

Commodity Exchange Compensation Fund Financial Statements

Report of the Futures Compensation Fund Committee

The members of the Committee present their annual report and the audited financial statements for the year ended 31 March 2000.

1. Establishment of the Commodity Exchange Compensation Fund (the Fund)

The Fund was established for the purpose set out in Part VIII of the Commodities Trading Ordinance (Chapter 250).

2. Financial Results

The financial results are set out in the financial statements presented on pages 83 to 89.

3. Members of the Committee

The members of the Committee during the year and up to the date of this report were:

Mr Mark Dickens	(appointed on 1 April 1999)
Mr Andrew Procter	
Mr Roderick Chalmers	
Mr William Grossman	(appointed on 17 September 1999)
Mr Robert B Gilmore	(resigned on 16 September 1999)
Mr Mark Ho	

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 year.

5. Auditors

The retiring auditors, Messrs KPMG, being eligible, offer themselves for re-appointment.

On behalf of the Committee

Mark Dickens
Chairman

10 May 2000

Auditors' Report to the Securities and Futures Commission (SFC)

We have audited the financial statements of the Commodity Exchange Compensation Fund (the Fund) established under Section 77 of the Hong Kong Commodities Trading Ordinance set out on pages 83 to 89 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

Respective Responsibilities of the SFC and Auditors

The Hong Kong Commodities Trading Ordinance requires the SFC to keep proper accounts of the Fund and to prepare an income and expenditure account and a balance sheet (the financial statements) of the Fund in respect of each financial year. The directors of the SFC do so on the basis that these financial statements should give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgments and accounting estimates are made which are prudent and reasonable and that the reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

Basis of Opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the SFC in the preparation of the financial statements and of whether the accounting policies are appropriate to the Fund's circumstances, have been consistently applied and are adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Fund at 31 March 2000 and of its surplus for the year then ended, and have been properly prepared in accordance with accounting principles generally accepted in Hong Kong.

KPMG
Certified Public Accountants
Hong Kong

10 May 2000

Income and Expenditure Account

For the year ended 31 March 2000 (Expressed in HK dollars)

	Note	2000	1999
Income			
Interest and investment income	4	\$ 6,336,225	\$ 5,522,711
Profit on disposal of held-to-maturity debt securities		238,998	32,998
		<u>\$ 6,575,223</u>	<u>\$ 5,555,709</u>
Expenditure			
Auditors' remuneration		\$ 38,900	\$ 37,000
Premium on investments amortized	4	271,175	132,630
Bank charges		68,463	51,491
Legal and professional fees		12,000	14,000
Sundry expenses		500	500
		<u>\$ 391,038</u>	<u>\$ 235,621</u>
Surplus of Income Over Expenditure Before Appropriations		\$ 6,184,185	\$ 5,320,088
Balance Brought Forward		-	-
Appropriations			
Transfer to Compensation Fund Account pursuant to S83(2)(a) of the Commodities Trading Ordinance (Chapter 250)	8	6,184,185	5,320,088
Balance Carried Forward		\$ -	\$ -

The notes on pages 86 to 89 form an integral part of the financial statements.

Balance Sheet

At 31 March 2000 (Expressed in HK dollars)

	Note	2000	1999
Non current held-to-maturity debt securities	4&5	\$ 64,576,698	\$ 44,204,727
Current Assets			
Current held-to-maturity debt securities	4&5	\$ 13,520,790	\$ 22,013,088
Interest receivable		939,258	859,802
Levy receivable		456,126	707,040
Bank fixed and call deposits		12,276,054	11,326,824
Cash at bank		14,374	26,239
		<u>\$ 27,206,602</u>	<u>\$ 34,932,993</u>
Current Liabilities			
Accounts payable and accrued charges		248,655	244,379
Net Current Assets		<u>\$ 26,957,947</u>	<u>\$ 34,688,614</u>
Net Assets		<u>\$ 91,534,645</u>	<u>\$ 78,893,341</u>
Representing:			
Compensation Fund			
Contributions from HKFE	6	\$ 21,800,000	\$ 21,100,000
Contract levy	4&7	52,369,338	46,682,950
Income and expenditure account	8	28,998,946	22,814,761
		<u>\$ 103,168,284</u>	<u>\$ 90,597,711</u>
Deduct: Compensation paid	9	(24,457,172)	(24,457,172)
Add: Recovery under subrogation	4&10	12,823,533	12,752,802
		<u>\$ 91,534,645</u>	<u>\$ 78,893,341</u>

Approved by the Futures Compensation Fund Committee on behalf of the Securities and Futures Commission on 10 May 2000 and signed on its behalf by

Mark Dickens
Chairman

Roderick Chalmers
Committee Member

William Grossman
Committee Member

The notes on pages 86 to 89 form an integral part of the financial statements.

