed in 2000 to further mutual assistance and exchange of information.

*For details, please see press releases issued on 26 May 2005 (India), 3 June (Guernsey), 5 May (Japan) and 13 May (Macau) respectively, available on the SFC website at: <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR127?openDocument>; <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR134?openDocument>; <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR114?openDocument>; and <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR119?openDocument>.*



## Circulars

The following recently published circulars are available on the SFC website under "Legislation & Regulatory Handbook" - "Regulatory Handbook" - "Codes, Guidelines and Circulars" at: <http://eapp01.sfc.hk/apps/cc/RegulatoryHandbook.nsf/eng/GenerateHTMLTB?openAgent>.

1. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing US President's Executive Order 13224 (14.06.2005)
2. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing - US President's Executive Order 13224 (18.05.2005)
3. Circular to Licensed Corporations which are Participants of the Stock Exchange of Hong Kong Limited and/or Hong Kong Futures Exchange Limited - Fidelity Insurance for Exchange Participants (09.05.2005)
4. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing - United Nations (Anti-Terrorism Measures) Ordinance & United Nations Sanctions (Afghanistan) Regulation (05.05.2005)
5. Circular to Licensed Corporations and Associated Entities - Anti-Money Laundering / Combating Terrorist Financing - US President's Executive Order 13224 (26.04.2005)



Investor focus

## Every vote counts

Voting at shareholders' meetings is the best way to voice your views about the management of the listed company in which you have invested.

By Hong Kong law, a company must hold an annual general meeting (AGM) every year. At the AGM, shareholders are asked to adopt the audited annual report, and to approve the appointment of directors and auditors. Shareholders may also be asked to approve the declaration of dividends or a general mandate for issuance of shares.

There are other occasions where shareholders' approval is sought. These include major changes of the company's business, certain corporate actions or significant transactions such as rights issues, takeovers and share consolidation or share split.

Voting may be done by a show of hands or by poll. On a show of hands, every shareholder present at a shareholders' meeting is entitled to one vote, regardless of the number of shares held. If

voting is held by poll, every share carries one vote.

Poll must be used for voting on transactions where interested shareholders are not allowed to vote e.g. connected transactions and granting of options to substantial shareholders, independent non-executive directors or their associates.

Normally, only registered shareholders can attend and vote at general meetings. You may vote in person or by proxy. A proxy is a person appointed by you to attend and vote on your behalf. The proxy needs not be a shareholder.

If your shares are held by a brokerage or a bank as nominee, you have to tell them how to vote for each resolution.

Your votes may influence how a company is run and may have a direct impact on your investment returns.

*For details, please visit the eIRC's "Features & Dr Wise / Shareholder Basics - FAQs" section at: [http://www.eirc.hk/eirc/html/EN/features/share/features\\_86\\_224\\_295.htm](http://www.eirc.hk/eirc/html/EN/features/share/features_86_224_295.htm).*

## Record enrolment for teachers workshops

The latest round of investor education workshops for teachers has attracted a record 1,800 enrolments.

The SFC has invited secondary school and vocational education teachers of Economics, Accounting, Commerce and related subjects to 16 workshops from 13 June to 14 July to improve their understanding of investment activities and investor protection measures.

The workshops ultimately aim to help students improve their financial literacy, develop positive values, and learn personal financial management.

The programme covers various investment products and services including a new Personal Financial Planning module.

Since 2000, the SFC has run 96 workshops with over 6,200 enrolments.

A "Teachers Corner" has been set up on the Electronic Investor Resources Centre (eIRC) at [www.eirc.hk](http://www.eirc.hk).

*For details, please see press release issued on 18 May 2005, available on the SFC website at: <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR120?openDocument>.*

## In brief

The SFC has consulted the public on proposed revisions to the **Prevention of Money Laundering and Terrorist Financing Guidance Note** in order to bring it in line with the latest recommendations of the Financial Action Task Force on Money Laundering, incorporate industry-specific guidance contained in an IOSCO paper for client identification, and add guidance to measures for licensees and their associated entities to effectively curtail money laundering and terrorist financing. We expect to publish the Consultation Conclusions in the third quarter and implement the new Guidance Note by the year end.



Investor resources

The following items of investor resources have been made available to the investing public or updated recently. They can be found on the Electronic Investor Resources Centre (eIRC) at the URLs provided.

### Investor Alert Updates (<http://www.eirc.hk/eirc/html/EN/alert/alert.htm>):

16 unlicensed companies/entities have been added to the Alert List: "Smith and Henderson" "Taylor Ferguson", "Wells Fargo (not related to Wells Fargo & Company, USA)", "Wilton & Smythe Associates" (15.06.2005); "Global Investor's Network System" (01.06.2005); "APAC Finance Ltd", "Crown Choice International Ltd", "Crown Sense Ltd", "Iontrack Ltd", "Options International Ltd", "Sinowest International Corp Ltd", "Trimark World Capital Corp", "SouthTrust Bank (not related to SouthTrust Bank, which has been merged with Wachovia Bank, N.A., USA)" (18.05.2005); "First Colonial Management", "Orion Ventures Limited", "Smith Klein Venture" (25.04.2005). Information of four entities including "Bernard Simpson Consultants" (15.06.2005); "SMI Limited (BVI)" (02.06.2005); "Orion Ventures Limited" (27.05.2005 and 25.05.2005); "The Williams Group" (20.05.2005) has been updated on the list.

