

# Securities and Futures Commission Financial Statements

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

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

We have audited the financial statements on pages 59 to 68 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

### **Respective Responsibilities of Directors and Auditors**

The Hong Kong Securities and Futures Commission Ordinance (the Ordinance) requires the SFC to prepare financial statements and 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 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 SFC'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 misstatements. 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 the SFC's financial affairs at 31 March 2000 and of its surplus and cash flows 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

15 May 2000

## Income and Expenditure Account

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

|   | Note  | 2000<br>\$'000 | 1999<br>\$'000 |
|---|-------|----------------|----------------|
| <b>Income</b>                           |       |                |                |
| Levies                                  | 2 (a) | 243,960        | 134,014        |
| Fees and charges                        | 2 (c) | 136,258        | 92,308         |
| Investment income                       |       | 62,351         | 68,811         |
| Others                                  |       | 2,531          | 5,502          |
|   |       | <b>445,100</b> | <b>300,635</b> |
| <b>Expenditure</b>                      |       |                |                |
| Staff costs                             | 5     | 275,205        | 248,455        |
| Premises                                |       |                |                |
| - rental charges under operating leases |       | 35,550         | 38,864         |
| - other                                 |       | 9,905          | 7,961          |
| Other expenses                          | 6     | 64,794         | 65,121         |
|   |       | <b>385,454</b> | <b>360,401</b> |
| Depreciation                            |       | 17,657         | 12,325         |
|   |       | <b>403,111</b> | <b>372,726</b> |
| Surplus / (Deficit) for the Year        |       | 41,989         | (72,091)       |
| Accumulated Surplus Brought Forward     |       | 699,970        | 922,061        |
|   |       | 741,959        | 849,970        |
| Contribution to Compensation Fund       | 14    | (150,000)      | (150,000)      |
| Accumulated Surplus Carried Forward     |       | 591,959        | 699,970        |

No separate statement of recognized gains or losses has been prepared as the surplus for the year would be the only component of this statement.

The notes on pages 62 to 68 form part of these financial statements.

## Balance Sheet

As at 31 March 2000 (Expressed in HK dollars)

|   | Note | 2000<br>\$'000 | 1999<br>\$'000 |
|---|------|----------------|----------------|
| <b>Non-Current Assets</b>                       |      |                |                |
| Fixed assets                                    | 7    | 27,233         | 20,864         |
| Non current held-to-maturity debt securities    | 8    | 477,289        | 511,422        |
| <b>Current Assets</b>                           |      |                |                |
| Current held-to-maturity debt securities        | 8    | 217,873        | 276,431        |
| Bank deposits                                   |      | 154,747        | 133,875        |
| Debtors, deposits and prepayments               | 9    | 43,191         | 23,088         |
| Cash at bank and in hand                        |      | 692            | 464            |
|   |      | <b>416,503</b> | <b>433,858</b> |
| <b>Current Liabilities</b>                      |      |                |                |
| Provision for contribution to compensation fund | 14   | 200,000        | 150,000        |
| Deferred income                                 | 3    | 27,521         | 27,356         |
| Creditors and accrued charges                   |      | 58,705         | 45,978         |
|   |      | <b>286,226</b> | <b>223,334</b> |
| <b>Net Current Assets</b>                       |      | <b>130,277</b> | <b>210,524</b> |
| <b>Net Assets</b>                               |      | <b>634,799</b> | <b>742,810</b> |
| <b>Funding and Reserves</b>                     |      |                |                |
| Initial Funding by Government                   | 10   | 42,840         | 42,840         |
| Income and Expenditure Account                  |      | 591,959        | 699,970        |
|   |      | <b>634,799</b> | <b>742,810</b> |

Approved by the Commission on 15 May 2000 and signed on its behalf by

Andrew L T Sheng  
Chairman

T Brian Stevenson  
Non-Executive Director

The notes on pages 62 to 68 form part of these financial statements.

## Cash Flow Statement

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

|   | Note | 2000<br>\$'000 | 1999<br>\$'000 |
|---|------|----------------|----------------|
| Net cash outflow from operating activities  | a    | (9,102)        | (115,404)      |
| Returns on investments and servicing of finance   |      |                |                |
| Interest received   |      | 61,045         | 70,653         |
| Payment to the Unified Exchange Compensation Fund   |      | (100,000)      | –              |
| Investing activities  |      |                |                |
| Payments to acquire held-to-maturity debt securities  |      | (586,662)      | (106,629)      |
| Receipts from redemption of held-to-maturity debt securities  |      | 107,000        | 168,500        |
| Receipts from disposal of held-to-maturity debt securities  |      | 573,004        | 81,273         |
| Payments to acquire fixed assets  |      | (24,213)       | (17,808)       |
| Receipts from disposal of fixed assets  |      | 28             | 79             |
| Net cash inflow from investing activities   |      | 69,157         | 125,415        |
| Increase in cash and cash equivalents   |      | 21,100         | 80,664         |
| Cash and cash equivalents at beginning of the year  |      | 134,339        | 53,675         |
| Cash and cash equivalents at end of the year  | b    | 155,439        | 134,339        |
| (a) Reconciliation of surplus / (deficit) of income over expenditure to net cash outflow from operating activities: |      |                |                |
|   |      | 2000<br>\$'000 | 1999<br>\$'000 |
| Surplus / (deficit) of income over expenditure for the year   |      | 41,989         | (72,091)       |
| Interest income   |      | (61,700)       | (69,519)       |
| Premium on investments  |      | 1,841          | 1,427          |
| Discount on investments   |      | (634)          | (854)          |
| Depreciation charges  |      | 17,657         | 12,325         |
| Loss / (profit) on disposal of fixed assets   |      | 159            | (71)           |
| (Gain) / loss on disposal of held-to-maturity debt securities   |      | (1,826)        | 135            |
| Gain on redemption of held-to-maturity debt securities  |      | (32)           | –              |
| (Increase) / decrease in debtors, deposits and prepayments  |      | (19,448)       | 10,757         |
| Increase in creditors and accrued charges   |      | 12,727         | 1,097          |
| Increase in deferred income   |      | 165            | 1,390          |
| Net cash outflow from operating activities  |      | (9,102)        | (115,404)      |
| (b) Analysis of the balance of cash and cash equivalents as shown in the balance sheet:                             |      |                |                |
|   |      | 2000<br>\$'000 | 1999<br>\$'000 |
| Bank deposits   |      | 154,747        | 133,875        |
| Cash at bank and in hand  |      | 692            | 464            |
|   |      | 155,439        | 134,339        |

