



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

Quarterly Report

Jul - Sep 2005

A large, abstract graphic consisting of several overlapping, semi-transparent yellow planes. A large, stylized number '2' is prominently displayed in the center, suggesting this is the second quarterly report.

2

2005 - 2006



Table of Contents

Operations Highlights	1
Review of Operations	3
Securities and Futures Commission Condensed Consolidated Financial Statements	14
Investor Compensation Fund Condensed Financial Statements	22
Unified Exchange Compensation Fund Condensed Financial Statements	29
Commodity Exchange Compensation Fund Condensed Financial Statements	37

This is the Securities and Futures Commission's second Quarterly Report for the financial year from 1 April 2005 to 31 March 2006. The report aims to enhance the transparency and accountability of the Commission.

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Operations Highlights

1 July to 30 September 2005

Regulatory Developments

1. We concluded the review of the definitions of certain regulated activities and proposed some changes to cater for market developments, subject to LegCo negative vetting.
2. We are analysing the responses to the consultation on proposed amendments to the Securities and Futures (Stock Market Listing) Rules and have been in talks with the Exchange regarding its comments on the draft rules.
3. Amendments to the Securities and Futures (Investor Compensation - Levy) Rules, which provide for an automatic levy triggering and suspension mechanism, have become effective.
4. We are consulting the public on 21 proposed reforms to the regime governing the public offering of shares and debentures.
5. We concluded in August a consultation on the review of the Codes on Takeovers and Mergers and Share Repurchases. Some revisions took effect on 1 October.
6. We concluded the proposed revisions to the Prevention of Money Laundering and Terrorist Financing Guidance Note on 27 October.
7. We commenced a review of the regulatory framework of derivative warrants.
8. We completed a thematic review of hedge fund managers and held high-level discussions with the prime brokers to better understand the market.
9. The SFC in July approved a Listing Rules amendment to enable Exchange Participants to participate in share placement activities and rights issues of a suspended company in the five days immediately following its suspension.
10. We released in July the findings of the Fund Management Activities Survey 2004.
11. The revised Hedge Fund Guidelines came into effect on 30 September.
12. The SFC in September approved HKEx's rule amendments for the rollout of Phase I of SDNet. Migration of Participants' links to HKEx systems completed on 31 October.
13. Three workshops were held in August in the SFC's effort to work with the industry to promote the development of eXtensible Business Reporting Language (XBRL) in Hong Kong.
14. We are working closely with the Government, HKEx and other regulators to prepare for contingency events that may take place during the Sixth Ministerial Conference (MC6) of the World Trade Organization in December.



Enforcement and Regulatory Actions

15. During the quarter, the SFC had 15 prosecutions and took disciplinary action against 29 licensees for various regulatory breaches.
16. We sent an inspection team to three licensed corporations related to Banco Delta Asia S.A.R.L, designated as a “primary money laundering concern” by the US Department of Treasury, to monitor their financial position and ensure proper safeguarding of client assets.

Other Activities

17. The SFC released the findings of its first Public Perception Survey.
18. We further improved both our corporate website and the Electronic Investor Resources Centre (eIRC).
19. We stepped up our investor education on warrants through the Dr Wise's Column and newspaper articles.
20. We partnered with Lingnan University to launch two credit-based investor education courses.
21. We signed Letters of Intent with Malaysia's Securities Commission in July and Jersey's Financial Services Commission in September to work towards mutual recognition of mutually agreed investment products regulated by each respective authority.

Corporate and Financial Affairs

22. The SFC recorded a surplus of \$87 million for the second quarter. Total revenue for the quarter increased 26% from \$165 million to \$208 million. Levy income increased 37% as the average daily stock market turnover rose. Total expenditure (including depreciation) amounted to \$121 million, against \$116 million recorded in the last quarter.
23. A surplus of \$136 million was therefore recorded for the first six months of the financial year, compared to the projected surplus of \$8 million in the approved budget. Our reserves stood at \$996 million on 30 September.
24. On 20 September, the Board passed a vote of thanks to Mr Andrew Sheng, for his leadership as Chairman over the past seven years, as he attended the last Commission meeting.
25. Mr Martin Wheatley was appointed Chairman of the SFC effective from 1 October.



Review of Operations

1 July to 30 September 2005

This is the Securities and Futures Commission's second Quarterly Report for the financial year starting 1 April 2005.

Market Overview

The US market rebounded in July amid robust economic performance and the Fed's positive comments on economic outlook. Rising oil prices however triggered concerns over inflation. The terrorist attacks in London in July did not appear to have significant dampening impact on the performance of the markets. The Dow, S&P and NASDAQ rose 2.9%, 3.1% and 4.6% respectively. European markets continued to outperform their US counterparts, with the DAX, CAC and FTSE rising 10.0%, 8.8% and 7.1% respectively.

In the Mainland, the Shanghai Composite Index and Shenzhen Composite Index gained 6.9% and 8.1% respectively during the quarter. Major developments in the Mainland during the quarter included the revaluation of the RMB, the move to a managed floating exchange system, non-tradable shares reform, the increase in QFII quotas and the launch of the stock investors' protection fund. Nevertheless, market analysts were not certain whether the gains were attributable to these developments or technical rebounds from the troughs.

In Hong Kong, the market advanced on the revaluation of the RMB and the better-than-expected earnings of several index heavyweights. Although there were profit-taking activities in August, stocks rebounded as the land sale results in late September beat market expectations and signs of funds inflow emerged. During the quarter, the HSI gained 8.6% to close at 15,429 on 30 September, while the H-shares and red chips indices surged 7.5% and 22.4% respectively.

Trading was more active than the previous quarter. The average daily turnover on the Main Board rose 34.2% to \$20.5 billion. The average daily turnover of HSI constituent stocks climbed 20.6% to \$7.9 billion. The average daily turnover of H-shares increased 55.9% to \$4.8 billion and red chips' turnover was up 30% to \$2.7 billion.

On the Growth Enterprise Market, the S&P/HKEx GEM Index advanced 12.1% during the quarter to close at 1,008. Average daily turnover was \$115.6 million, representing a 41.8% increase from the previous quarter.

IPO activities were less active during the quarter. There were seven IPOs on the Main Board and three on GEM, compared with 14 on the Main Board in the previous quarter. The total amount of funds raised through IPOs was \$4.1 billion, compared to \$59 billion raised in the previous quarter when several new heavyweights were listed.



At the end of September, the open interest of HSI futures was 117,854 contracts, 3.6% lower than the end-June level. The open interests of H-shares Index Futures and HSI Options were 33,702 contracts and 214,039 contracts respectively, 24.6% and 31.5% higher than the end-June levels.

Securities and Futures Ordinance (SFO)

Maintenance of the SFO continued during the quarter.

The consultation conclusions paper on proposed amendments to the legal definitions of certain regulated activities set out in Part 2 of Schedule 5 to the SFO was published on 21 September. The Notice effecting the amendments is anticipated to be tabled before LegCo in November for negative vetting, with a proposed commencement date of 30 December. It is proposed that the definition of “asset management” be extended to include management of real estate investment trusts. To cater for market developments, dealings under certain prescribed circumstances would be excluded from the definition of “dealing in securities”. Giving of advice by a licensed asset manager in certain circumstances will also be excluded from “advising on securities/ futures contracts” definitions.

In conjunction with the Government’s consultation on proposed amendments to the SFO to give statutory backing to major listing requirements, the SFC issued a consultation paper on proposed amendments to the Securities and Futures (Stock Market Listing) Rules in January. We are now analysing the responses to the consultation and have been in talks with the Exchange regarding their comments on the draft rules.

Amendments to the Securities and Futures (Investor Compensation - Levy) Rules that provide for an automatic levy triggering and suspension mechanism were gazetted on 30 June and submitted to the LegCo for negative vetting on 6 July. Under the mechanism, the current investor compensation levies will be suspended if the net asset value of the Investor Compensation Fund exceeds \$1.4 billion, and re-imposed if the net asset value falls below \$1 billion. The Amendment Rules became effective on 28 October.

We met with respondents to the public consultation on a review of the disclosure of interests regime under Part XV to discuss proposed amendments to the law. A Working Group on Disclosure Requirements for Security Interests comprising market participants, investors, the lending industry and other interested parties held its first meeting in early October to study the issues raised during the public consultation and explore alternatives.