### Dr Wise's Column (<http://www.eirc.hk/eirc/html/EN/features/index.htm>)

"Know a Fund's Asset Mix" (31.05.2005) and "Be Smart When Investing Online" (26.04.2005).

# Working group to develop XBRL

A Preparatory Working Group (PWG) has been formed to assist with the development of an evolving global standard for handling business and financial data in Hong Kong.

Major markets including the US, UK, Japan and the Mainland are considering adopting the eXtensible Business Reporting Language (XBRL) in the areas of regulatory filings and the filing of corporation tax returns. XBRL greatly accelerates data handling, reduces error and permits automatic information checking.

By providing an identifying tag for each individual item of data, XBRL facilitates the standardisation for processing of accounting information. Previously, such consolidation would require manual adjustment of each category of accounting information into a standard format.

The PWG aims to identify regulatory and business applications of XBRL for financial reporting in Hong Kong; recommend to adopt relevant accounting standards and regulatory requirements for XBRL implementation; prepare to form the "XBRL Jurisdiction" in Hong Kong; and determine the time frame for XBRL development in Hong Kong and establish links with established XBRL Jurisdictions.

For details, please see press release issued on 26 April 2005, available on the SFC website at: <http://eapp01.sfc.hk/apps/cc/PressRelease.nsf/eng/lkupNewsCode/05PR110?openDocument>.



Under the proposed framework for the PWG, there is a Steering Committee which provides the necessary leadership and direction. Members of the Committee: (Back row, from left) Ms Margaret Chan (Commerce, Industry & Technology Bureau), Mr Michael Taylor (HKMA), Mr Gordon Jones (Companies Registry), Mr Andrew Sheng (SFC), Ms Lucia Li (The Treasury), Ms Diana Chan (Mandatory Provident Fund Schemes Authority), Ms Alice Cheung (Financial Services and the Treasury Bureau). (Front row, from left) Mr Andrew Kanaganyagam (Hong Kong Association of Banks), Ms Irene Wong (Hong Kong Federation of Insurers), Mr Herbert Hui (Hong Kong Institute of Directors), Mr William Gee (PwC), Mr Michael Chan (HKICPA), Mr Stephen Mak (OGCIO), Mr Karl Lung (Hong Kong Society of Financial Analysts), and Mr Chau Ho Man (Inland Revenue Department). We have created a new section for XBRL on the SFC's website at: [www.sfc.hk/sfc/html/EN/xbrl/xbrl.html](http://www.sfc.hk/sfc/html/EN/xbrl/xbrl.html) where you can find an introduction to the PWG and XBRL's benefits to Hong Kong.

## Other publications

The following publications have been published since the release of the last *SFC Alert*. They are available on the SFC website under "Speeches, Publications & Consultations" - "Publications" at: <http://www.sfc.hk/sfc/html/EN/speeches/public/public.html>.

1. Consultation Conclusions on Draft Practice Note on Overseas Investments by SFC-authorized Real Estate Investment Trusts (16.06.2005)
2. Revised Code on Real Estate Investment Trusts (16.06.2005)
3. SFC Enforcement Reporter - June 2005 (10.06.2005)
4. Consultation Conclusions on the Review of the Disclosure of Interests Regime under Part XV of the Securities and Futures Ordinance (31.05.2005)
5. Information on the SFC's policy regarding investigation of cases involving suspected breach of the Disclosure of Interests provisions in Part XV of the Securities and Futures Ordinance (31.05.2005)
6. SFC Quarterly Bulletin - Spring 2005 (30.05.2005)
7. Consultation Paper on the Review of Chapter 8.7 of the Code on Unit Trusts and Mutual Funds [on hedge funds guidelines] (26.05.2005)
8. Enforcement Reporter - May 2005 (20.05.2005)
9. SFC Annual Report 2004-2005 (11.05.2005)
10. Consultation Paper on the Proposed Revised Prevention of Money Laundering and Terrorist Financing Guidance Note (29.04.2005)



## Recruitment

The following SFC positions are open. For application and details of the openings, please visit the SFC website at: <http://www.sfc.hk/sfc/html/EN/aboutsfc/employment/employment.html>.

- **Manager - Investment Products**
- **Senior Translator/Translator**
- **Temporary Assistant**



## Subscription information

The bi-monthly *SFC Alert* forms part of our range of regular publications; others include the monthly *SFC Enforcement Reporter*, the *Quarterly Report*, the *Quarterly Bulletin* and the *Annual Report*. All these publications are posted on the SFC website.

Free subscription to the electronic version of the *SFC Alert* (and other publications) can be made to [sfcalert@sfc.hk](mailto:sfcalert@sfc.hk).



## Feedback

Tell us what you think of the *SFC Alert*. Questions and comments can be sent to [sfcalert@sfc.hk](mailto:sfcalert@sfc.hk).

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