Statement of Recognized Gains and Losses

For the year ended 31 March 2000 (Expressed in HK dollars)

	Note	2000	1999
Net contributions from HKFE	6	\$ 700,000	\$ 100,000
Contract levy from HKFE	4	5,686,388	8,429,708
Recovery under subrogation	10	70,731	1,165,510
Compensation paid	9	–	(3,993,427)
Net gains not recognized in the income statement		\$ 6,457,119	\$ 5,701,791
Net surplus for the year		6,184,185	5,320,088
Total recognized gains		\$ 12,641,304	\$ 11,021,879

The notes on pages 86 to 89 form an integral part of the financial statements.

Notes to the Financial Statements

For the year ended 31 March 2000 (Expressed in HK dollars)

1. Status Change of the HKFE Shareholders

As a result of a scheme of arrangements, on 6 March 2000 the Hong Kong Futures Exchange Limited (the HKFE) became a wholly owned subsidiary of the Hong Kong Exchanges and Clearing Limited (HKEx), and the ownership of shares in the HKFE was separated from access to its trading facilities. The existing shareholders of the HKFE ceased to be shareholders of the HKFE and became exchange participants and/or holders of a trading right. To become an exchange participant of the HKFE, a person must first become a holder of a trading right.

Pursuant to the Exchanges and Clearing Houses (Merger) Ordinance which came into effect on 6 March 2000 -

“exchange participant” means a person who, in accordance with the rules of the Exchange Company, may trade on or through the Exchange Company; and whose name is entered in a list, register or roll kept by the Exchange Company as a person who may trade on or through the Exchange Company; and “trading right” means a right to be eligible to trade on or through the Exchange Company and entered as such a right in a list, register or roll kept by the Exchange Company.

2. Money Constituting the Fund

The Fund is derived principally from monies paid to the Securities and Futures Commission (SFC) by the HKFE by way of deposits in respect of its holders of trading rights, by way of a contract levy chargeable on contracts traded on the HKFE, from the return or profit on the investment of surplus funds and from monies recovered by or on behalf of the SFC by the exercise of any right of action conferred by Part VIII of the Hong Kong Commodities Trading Ordinance (Chapter 250) (CTO).

3. Purpose, Limitation and Principal Activity

The purpose of the Fund is to meet claims, as determined and allowed by the HKFE, for pecuniary losses suffered by persons as a result of defaults on the part of exchange participants of the HKFE.

The total amount of compensation that may be paid to claimants consequent upon the default of any one exchange participant is normally limited to \$2,000,000 pursuant to Section 87(3) of the CTO. If the aggregate of allowed claims in respect of an exchange participant exceeds the \$2,000,000 limit, that amount shall be apportioned among claimants as determined to be equitable by the HKFE.

Should defaults at any given time on the part of exchange participants of the HKFE give rise to allowed and/or apportioned claims exceeding the net assets of the Fund, compensation payments to claimants would be apportioned in accordance with Section 97(1) of the CTO, the unpaid amount of such allowed and/or apportioned claims being charged against further receipts by the Fund and paid out as and when money is available.

Notes to the Financial Statements (cont'd)

For the year ended 31 March 2000 (Expressed in HK dollars)

4. Accounting Policies

a *Statement of compliance*

These financial statements have been prepared in accordance with all applicable Statements of Standard Accounting Practice and Interpretations issued by the Hong Kong Society of Accountants and accounting principles generally accepted in Hong Kong. The significant accounting policies adopted by the Fund are set out below.

b *Basis of preparation of financial statements*

These financial statements have been prepared on the historical cost basis.