Raising Market Standards

The SFC issued a consultation paper on possible reforms to the regime governing the public offering of shares and debentures as set out in the Companies Ordinance (CO) in August 2005. The consultation paper contained 21 wide-ranging proposals: to unify the offering regimes for all investments currently regulated under the CO and the SFO; to extend prospectus liability to sponsors of a public offering and



the right to claim compensation for untrue statements in prospectuses to secondary market purchasers; to ban all written pre-deal research by connected analysts, and/or require publication of pre-deal research if leakage occurs in the media; to shorten prospectuses by allowing information to be incorporated by reference, etc. The consultation will end on 30 November.

In August, the SFC issued a consultation conclusions paper on the review of the Codes on Takeovers and Mergers and Share Repurchases. Main revisions that took effect on 1 October include new provisions barring “low-ball” offers and restricting existing board from taking frustrating actions against a successful offeror, a broad framework for dealing with telecom mergers and changes to shorten the vetting process. The SFC has also increased the membership of the Takeovers Panel from 30 to 40, to facilitate the expeditious and efficient dealing of matters by the Panel. New members were appointed to the Takeovers Panel and the Takeovers Appeal Committee in October.

Following the consultation on proposed revisions to the Prevention of Money Laundering and Terrorist Financing Guidance Note in April, the SFC held discussion with selected respondents during the quarter to better assess their views. The consultation conclusions paper was published on 27 October and the revised Guidance Note will be effective six months thereafter.

In light of the market concerns and comments regarding the derivative warrants market, the SFC has commenced a review of the regulatory framework of derivative warrants. In September, questionnaires were sent to all issuers, requesting information on incentive schemes and liquidity provision that would help the SFC consider the way forward on these two matters. We have also carried out an initial review of the Listing Rules and are studying the results and suggestions. In addition, we are closely monitoring the market to better understand and identify the related risks. We will work with the Exchange on the review and will consult on any proposed changes.

Partnership with the Industry

The number of intermediaries licensed by or registered with the SFC steadily increased by 3.8% from 23,805 as at 30 June to 24,722 as at 30 September.

To better understand the hedge fund industry, we have completed a thematic review of hedge fund managers based in Hong Kong, covering funds representing 45% of the total hedge funds assets under management in Hong Kong. In addition, we also held high-level discussions with senior management of the prime brokers of hedge funds. It was noted from this limited review that simple equity long short strategy was the most common investment strategy employed by single hedge funds, while leverage at the fund level was modest. We published a feature article in the form of FAQs in the July/August issue of the SFC Alert to address common licensing issues raised by fund managers.

The SFC in July approved a Listing Rules amendment to enable Exchange Participants to participate in share placement activities and rights issues of a suspended company in the five days immediately following its suspension.



The China Securities Regulatory Commission (CSRC) issued in August implementation details under Phase II of the Closer Economic Partnership Arrangement (CEPA) concerning joint venture futures brokerage in the Mainland with Hong Kong intermediaries. We have posted relevant FAQs on the SFC website for intermediaries' easy reference.

Statistical Information and Financial Position of the Securities Industry						
	As at 30 Sep 2005	As at 30 Sep 2004				
Total number of securities dealers and securities margin financiers	640	658				
Total number of active cash clients (Note 1)	610,062	599,763				
Total number of active margin clients (Note 1)	71,455	70,335				
Balance Sheet (Note 2)	(\$ Million)	(\$ Million)				
Cash in hand and at bank (Note 3)	107,785	97,864				
Amounts receivable from margin clients (Note 4)	17,263	15,775				
Amounts receivable from clients and other dealers arising from dealing in securities	160,211	83,372				
Proprietary positions	109,716	57,928				
Other assets	77,459	53,400				
Total assets	472,434	308,339				
Amounts payable to clients and other dealers arising from dealing in securities	226,188	134,014				
Total borrowings from financial institutions	66,118	39,421				
Short positions held for own account	36,855	19,453				
Other liabilities	62,464	40,752				
Total shareholders' fund (Note 5)	80,809	74,699				
Total liabilities and shareholders' fund	472,434	308,339				
Note 1: Active clients are clients for whom the licensed corporation is required to prepare and deliver monthly statement of accounts in respect of the relevant reporting month in accordance with Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules. Note 2: The significant increase in various items of the balance sheet is mainly attributable to the increase in market turnover during the period. Note 3: Cash in hand and at bank includes trust monies held on behalf of clients amounting to \$47,234 million (30/9/2004: \$42,153 million). Note 4: Average collateral coverage (the number of times the aggregate market value of securities collateral deposited by clients covers the amounts receivable from margin clients on a given date on an industry-wide basis): <table><tr><td><u>As at 30 Sep 2005</u></td><td><u>As at 30 Sep 2004</u></td></tr><tr><td>4.4</td><td>4.2</td></tr></table> Note 5: The value of shareholder's fund includes value of redeemable shares. Sources: Monthly Financial Returns submitted in accordance with the Securities and Futures (Financial Resources) Rules by securities dealers and securities margin financiers.			<u>As at 30 Sep 2005</u>	<u>As at 30 Sep 2004</u>	4.4	4.2
<u>As at 30 Sep 2005</u>	<u>As at 30 Sep 2004</u>					
4.4	4.2					

Facilitating Market Development

We released in July the findings of the Fund Management Activities Survey 2004 that covered licensed corporations and registered institutions. The combined fund management business had grown by 23% from \$2,947 billion in 2003 to \$3,618 billion at the end of 2004. Since the establishment of the SFC in 1989, the number of retail funds in Hong Kong had more than doubled from 781 to 1,933 at the end of 2004, with the value jumping 15 times from \$283 billion to \$4,300 billion. These findings again confirm Hong Kong's position as the Asian fund management hub for investors worldwide.

The SFC released the consultation conclusions paper on the Review of the Hedge Fund Guidelines on 26 September. Respondents supported the SFC proposals to strengthen the assessment criteria of hedge fund managers, to increase fund transparency, and to codify existing SFC regulatory practices in the authorisation of hedge funds. The revised Guidelines came into effect on 30 September. By the end of September, the SFC had authorised 13 retail hedge funds with assets under management of approximately US\$1.2 billion as at 30 June.

The SFC continued to monitor the latest developments in the Undertakings for Collective Investment in Transferable Securities (UCITS) III, the new regulations issued by the European Union Commission that govern funds domiciled in the EU states, and maintain dialogue with overseas regulators and market practitioners. As of the end of September, the SFC had authorised 850 UCITS III funds, representing over 84% of the applications received.

Number of SFC Authorised Collective Investment Schemes			
	30 Sep 2005	30 Jun 2005	30 Sep 2004
Unit Trusts and Mutual Funds	1,997	1,943	1,926
Investment-Linked Assurance Schemes	187	182	171
Pooled Retirement Funds	37	37	38
MPF Master Trust / Industry Schemes	45	45	45
MPF Pooled Investment Funds (Note1)	280	275	253
Other Schemes (Note 2)	94	87	57
Total	2,640	2,569	2,490
Note 1: There are 122 funds included in this category that are offered both as retail unit trusts as well as pooled investment funds for MPF purpose.			
Note 2: The schemes included equity-linked deposits.			

The SFC in September approved HKEx's rule amendments for the rollout of Phase I of SDNet, the next generation network for HKEx's securities and derivatives markets. Migration of Participants' links to its Hong Kong Futures Automated Trading System, Derivatives Clearing and Settlement System and Price Reporting System for the derivatives market onto SDNet completed on 31 October.

HKEx plans to introduce callable bull/bear contracts to the market next year. It is hoped that, subject to the right regulatory framework, these can provide an additional product choice for investors. The SFC continued to work closely with HKEx on the launch of the product.



The SFC continued to work with the industry to promote the development of eXtensible Business Reporting Language (XBRL) taxonomies for Hong Kong. XBRL is an evolving global standard for faster and more accurate electronic communication of business and financial data, while taxonomies are the dictionaries which XBRL uses and define the specific tags for individual items of data for financial reporting. Three workshops were held in August to promote market awareness of XBRL.

Hong Kong will be hosting the Sixth Ministerial Conference (MC6) of the World Trade Organization in December 2005. The SFC has set up a cross-divisional MC6 Task Force to prepare for any emergencies affecting the securities and futures markets that may arise. The Commission has been working closely with the Government, HKEx and other regulators to discuss the preparation for MC6 and identify areas for co-ordination.

Enforcement and Regulatory Actions

In July - September, the SFC successfully prosecuted 13 people and two companies - for disclosure of interests breaches, unlicensed activities, making unsolicited calls and providing misleading information to the SFC. Although there were no acquittals after trial during the quarter, we offered no evidence against one person and a company, and withdrew a summons issued to another person.

An individual convicted of market manipulation in the previous quarter was sentenced to three months' imprisonment, suspended for 18 months, and ordered to pay investigation costs to the SFC.

During the quarter, the SFC took disciplinary action against 29 entities for various breaches:

1. *Settlement without formal sanction* - A licensed corporation agreed to settle with the SFC over alleged failure to seek board approval or inform shareholders prior to changing the valuation time of four funds it administered and advised. Without admission of liability, the firm paid ex-gratia payments ranging from US\$10,000 to US\$60,000 to the four funds.
2. *Settlement with sanctions* - Five licensed corporations agreed to disciplinary actions including public reprimands and fines ranging from \$30,000 to \$400,000, for:
 - breaching Client Money Rules and Financial Resources Rules (FRR);
 - failing to prevent and detect unregistered dealing activities; and
 - internal control failures.

A total of 13 licensed individuals, including five responsible officers, agreed to disciplinary actions including public reprimands, fines ranging from \$6,000 to \$100,000, and suspensions for six weeks to five months, for:

- illegal short selling;
- improper trading activities in warrants;

- breaches of Client Money Rules and Money Laundering Guidelines;
- failing to inquire into clients' suspicious trades;
- accepting orders from unauthorised third parties;
- conducting discretionary trades without prior written authorisation; and
- failing to prevent and detect unregistered dealing activities.

3. *Suspensions* - The Securities and Futures Appeals Tribunal affirmed an SFC decision to suspend a previously licensed individual for failing to diligently explain to his client the downside risk of an investment, but reduced the suspension from six months to one month after the individual put forward important new evidence at the hearing. A responsible officer was suspended for three months for failing to properly supervise staff and negligently signing correspondence to the SFC which contained inaccurate and misleading information. A licensed representative, who was suspended for eight months for using client accounts to conduct personal trades and misallocation of a client's order, had her suspension extended by eight and a half months for using client accounts to conduct improper trading activities.
4. *Reprimands and fines* - A licensed corporation and its responsible officer were reprimanded and fined for FRR breaches. Two licensed representatives were reprimanded and fined for short selling and the responsible officer of their firms was also reprimanded and fined for failing to detect the short selling.
5. *Reprimands* - The Securities and Futures Appeals Panel (now repealed) decided that a public reprimand, instead of a suspension, was the appropriate penalty for a licensee who accepted unauthorised third party's dealing instructions because she had acted with the approval from her supervisors. A licensed representative (formerly a relevant individual of a bank) was reprimanded for short selling and other failings.

Statistics of Enforcement Actions			
	Jul - Sep 2005	Apr - Jun 2005	Jul - Sep 2004
Successful prosecutions	15	18	23
Entities disciplined (including settlement cases) (Note 1)	29	14	21
Warning letters issued (Note 2)	30	88	63
Cases under investigation (Notes 3 and 4)	494	494	538
Disciplinary inquiries in progress (Note 4)	109	108	105
Note 1: The number includes currently and previously licensed entities.			
Note 2: The decrease from the previous quarter was mainly owing to disclosure of interests breaches.			
Note 3: Some cases are ongoing investigations from the previous quarter.			
Note 4: Number of cases as at end of quarters.			



In September, an inspection team was sent to three licensed corporations related to Banco Delta Asia S.A.R.L, which had been designated as a “primary money laundering concern” by the US Department of Treasury, to monitor their financial position and ensure proper safeguarding of client assets as well as to review any anti-money laundering issues. The SFC has been liaising with HKMA and HKEx and we will continue to monitor the situation closely.

On the gatekeeping front, a public statement was issued against a licence applicant in respect of his previous misconduct. He had left the industry before a previous disciplinary action against him was concluded. Three licence applications were withdrawn by the applicants or the sponsoring licensed corporations during the quarter, where the applicants were involved in on-going investigation or disciplinary actions.

During the quarter, the SFC received 28 complaints in relation to boiler room operations. Liaison work with other domestic and overseas enforcement bodies in this regard will continue.

Strengthening Communication with Investors and Other Stakeholders

In September, the SFC released a report of findings of its first Public Perception Survey, conducted by the Social Sciences Research Centre of the University of Hong Kong. 1,375 individuals were interviewed. A majority of the public understood the SFC's overall responsibilities. About 66% of the respondents described the SFC as an overall securities market regulator. “Ensure the securities and futures markets are fair, efficient, competitive, transparent and orderly”, “Ensure proper disclosures of information by listed companies” and “Handle investors' complaints about market crimes/misconduct” were the three functions most recognised as the SFC's responsibilities. The overall rating of the SFC's performance in fulfilling its statutory objectives was 6.5 points out of 10. The survey establishes benchmarks against which the SFC may assess the public's perception and views in the future. The SFC will consider strengthening its publicity and investor education in areas of relatively low recognition and will further study the findings and determine how it may more effectively get its messages across to the public.

To make the SFC websites more resourceful and accessible, both our corporate website and the investor portal, the Electronic Investor Resources Centre (eIRC) were enriched during the quarter. We have added to the corporate website (www.sfc.hk) a text-only version to aid visually impaired visitors, and other new sections such as “Upcoming Events and Calendar” and “Contingency Information”. On the eIRC (www.eirc.hk), new interactive games on warrants, IPO, hedge funds, parallel trading and stock transaction costs were launched, together with new articles on Investment-linked Assurance Schemes and an online survey to gauge the public's views on the eIRC.

We have stepped up our investor education on the general misconceptions about warrants. The September issue of the educational Dr Wise's Column reminded investors that derivative warrants were not for everyone. We have started a warrant series in a weekly column in Metropolis Daily since late August. We are also reviewing existing educational information on warrants on the eIRC. In addition, we reminded



investors to exercise judgement on warrants recommendations in issuer-sponsored programmes and newspaper articles.

During the quarter, we gave talks to 130 participants of the Capacity Mileage Programme for Women jointly organised by the Open University of Hong Kong and the Women's Commission. We also spoke to secondary school and university students on market basics, investment advisors and financial analysts' recommendations.

In early October, the SFC introduced a wallet-sized card to remind investors to ask the right questions when choosing a financial product. We also partnered with Lingnan University again to launch two credit-based investor education courses.

We set up an exhibition in the Financial World Expo 2005 in Hong Kong where we distributed education materials on investment products and consumerism in engaging investment advisory services. The Expo, held in early October, drew more than 21,000 visitors.

In addition to derivative warrants, Dr Wise's Column also discussed structured notes and the risks of letting other people use your securities trading accounts.

We published the first Quarterly Report for the financial year 2005 - 2006 in mid-August on our financial position and operations in April - June.

We also continued to publish the bi-monthly newsletter SFC Alert, the monthly SFC Enforcement Reporter, and the Summer issue of Quarterly Bulletin to communicate with the public on our work and enforcement actions and to educate the investing public. All these publications are available on the SFC website.

Statistics of Investor Enquiries and Public Complaints			
	Jul - Sep 2005	Apr - Jun 2005	Jul - Sep 2004
Enquiries	1,205	1,159	918
Complaints	252	332	299

International Co-operation and External Relations

We continued to strengthen regulatory co-operation with our overseas counterparts. The SFC signed Letters of Intent with Malaysia's Securities Commission in July and Jersey's Financial Services Commission in September to work towards mutual recognition of mutually agreed investment products regulated by each respective authority.

During the quarter, the Commission received 15 requests from overseas regulators, nine seeking non-public information and six seeking investigatory and other assistance. Responses were provided to seven requests and the remainders were being processed. During this period, the Commission made one request to an overseas regulator for investigatory assistance.



We welcomed one local delegation, one Korean delegation, one Thai delegation and four Mainland delegations from both the government and the private sector during the quarter.