c

- (i) Interest income and contract levies are recognized in the financial statements on an accruals basis. The contract levy is taken directly to the Fund.
- (ii) Premium or discount on the purchase of held-to-maturity debt securities is amortized or accreted respectively to the income and expenditure account on a straight line basis over the holding periods to redemption.
- (iii) Profits or losses on disposal of investments in held-to-maturity debt securities are accounted for in the income and expenditure account as they arise.
- (iv) Investments, representing held-to-maturity debt securities, are stated at cost adjusted for the amortization of premiums and accretion of discounts on purchase over the holding periods to redemption, and less provisions for impairment. The carrying amounts of held-to-maturity debt securities are reviewed as at the balance sheet date in order to assess whether the carrying amounts are expected to be recovered. Provisions are made for the parts of carrying amounts which are not expected to be recovered and are recognized as an expense in the income and expenditure account. Provisions against the carrying value of the held-to-maturity debt securities are written back to income when the circumstances and events that lead to the write-down cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.
- (v) Recovery of any payment out of the Fund in respect of any claim under subrogation pursuant to Section 95 of the CTO is recognized in the financial statements on a cash basis and taken directly to the Fund.
- (vi) Provision for compensation is made for known liabilities arising from claims for pecuniary losses suffered by persons as a result of defaults on the part of the exchange participants of the HKFE which are determined up to the date on which the financial statements are approved by the Committee. Such provisions are transferred directly from the Fund.
- (vii) The Fund is exempt from taxation pursuant to Section 87 of the Hong Kong Inland Revenue Ordinance, Chapter 112.
- (viii) For the purposes of these financial statements, parties are considered to be related to the Fund if the Committee has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Fund and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

Notes to the Financial Statements (cont'd)

For the year ended 31 March 2000 (Expressed in HK dollars)

5. Held-to-Maturity Debt Securities

		2000	1999
Maturing after one year	- listed in Hong Kong	\$ 3,966,988	\$ 4,941,852
	- listed outside Hong Kong	15,017,647	-
	- unlisted	45,592,063	39,262,875
		<u>\$ 64,576,698</u>	<u>\$ 44,204,727</u>
Maturing within one year	- listed in Hong Kong	\$ -	\$ 1,004,640
	- unlisted	13,520,790	21,008,448
		<u>\$ 13,520,790</u>	<u>\$ 22,013,088</u>
		<u>\$ 78,097,488</u>	<u>\$ 66,217,815</u>
Market value at 31 March	- listed in Hong Kong	\$ 3,984,400	\$ 5,942,100
	- listed outside Hong Kong	15,027,000	-
	- unlisted	59,283,650	60,628,400
		<u>\$ 78,295,050</u>	<u>\$ 66,570,500</u>

During the year, held-to-maturity debt securities, with an amortized cost of \$48,044,540, and which were within a few months of maturity, were sold to purchase debt securities with longer maturities. In addition, held-to-maturity debt securities, with an amortized cost of \$2,998,962, were disposed of because of deterioration in the credit rating of the issuer. The aggregate profit on the disposal amounted to \$238,998.

6. Contributions from HKFE

		2000	1999
Balance brought forward		\$ 21,100,000	\$ 21,000,000
Add: Contributions received during the year		1,200,000	900,000
Deduct : Refunds to outgoing shareholders		(500,000)	(800,000)
Balance carried forward		<u>\$ 21,800,000</u>	<u>\$ 21,100,000</u>

Notes to the Financial Statements (cont'd)

For the year ended 31 March 2000 (Expressed in HK dollars)

7. Contract Levy

	2000	1999
Balance brought forward	\$ 46,682,950	\$ 38,253,242
Add: Contract levy received during the year	5,686,388	8,429,708
Balance carried forward	<u>\$ 52,369,338</u>	<u>\$ 46,682,950</u>

8. Movement in Income & Expenditure Account

	2000	1999
Balance brought forward	\$ 22,814,761	\$ 17,494,673
Transfer of surplus for the year	6,184,185	5,320,088
Balance carried forward	<u>\$ 28,998,946</u>	<u>\$ 22,814,761</u>

9. Compensation Paid

	2000	1999
Balance brought forward	\$ 24,457,172	\$ 20,463,745
Add: Compensation paid	-	3,993,427
Balance carried forward	<u>\$ 24,457,172</u>	<u>\$ 24,457,172</u>

10. Recovery Under Subrogation

	2000	1999
Balance brought forward	\$ 12,752,802	\$ 11,587,292
Add: Amount recovered during the year	70,731	1,165,510
Balance carried forward	<u>\$ 12,823,533</u>	<u>\$ 12,752,802</u>

Under Section 95 of the CTO, the SFC is entitled to receive in place of the claimants, all claims, remedies and distributions of surplus assets on liquidation of the exchange participants in relation to the loss sustained by the claimants, to the extent of the payment made by the SFC out of the Fund. The SFC has passed all amounts so received back to the Fund.