Financial Review¹

The SFC's financial position remained healthy during the quarter.

As compared with the previous quarter, total revenue for July - September increased 26% from \$165 million to \$208 million. Levy income increased 37% to \$151 million from \$110 million as the average daily stock market turnover rose from \$17 billion to \$22 billion². Total expenditure (including depreciation) increased 4% to \$121 million, from \$116 million. As a result, the SFC recorded a surplus of \$87 million for the quarter, 78% higher than the \$49 million recorded for April to June.

By the end of September, total revenue for the first six months of the financial year was \$373 million, 33% higher than the \$280 million in the same period last year. Levy income rose 40% to \$261 million as the average daily stock market turnover increased to \$19 billion from \$14 billion in the same period last year. Fees and charges income also rose 21% to \$94 million for the first six months this year, from \$78 million in the same period last year, owing to the increased market activity.

Total expenditure (including depreciation) for the six months was \$237 million, 6% lower than the approved budget of \$252 million. It was 17% higher than the \$203 million recorded in the same period last year mainly because no provision for staff variable pay was made last year. If a provision had been made last year, expenditure for the first half would only be 8% higher than that of the same period last year. This moderate increase was attributable to an increase in staff number and other expenses. The total number of staff at the end of September was 437, comprising 390 regular staff and 47 temporary staff. There were 421 staff a year ago.

As a result, the Commission recorded a surplus of \$136 million for the first six months of the financial year, compared to the projected surplus of \$8 million in the approved budget and the \$77 million surplus recorded in the same period last year.

At the end of September, our reserves stood at \$996 million, equivalent to 1.96 times the approved annual operating expenditure (including depreciation) of \$508 million.

Based on the current information and by managing our budget prudently, we continue to expect a surplus in the third quarter.

¹ We have consolidated the financial results of Investor Compensation Company Limited in this financial report.

² For income purpose, the turnover figure includes the amount of new fund raisings, which also attract transaction levy.



Corporate Affairs

The SFC welcomes the appointment of Mrs Susan Chow, Mr Stephen Hui and Mr Kevin Westley as new members to the Committee on Real Estate Investment Trusts (REITs) for one year, from 1 September 2005 to 31 August 2006, and thanks Mr Roger Hepper for his valuable contribution during the past two years.

The SFC also welcomes Ms Julia Charlton, Mr Stephen Cheung, Mr Herbert Hui, Mr Bill Kwok, Mr Michael Palin, Mr Gregory Terry, Mr Kenneth Willman, Ms Christine Wong and Mr Harold Wong as new members of the Takeovers and Mergers Panel and the Takeovers Appeal Committee from 1 October 2005 to 31 March 2006.

The Commission Possible Volunteers Group, the SFC's volunteers group, organised an outing to the Ocean Park with some South Asian ethnic minority families in July and a home visit to over 40 elderly people living in Wanchai during the Mid-Autumn Festival.

Looking Ahead

This is the first Quarterly Report since I was appointed SFC Chairman on 1 October.

I am honoured to be appointed by the HKSAR Chief Executive as Chairman of the SFC and feel privileged to succeed Mr Andrew Sheng. Mr Sheng has ably led the Commission for the last seven years and has made tremendous contribution to raising the international profile of the SFC and Hong Kong. On 20 September, the Board passed a vote of thanks to Mr Sheng for his leadership over the past seven years as he attended the last Commission meeting. Mr Sheng's tenure ended on 30 September.

Looking ahead, the challenge for Hong Kong is to preserve and build on its enviable status in Asia as a hub for finance and further develop its synergy with the Mainland. The objectives of the Commission will continue to be as set out in the SFO. As we regulate, we will balance the need for investor protection with facilitation of market development. We will continue to educate investors and practitioners. We will also enforce the law firmly and fairly.

I look forward to working closely with the Government, HKEx, market practitioners, professionals, investors, as well as the media to help Hong Kong excel as an international financial centre and premier fund raising centre for the Mainland.

Martin Wheatley
Chairman

14 November 2005



Independent Review Report

To the Securities and Futures Commission (the SFC)

(Established in Hong Kong under the Securities and Futures Ordinance)

Introduction

We have been instructed by the SFC to review the interim financial report for the six months ended 30 September 2005 set out on pages 15 to 21. We have not been instructed to review and have not reviewed the financial information for the three months ended 30 September 2005 included on page 15 of the interim financial report.

Respective responsibilities of directors and auditors

The directors are responsible for preparing an interim financial report of the SFC to comply with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board. The interim financial report is the responsibility of, and has been approved by, the directors.

It is our responsibility to form an independent conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Review work performed

We conducted our review in accordance with Statement of Auditing Standards 700 “Engagements to review interim financial reports” issued by the Hong Kong Institute of Certified Public Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

Review conclusion

On the basis of our review, which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six months ended 30 September 2005.

KPMG
Certified Public Accountants
Hong Kong
7 November 2005

Securities and Futures Commission

Consolidated Income and Expenditure Account

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited Three Months Ended		Unaudited Six Months Ended	
		30 Sep 2005	30 Sep 2004	30 Sep 2005	30 Sep 2004
		\$'000	\$'000	\$'000	\$'000
Income					
Levies		150,973	90,994	260,638	186,801
Fees and charges		48,123	37,753	93,982	77,983
Investment income		8,161	4,992	15,051	10,156
Recoveries from the Investor Compensation Fund		768	869	1,558	1,828
Other income		262	440	1,626	3,426
		<u>208,287</u>	<u>135,048</u>	<u>372,855</u>	<u>280,194</u>
Expenses					
Staff costs and directors' emoluments		94,184	77,458	185,742	155,639
Premises					
- rent		5,358	5,324	10,716	9,856
- other		3,430	3,336	6,868	6,130
Other expenses		13,401	10,067	24,520	20,820
		<u>116,373</u>	<u>96,185</u>	<u>227,846</u>	<u>192,445</u>
Depreciation		4,957	5,727	9,496	10,455
		<u>121,330</u>	<u>101,912</u>	<u>237,342</u>	<u>202,900</u>
Surplus	2	<u>86,957</u>	<u>33,136</u>	<u>135,513</u>	<u>77,294</u>

We have not prepared a separate statement of changes in equity as the surplus would be the only component of such a statement.

The notes on pages 19 to 21 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Consolidated Balance Sheet

At 30 September 2005

(Expressed in Hong Kong dollars)

	<u>Note</u>	<u>Unaudited</u> <u>At 30 Sep 2005</u> \$'000	<u>Audited</u> <u>At 31 Mar 2005</u> \$'000
Non-current assets			
Fixed assets		21,910	25,258
Held-to-maturity debt securities	3	602,092	550,407
		<u>624,002</u>	<u>575,665</u>
Current assets			
Held-to-maturity debt securities	3	438,366	294,398
Bank deposits		21,851	69,656
Debtors, deposits and prepayments		64,405	58,181
Cash at bank and in hand		2,969	1,692
		<u>527,591</u>	<u>423,927</u>
Current liabilities			
Fees received in advance		43,333	36,675
Creditors and accrued charges		45,066	30,765
		<u>88,399</u>	<u>67,440</u>
Net current assets		<u>439,192</u>	<u>356,487</u>
Total assets less current liabilities		1,063,194	932,152
Non-current liabilities	4	67,596	72,067
Net assets		<u>995,598</u>	<u>860,085</u>
Funding and reserves			
Initial funding by Government		42,840	42,840
Accumulated surplus	2	952,758	817,245
		<u>995,598</u>	<u>860,085</u>

The notes on pages 19 to 21 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Balance Sheet

At 30 September 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited At 30 Sep 2005 \$'000	Audited At 31 Mar 2005 \$'000
Non-current assets			
Fixed assets		21,776	25,012
Held-to-maturity debt securities	3	602,092	550,407
		<u>623,868</u>	<u>575,419</u>
Current assets			
Held-to-maturity debt securities	3	438,366	294,398
Bank deposits		21,851	69,656
Debtors, deposits and prepayments		63,833	57,845
Cash at bank and in hand		1,268	945
		<u>525,318</u>	<u>422,844</u>
Current liabilities			
Fees received in advance		43,333	36,675
Creditors and accrued charges		42,659	29,451
		<u>85,992</u>	<u>66,126</u>
Net current assets		<u>439,326</u>	<u>356,718</u>
Total assets less current liabilities		1,063,194	932,137
Non-current liabilities	4	<u>67,596</u>	<u>72,052</u>
Net assets		<u>995,598</u>	<u>860,085</u>
Funding and reserves			
Initial funding by Government		42,840	42,840
Accumulated surplus	2	952,758	817,245
		<u>995,598</u>	<u>860,085</u>

The notes on pages 19 to 21 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Consolidated Cash Flow Statement

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	Unaudited Six months ended 30 Sep 2005 \$'000	Unaudited Six months ended 30 Sep 2004 \$'000
Cash flows from operating activities		
Surplus for the period	135,513	77,294
Adjustments for:		
Depreciation	9,496	10,455
Investment income	(15,051)	(10,156)
Gain on sale of fixed assets	-	(27)
	<u>129,958</u>	<u>77,566</u>
(Increase) / decrease in debtors, deposits and prepayments	(3,593)	5,429
Increase in creditors and accrued charges	15,201	7,973
Increase / (decrease) in fees received in advance	6,658	(2,822)
(Decrease) / increase in non-current liabilities	<u>(4,471)</u>	<u>6,334</u>
Net cash generated from operating activities	<u>143,753</u>	<u>94,480</u>
Cash flows from investing activities		
Interest received	15,878	13,369
Held-to-maturity debt securities bought	(375,815)	(415,773)
Held-to-maturity debt securities redeemed	176,704	300,730
Fixed assets bought	(7,048)	(3,696)
Fixed assets sold	-	43
	<u>(190,281)</u>	<u>(105,327)</u>
Net decrease in cash and cash equivalents	<u>(46,528)</u>	<u>(10,847)</u>
Cash and cash equivalents at beginning of the six months	<u>71,348</u>	<u>77,963</u>
Cash and cash equivalents at end of the six months	<u>24,820</u>	<u>67,116</u>
Analysis of the balance of cash and cash equivalents :		
	Unaudited At 30 Sep 2005 \$'000	Unaudited At 30 Sep 2004 \$'000
Bank deposits	21,851	64,741
Cash at bank and in hand	2,969	2,375
	<u>24,820</u>	<u>67,116</u>



Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

1. Basis of preparation

We have prepared the interim financial report in accordance with International Accounting Standard 34 "Interim financial reporting" adopted by the International Accounting Standards Board.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the SFC's statutory accounts for that financial year but is derived from those financial statements.

We consolidated the financial results of Investor Compensation Company Limited in the SFC's condensed financial statements made up to 30 September 2005. We eliminated all material intragroup balances and transactions in preparing the condensed consolidated financial statements. We have applied the same accounting policies adopted in the consolidated financial statements for the year ended 31 March 2005 to the interim financial report.

There were no significant changes in the operation of the SFC for the six months ended 30 September 2005.

2. Accumulated surplus

The Group and the SFC

Movements of accumulated surplus during the six months ended 30 September 2005 are as follows :

	<u>Unaudited</u> \$'000
Balance at 31 March 2005	817,245
Surplus	135,513
Balance at 30 September 2005	<u>952,758</u>

3. Held-to-maturity debt securities

As of 30 September 2005, the total market value of held-to-maturity debt securities amounted to \$1,031,744,000 (31 March 2005 : \$837,775,000), which was below the total carrying cost of \$1,040,458,000 (31 March 2005 : \$844,805,000).



Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

4. Non-current liabilities

The Group and the SFC

Non-current liabilities represent deferred lease incentives and provision for premises reinstatement cost. Deferred lease incentives consist of incentives granted by our landlord in connection with the lease of our office premises. We recognise the deferred lease incentives in our income and expenditure account on a straight line basis over the lease period from 2004 to 2013 as an integral part of the lease expense.

5. Ageing analysis of debtors and creditors

There was no material debtor balance and creditor balance included in “debtors, deposits and prepayments” and “creditors and accrued charges” respectively as at 30 September 2005. Therefore we do not provide an ageing analysis of debtors and creditors.

6. Exchange fluctuation

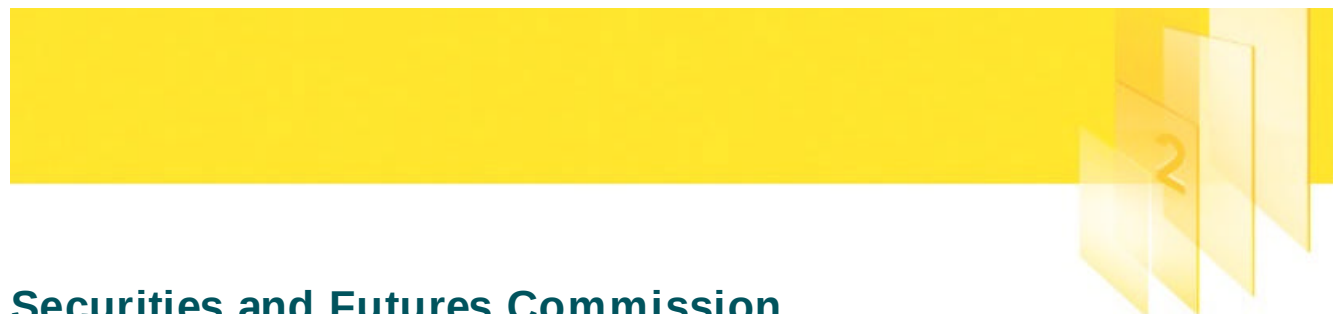
All our balance sheet items are denominated in either United States dollars or Hong Kong dollars, and, as a result, we are not exposed to significant exchange rate risk.

7. Investments in subsidiaries

The SFC formed FinNet Limited (FinNet) on 6 November 2000 with an authorised share capital of \$10,000 and issued share capital of \$2 and Investor Compensation Company Limited (ICC) on 11 September 2002 with an authorised share capital of \$1,000 and issued share capital of \$0.2. Both FinNet and ICC are incorporated in Hong Kong.

The objective of FinNet is to operate an electronic network to facilitate payment and delivery transactions and interconnection of all financial institutions and financial entities in Hong Kong.

The objective of ICC is to facilitate the administration and management of the Investor Compensation Fund established under the Securities and Futures Ordinance.



Securities and Futures Commission

Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

7. Investments in subsidiaries - Cont'd

Both companies are wholly owned subsidiaries of the SFC. As at 30 September 2005, the investment in subsidiaries, which is stated at cost less any impairment losses, amounted to \$2.2. The balance is too small to appear on the balance sheet which is expressed in thousands of dollars.

FinNet has not commenced operations. The balance sheet of FinNet as at 30 September 2005 and the income and expenditure account for the period then ended were immaterial. Therefore, we have not accounted for its result in the condensed consolidated financial statements.

The financial statements of ICC are included in the condensed consolidated financial statements.

8. Related party transactions

We have related party relationships with the Unified Exchange Compensation Fund, the Commodity Exchange Compensation Fund, the Investor Compensation Fund, the Securities Ordinance (Chapter 333) - Dealers' Deposits Fund, the Commodities Trading Ordinance (Chapter 250) - Dealers' Deposits Fund and the Securities Ordinance (Chapter 333) - Securities Margin Financiers' Security Fund. During the period, we received reimbursement from the ICF for all the ICC's expenses, which is in accordance with section 242(1) of the Securities and Futures Ordinance.



Investor Compensation Fund (the Fund)

Report of the Investor Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the six months ended 30 September 2005.

1. ESTABLISHMENT OF THE FUND

Part XII of the Securities and Futures Ordinance (Chapter 571) established the Fund on 1 April 2003.

2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 24 to 28.

3. MEMBERS OF THE COMMITTEE

The members of the Committee during the six months ended 30 September 2005 and up to the date of this report were : -

Mr Martin Wheatley	[appointed on 21 June 2005]
Mr Peter Au-Yang	[appointed on 1 April 2005 and resigned on 20 June 2005]
Mr Eddy Fong, SBS, JP	[appointed on 21 June 2005]
Mr Gerald Greiner	
Mrs Alexa Lam	
Ms Anna HY Wu, SBS, JP	

4. INTERESTS IN CONTRACTS

No contract of significance to which the Fund was a party and in which a Committee member had a material interest, whether directly or indirectly, subsisted at the balance sheet date or at any time during the six months.

On behalf of the Committee

Martin Wheatley
Chairman

7 November 2005



Independent review report to the board of directors of the Securities and Futures Commission (the SFC)

(Established in Hong Kong under the Securities and Futures Ordinance)

Introduction

We have been instructed by the SFC to review the interim financial report for the six months ended 30 September 2005 of the Investor Compensation Fund (the Fund), established under Part XII of the Securities and Futures Ordinance, set out on pages 24 to 28. We have not been instructed to review and have not reviewed the financial information for the three months ended 30 September 2005 included on page 24 of the interim financial report.

Respective responsibilities of directors and auditors

The SFC is responsible for preparing an interim report of the Fund to comply with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board. The interim financial report is the responsibility of SFC, and has been approved by the SFC.

It is our responsibility to form an independent conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Review work performed

We conducted our review in accordance with Statement of Auditing Standards 700 “Engagements to review interim financial reports” issued by the Hong Kong Institute of Certified Public Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

Review conclusion

On the basis of our review, which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six months ended 30 September 2005.

KPMG
Certified Public Accountants
Hong Kong
7 November 2005

Investor Compensation Fund

Income and Expenditure Account

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	Note	Unaudited Three Months Ended		Unaudited Six Months Ended	
		30 Sep 2005	30 Sep 2004	30 Sep 2005	30 Sep 2004
		\$'000	\$'000	\$'000	\$'000
Income					
Net investment income		11,844	11,189	35,505	11,591
Transaction levy from the SEHK		56,899	33,839	97,903	69,731
Contract levy from the HKFE		4,366	3,234	7,925	6,656
		<u>73,109</u>	<u>48,262</u>	<u>141,333</u>	<u>87,978</u>
Expenses					
ICC expenses	2	769	869	1,558	1,828
Auditors' remuneration		15	12	30	18
Bank charges		344	386	772	412
Professional fees		601	478	1,161	483
Exchange difference		1,949	350	4,982	355
Sundry expenses		-	-	1	1
		<u>3,678</u>	<u>2,095</u>	<u>8,504</u>	<u>3,097</u>
Surplus		69,431	46,167	132,829	84,881
Accumulated surplus brought forward		<u>416,877</u>	<u>193,323</u>	<u>353,479</u>	<u>154,609</u>
Accumulated surplus carried forward		<u>486,308</u>	<u>239,490</u>	<u>486,308</u>	<u>239,490</u>

The notes on page 28 form part of the condensed financial statements.

Investor Compensation Fund

Balance Sheet

At 30 September 2005

(Expressed in Hong Kong dollars)

	Unaudited At 30 Sep 2005 \$'000	Audited At 31 Mar 2005 \$'000
Current assets		
Debt securities	1,281,325	1,182,665
Equity securities	132,752	122,409
Other receivable	-	384
Interest receivable	15,087	13,731
Due from ICC	2,371	1,111
Levy receivable from the SEHK	16,119	16,434
Levy receivable from the HKFE	1,375	1,283
Fixed and call deposits with banks	140,258	81,663
Cash at bank	438	37,295
	<u>1,589,725</u>	<u>1,456,975</u>
Current liabilities		
Accounts payable and accrued charges	691	818
Other payable	48	-
	<u>739</u>	<u>818</u>
Net current assets	<u>1,588,986</u>	<u>1,456,157</u>
Net assets	<u>1,588,986</u>	<u>1,456,157</u>
Representing:		
<u>Compensation fund</u>		
Contributions from UECF	994,718	994,718
Contributions from CECF	107,960	107,960
Accumulated surplus	486,308	353,479
	<u>1,588,986</u>	<u>1,456,157</u>

The notes on page 28 form part of the condensed financial statements.

Investor Compensation Fund
Statement of Changes in Equity
For the six months ended 30 September 2005
(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended <u>30 Sep 2005</u> \$'000	Unaudited Six Months Ended <u>30 Sep 2004</u> \$'000
Compensation Fund balance as at 1 April	1,456,157	962,209
Surplus for the period	132,829	84,881
Contributions from UECF	-	249,078
Compensation Fund balance as at 30 September	<u>1,588,986</u>	<u>1,296,168</u>

The notes on page 28 form part of the condensed financial statements.

Investor Compensation Fund

Cash Flow Statement

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended 30 Sep 2005 \$'000	Unaudited Six Months Ended 30 Sep 2004 \$'000
Cash flows from operating activities		
Surplus for the period	132,829	84,881
Net investment income	(35,505)	(11,591)
Exchange difference	4,982	355
Decrease in levies receivable	223	3,623
Increase in accounts receivables	(1,260)	(328)
(Decrease) / Increase in accounts payable and accrued charges	(127)	581
Net cash generated from operating activities	<u>101,142</u>	<u>77,521</u>
Cash flows from investing activities		
Purchase of debt securities	(1,943,070)	(1,567,680)
Purchase of equity securities	-	(99,990)
Sale or maturity of debt securities	1,838,015	653,407
Sale of equity securities	308	-
Interest received	25,343	159
Net cash used in investing activities	<u>(79,404)</u>	<u>(1,014,104)</u>
Cash flows from financing activities		
Contributions received from UECF	-	249,078
Net cash generated from financing activities	<u>-</u>	<u>249,078</u>
Net increase / (decrease) in cash and cash equivalents	21,738	(687,505)
Cash and cash equivalents at beginning of the six months	118,958	766,977
Cash and cash equivalents at end of the six months	<u>140,696</u>	<u>79,472</u>
Analysis of the balance of cash and cash equivalents:		
	Unaudited At 30 Sep 2005 \$'000	Unaudited At 30 Sep 2004 \$'000
Cash at bank	438	8,429
Fixed and call deposits with banks	140,258	71,043
	<u>140,696</u>	<u>79,472</u>



Investor Compensation Fund

Notes to the Condensed Financial Statements

For the six months ended to 30 September 2005

(Expressed in Hong Kong dollars)

1. BASIS OF PREPARATION

The Fund prepares the interim financial report in accordance with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2005 to the interim financial report.

2. ICC EXPENSES

The SFC formed the Investor Compensation Company Limited (ICC) in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the Securities and Futures Ordinance (SFO). The Fund is responsible for funding the establishment and operation of ICC. For the six months ended 30 September 2005, ICC incurred \$1,558,000 for its operation (For the six months ended 30 September 2004 : \$1,828,000).

3. CONTINGENT LIABILITIES

As at the date of this report, the Fund has received claims against three intermediaries. The validity of these claims is under investigation. We have not made any provision for these claims. The maximum contingent liability of the Fund to these claims is \$600,000 (As at 31 March 2005 : \$900,000).



Unified Exchange Compensation Fund (the Fund)

Report of the Securities Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the six months ended 30 September 2005.

1. ESTABLISHMENT OF THE FUND

Part X of the repealed Securities Ordinance (Chapter 333) established the Fund. However, when the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single investor compensation fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. After reserving sufficient money in the Fund to meet claims against it and its other liabilities, the SFC will eventually transfer the remaining balance of the Fund to the ICF.

Part X of the repealed Securities Ordinance remains effective in respect of the operation of the Fund to the extent described in Section 74 of Schedule 10 of the SFO.

2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 31 to 36.

3. MEMBERS OF THE COMMITTEE

The members of the Committee during the six months ended 30 September 2005 and up to the date of this report were : -

Mr Martin Wheatley	[appointed on 21 June 2005]
Mr Peter Au-Yang	[appointed on 1 April 2005 and resigned on 20 June 2005]
Mr Eddy C Fong, SBS, JP	[appointed on 1 April 2005]
Mr Gerald Greiner	[appointed on 1 April 2005]
Mrs Alexa Lam	
Mr David M Roberts	

4. INTERESTS IN CONTRACTS

No contract of significance to which the Fund was a party and in which a Committee member had a material interest, whether directly or indirectly, subsisted at the balance sheet date or at any time during the six months.

On behalf of the Committee

Martin Wheatley
Chairman

31 October 2005



Independent review report to the board of directors of the Securities and Futures Commission (the SFC)

(Established in Hong Kong under the Securities and Futures Ordinance)

Introduction

We have been instructed by the SFC to review the interim financial report for the six months ended 30 September 2005 of the Unified Exchange Compensation Fund (the Fund) set out on pages 31 to 36. We have not been instructed to review and have not reviewed the financial information for the three months ended 30 September 2005 included on page 31 of the interim financial report.

Respective responsibilities of directors and auditors

The SFC is responsible for preparing an interim report of the Fund to comply with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board. The interim financial report is the responsibility of the SFC and has been approved by the Securities Compensation Fund Committee on behalf of the SFC.

It is our responsibility to form an independent conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Review work performed

We conducted our review in accordance with Statement of Auditing Standards 700 “Engagements to review interim financial reports” issued by the Hong Kong Institute of Certified Public Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

Review conclusion

On the basis of our review, which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six months ended 30 September 2005.

KPMG
Certified Public Accountants
Hong Kong
31 October 2005

Unified Exchange Compensation Fund

Income and Expenditure Account

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	<u>Note</u>	Unaudited Three Months Ended		Unaudited Six Months Ended	
		<u>30 Sep 2005</u>	<u>30 Sep 2004</u>	<u>30 Sep 2005</u>	<u>30 Sep 2004</u>
		\$'000	\$'000	\$'000	\$'000
Income					
Net investment income		412	1,744	704	766
Recoveries	2	726	738	890	10,771
Replenishments from the SEHK	3	-	-	1	-
		<u>1,138</u>	<u>2,482</u>	<u>1,595</u>	<u>11,537</u>
Expenses					
Provision for compensation made / (reversed)		(861)	(2,608)	15	(3,531)
Auditors' remuneration		9	9	19	18
Bank charges		-	13	-	29
Professional fees		10	10	10	23
Sundry expenses		-	-	1	1
		<u>(842)</u>	<u>(2,576)</u>	<u>45</u>	<u>(3,460)</u>
Surplus		1,980	5,058	1,550	14,997
Accumulated surplus / (deficit) brought forward		<u>7,025</u>	<u>(3,345)</u>	<u>7,455</u>	<u>(13,284)</u>
Accumulated surplus carried forward		<u>9,005</u>	<u>1,713</u>	<u>9,005</u>	<u>1,713</u>

The notes on pages 35 to 36 form part of the condensed financial statements.

Unified Exchange Compensation Fund

Balance Sheet

At 30 September 2005

(Expressed in Hong Kong dollars)

	<u>Note</u>	<u>Unaudited</u> <u>At 30 Sep 2005</u> \$'000	<u>Audited</u> <u>At 31 Mar 2005</u> \$'000
Current assets			
Equity securities received under subrogation	2	694	7,793
Interest receivable		55	36
Fixed and call deposits with banks		54,890	47,028
Cash at bank		82	52
		<u>55,721</u>	<u>54,909</u>
Current liabilities			
Accounts payable and accrued charges		4,327	4,291
Provision for compensation	4	718	1,492
		<u>5,045</u>	<u>5,783</u>
Net current assets		<u>50,676</u>	<u>49,126</u>
Net assets		<u>50,676</u>	<u>49,126</u>
Representing:			
<u>Compensation fund</u>			
Contributions from the SEHK		46,100	46,100
Excess transaction levy from the SEHK		353,787	353,787
Special contribution		3,500	3,500
Additional contribution from the SEHK		300,000	300,000
Additional contribution from the SFC		330,000	330,000
Special levy surplus		3,002	3,002
Accumulated surplus		9,005	7,455
		<u>1,045,394</u>	<u>1,043,844</u>
Contributions to Investor Compensation Fund		<u>(994,718)</u>	<u>(994,718)</u>
		<u>50,676</u>	<u>49,126</u>

The notes on pages 35 to 36 form part of the condensed financial statements.

Unified Exchange Compensation Fund
Statement of Changes in Equity
For the six months ended 30 September 2005
(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended <u>30 Sep 2005</u> \$'000	Unaudited Six Months Ended <u>30 Sep 2004</u> \$'000
Compensation Fund balance as at 1 April	49,126	323,815
Surplus for the period	1,550	14,997
Contributions refunded to the SEHK	-	(250)
Contributions to Investor Compensation Fund	-	(249,078)
Compensation Fund balance as at 30 September	<u>50,676</u>	<u>89,484</u>

The notes on pages 35 to 36 form part of the condensed financial statements.

Unified Exchange Compensation Fund
Cash Flow Statement
For the six months ended 30 September 2005
(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended <u>30 Sep 2005</u> \$'000	Unaudited Six Months Ended <u>30 Sep 2004</u> \$'000
Cash flows from operating activities		
Surplus for the period	1,550	14,997
Net investment income	(704)	(766)
Decrease in equity securities received under subrogation	7,099	394
Decrease in provision for compensation	(774)	(5,592)
Increase / (decrease) in accounts payable and accrued charges	36	(265)
Net cash generated from operating activities	<u>7,207</u>	<u>8,768</u>
Cash flows from investing activities		
Debt securities redeemed	-	90,500
Debt securities sold	-	67,763
Interest received	685	5,499
Net cash generated from investing activities	<u>685</u>	<u>163,762</u>
Cash flows from financing activities		
Contributions refunded to the SEHK	-	(250)
Contributions to Investor Compensation Fund	-	(249,078)
Net cash used in financing activities	<u>-</u>	<u>(249,328)</u>
Net increase / (decrease) in cash and cash equivalents	7,892	(76,798)
Cash and cash equivalents at beginning of the six months	47,080	167,622
Cash and cash equivalents at end of the six months	<u>54,972</u>	<u>90,824</u>
Analysis of the balance of cash and cash equivalents:		
	Unaudited <u>At 30 Sep 2005</u> \$'000	Unaudited <u>At 30 Sep 2004</u> \$'000
Cash at bank	82	503
Fixed and call deposits with banks	<u>54,890</u>	<u>90,321</u>
	<u>54,972</u>	<u>90,824</u>

Unified Exchange Compensation Fund
Notes to the Condensed Financial Statements
For the six months ended 30 September 2005
(Expressed in Hong Kong dollars)

1. BASIS OF PREPARATION

The Fund prepares the interim financial report in accordance with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board. As the Fund will eventually cease operation as a result of the Securities and Futures Ordinance (SFO) which came into effect from 1 April 2003, the Fund prepares the interim financial report on a break-up basis with assets stated at recoverable amounts.

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2005 included in this report does not constitute the Fund’s statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2005 to the interim financial report.

2. EQUITY SECURITIES AND RECOVERIES

In relation to the share distribution from C.A. Pacific Securities Ltd. and C.A. Pacific Finance Ltd., the liquidators had advised the Securities and Futures Commission (SFC) that shares were allocated to the Fund under its subrogation rights, subject to paying a processing fee to the liquidators. The Fund recognised as recoveries the sale proceeds and the remaining shares at market value as of 30 September 2005 after deducting relevant processing fees and charges for collecting and selling the securities received.

3. REPLENISHMENTS FROM THE SEHK

Under Section 107 of the repealed Securities Ordinance, the SFC may require the SEHK to replenish the Fund with an amount that is equal to that paid in connection with the satisfaction of the claim (limited to \$8,000,000 per each defaulted case) after the SFC has exhausted all relevant rights of action and other legal remedies against the defaulter. During the period, the Fund received replenishments of \$883 from the SEHK in respect of one defaulted case.

Unified Exchange Compensation Fund
Notes to the Condensed Financial Statements
For the six months ended 30 September 2005
(Expressed in Hong Kong dollars)

4. PROVISION FOR COMPENSATION

	Unaudited \$'000
Balance as at 1 April 2004	9,545
Less: amount paid during the year ended 31 March 2005	(2,851)
Less: unused provision reversed during the year ended 31 March 2005	<u>(5,202)</u>
Balance as at 31 March 2005	1,492
Less: amount paid during the six months ended 30 September 2005	(789)
Add: provision made during the six months ended 30 September 2005	<u>15</u>
Balance as at 30 September 2005	<u><u>718</u></u>

We made provision for claims in respect of three SEHK exchange participants for which the SEHK has published a notice calling for claims. The maximum liabilities of the Fund in respect of these three default cases can exceed the normal \$8 million limit.

5. CONTINGENT LIABILITIES

As at the date of this report, the SEHK has received claims against seven exchange participants. They are subject to the normal \$8 million ceiling pursuant to Section 109 of the repealed Securities Ordinance. The validity of these claims is under investigation. We have not made any provision for these claims. The maximum contingent liability of the Fund to these claims is \$56 million (As at 31 March 2005 : \$56 million).



Commodity Exchange Compensation Fund (the Fund)

Report of the Futures Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the six months ended 30 September 2005.

1. ESTABLISHMENT OF THE FUND

Part VIII of the repealed Commodities Trading Ordinance (Chapter 250) established the Fund. However, when the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single investor compensation fund (ICF) was formed to ultimately replace the Fund and the Unified Exchange Compensation Fund. After reserving sufficient money in the Fund to meet claims against it and its other liabilities, the SFC will eventually transfer the remaining balance of the Fund to the ICF.

Part VIII of the repealed Commodities Trading Ordinance remains effective in respect of the operation of the Fund to the extent described in Section 75 of Schedule 10 of the SFO.

2. FINANCIAL RESULTS

The Committee presents the financial results which are set out in the condensed financial statements on pages 39 to 43.

3. MEMBERS OF THE COMMITTEE

The members of the Committee during the six months ended 30 September 2005 and up to the date of this report were :-

Mr Martin Wheatley	[appointed on 21 June 2005]
Mr Peter Au-Yang	[appointed on 1 April 2005 and resigned on 20 June 2005]
Mr Eddy C Fong, SBS, JP	[appointed on 1 April 2005]
Mr Gerald Greiner	
Mrs Alexa Lam	
Mr Calvin Tai	

4. INTERESTS IN CONTRACTS

No contract of significance to which the Fund was a party and in which a Committee member had a material interest, whether directly or indirectly, subsisted at the balance sheet date or at any time during the six months.

On behalf of the Committee

Martin Wheatley
Chairman

31 October 2005



Independent review report to the board of directors of the Securities and Futures Commission (the SFC)

(Established in Hong Kong under the Securities and Futures Ordinance)

Introduction

We have been instructed by the SFC to review the interim financial report for the six months ended 30 September 2005 of the Commodity Exchange Compensation Fund (the Fund) set out on pages 39 to 43. We have not been instructed to review and have not reviewed the financial information for the three months ended 30 September 2005 included on page 39 of the interim financial report.

Respective responsibilities of directors and auditors

The SFC is responsible for preparing an interim report of the Fund to comply with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board. The interim financial report is the responsibility of SFC, and has been approved by the Futures Compensation Fund Committee on behalf of the SFC.

It is our responsibility to form an independent conclusion, based on our review, on the interim financial report and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Review work performed

We conducted our review in accordance with Statement of Auditing Standards 700 “Engagements to review interim financial reports” issued by the Hong Kong Institute of Certified Public Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial report and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial report.

Review conclusion

On the basis of our review, which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial report for the six months ended 30 September 2005.

KPMG
Certified Public Accountants
Hong Kong
31 October 2005

Commodity Exchange Compensation Fund

Income and Expenditure Account

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	Unaudited Three Months Ended		Unaudited Six Months Ended	
	<u>30 Sep 2005</u>	<u>30 Sep 2004</u>	<u>30 Sep 2005</u>	<u>30 Sep 2004</u>
	\$'000	\$'000	\$'000	\$'000
Income				
Net investment income	4	-	6	-
	-----	-----	-----	-----
Expenses				
Auditors' remuneration	7	9	13	18
Professional fees	9	9	9	9
Sundry expenses	-	-	1	1
	-----	-----	-----	-----
	16	18	23	28
	=====	=====	=====	=====
Deficit	(12)	(18)	(17)	(28)
Accumulated surplus brought forward	108,223	108,252	108,228	108,262
	-----	-----	-----	-----
Accumulated surplus carried forward	108,211	108,234	108,211	108,234
	=====	=====	=====	=====

The note on page 43 forms part of the condensed financial statements.

Commodity Exchange Compensation Fund

Balance Sheet

At 30 September 2005

(Expressed in Hong Kong dollars)

	Unaudited At 30 Sep 2005 \$'000	Audited At 31 Mar 2005 \$'000
Current assets		
Interest receivable	1	-
Fixed and call deposits with banks	461	488
Cash at bank	1	4
	<u>463</u>	<u>492</u>
Current liabilities		
Accounts payable and accrued charges	212	224
	<u>251</u>	<u>268</u>
Net current assets	<u>251</u>	<u>268</u>
Net assets	<u>251</u>	<u>268</u>
Representing:		
<u>Compensation fund</u>		
Accumulated surplus	108,211	108,228
Contributions to Investor Compensation Fund	(107,960)	(107,960)
	<u>251</u>	<u>268</u>

The note on page 43 forms part of the condensed financial statements.

Commodity Exchange Compensation Fund
Statement of Changes in Equity
For the six months ended 30 September 2005
(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended <u>30 Sep 2005</u> \$'000	Unaudited Six Months Ended <u>30 Sep 2004</u> \$'000
Compensation Fund balance as at 1 April	268	302
Deficit for the period	(17)	(28)
Compensation Fund balance as at 30 September	<u>251</u>	<u>274</u>

The note on page 43 forms part of the condensed financial statements.

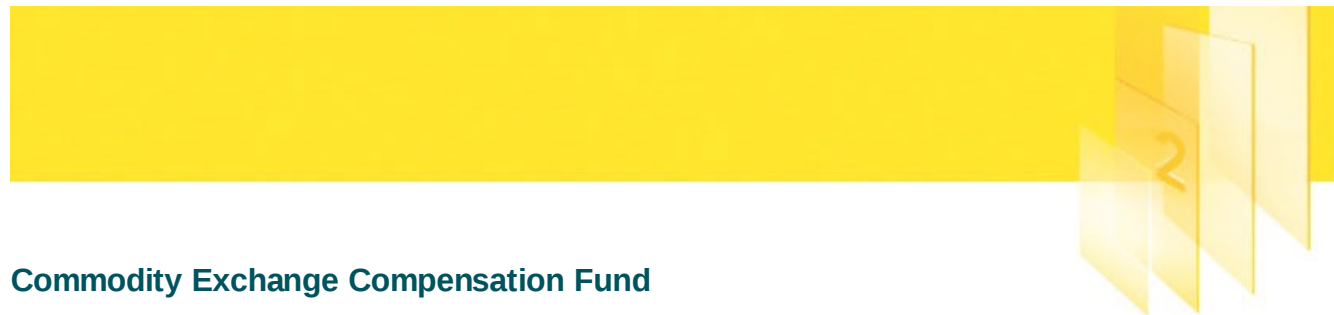
Commodity Exchange Compensation Fund

Cash Flow Statement

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

	Unaudited Six Months Ended 30 Sep 2005 \$'000	Unaudited Six Months Ended 30 Sep 2004 \$'000
Cash flows from operating activities		
Deficit for the period	(17)	(28)
Net investment income	(6)	-
Decrease in accounts payable and accrued charges	(12)	(10)
Net cash used in operating activities	<u>(35)</u>	<u>(38)</u>
Cash flows from investing activities		
Interest received	5	-
Net cash generated from investing activities	<u>5</u>	<u>-</u>
Net decrease in cash and cash equivalents	(30)	(38)
Cash and cash equivalents at beginning of the six months	492	529
Cash and cash equivalents at end of the six months	<u>462</u>	<u>491</u>
Analysis of the balance of cash and cash equivalents:		
	Unaudited At 30 Sep 2005 \$'000	Unaudited At 30 Sep 2004 \$'000
Cash at bank	1	4
Fixed and call deposits with banks	461	487
	<u>462</u>	<u>491</u>



Commodity Exchange Compensation Fund

Notes to the Condensed Financial Statements

For the six months ended 30 September 2005

(Expressed in Hong Kong dollars)

1. BASIS OF PREPARATION

The Fund prepares the interim financial report in accordance with International Accounting Standard 34 “Interim financial reporting” adopted by the International Accounting Standards Board. As the Fund will eventually cease operation as a result of the Securities and Futures Ordinance (SFO) which came into effect from 1 April 2003, the Fund prepares the interim financial report on a break-up basis with assets stated at recoverable amounts.

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