## Notes to the Financial Statements

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

### 1. Status and Principal Activities of the Securities and Futures Commission (SFC)

The SFC was established under and is governed by the Hong Kong Securities and Futures Commission Ordinance (the Ordinance).

### 2. Income

Details of the funding of the SFC are set out in Sections 52 to 54 of the Ordinance. In particular,

- a The SFC receives a share of the levies collected by The Stock Exchange of Hong Kong Limited and Hong Kong Futures Exchange Limited on transactions recorded on the Exchanges at rates specified by the Chief Executive in Council.
- b In each financial year, the SFC shall be paid out of general revenue such moneys as shall be appropriated by the Legislative Council. At the request of the SFC, no appropriation has been made since the financial year ended 31 March 1994.
- c Subsidiary legislation provides for the payment to the SFC of fees or other charges in relation to the functions and services performed by the SFC.

### 3. Significant 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. A summary of the significant accounting policies adopted by the SFC are set out below.

#### b *Basis of preparation of the financial statements*

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

#### c *Recognition of income*

##### (i) Levies

Levies from the two Exchanges are credited to the income and expenditure account on an accruals basis.

##### (ii) Fees and charges

Annual fees from registered persons and in respect of authorized investment arrangements are credited to the income and expenditure account on a straight line basis over the periods to which they relate. Other fees and charges are credited to the income and expenditure account when receivable.

##### (iii) Investment income

Investment income is credited to the income and expenditure account on an accruals basis. It comprises interest earned on bank deposits and held-to-maturity debt securities and the premium or discount on purchase of held-to-maturity debt securities amortized or accreted on a straight line basis over the periods to redemption.

#### d *Operating leases*

Rental payable under operating leases is accounted for on a straight line basis over the period to the next rent review date.

## Notes to the Financial Statements (cont'd)

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

### 3. Significant Accounting Policies (cont'd)

#### e Fixed assets and depreciation

Fixed assets are stated at cost less accumulated depreciation, which is calculated to write off their cost over their anticipated useful lives on a straight line basis. The useful lives used are as follows:

|   |   |
|---|---|
| Leasehold improvements                      | – over the shorter of the period of the respective leases and 3 years |
| Furniture and fixtures                      | – 3 years   |
| Office equipment                            | – 5 years   |
| Personal computers and software             | – 3 years   |
| Mainframe computers and application systems | – 4 years   |
| Motor vehicles                              | – 4 years   |

#### f Investments

Investments, representing debt securities which are intended to be held to maturity, are stated at cost adjusted for the amortization of premiums and accretion of discounts on purchase over the periods to redemption less any provisions for impairments.

The carrying amounts of 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 the 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 debt securities are written back when the circumstances and events that have led to the write-down or write-off cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

Profits or losses on disposal of debt securities are accounted for in the income and expenditure account as they arise.

#### g Related parties

For the purpose of these financial statements, parties are considered to be related to the SFC if the SFC 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 SFC and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

#### h Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses are dealt with in the income and expenditure account.

### 4. Taxation

In accordance with section 3(3) of the Ordinance, the receipts of the SFC are not subject to Hong Kong taxation under the Hong Kong Inland Revenue Ordinance.

## Notes to the Financial Statements (cont'd)

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

**5. Staff Costs**

a Staff costs comprise:

|  | 2000<br>\$'000 | 1999<br>\$'000 |
|--|----------------|----------------|
| Directors' fees                                | 1,404          | 1,229          |
| Directors' salaries, allowances and gratuities | 27,670         | 26,761         |
| Directors' bonuses / variable pay              | 1,295          | 447            |
| Staff salaries, allowances and gratuities      | 233,179        | 209,507        |
| Retirement benefits                            | 3,722          | 3,277          |
| Medical and life insurance                     | 6,768          | 6,131          |
| Overtime pay                                   | 1,167          | 1,103          |
|  | <b>275,205</b> | <b>248,455</b> |

b The number of directors whose emoluments fell within the following bands were:

| Emolument Ranges           | 2000<br>No. of<br>directors | 1999<br>No. of<br>directors |
|----------------------------|-----------------------------|-----------------------------|
| \$0 to \$1,000,000         | 6                           | 9                           |
| \$1,000,001 to \$1,500,000 | -                           | 1                           |
| \$3,500,001 to \$4,000,000 | 1                           | -                           |
| \$4,000,001 to \$4,500,000 | 3                           | 3                           |
| \$4,500,001 to \$5,000,000 | -                           | 1                           |
| \$5,000,001 to \$5,500,000 | 1                           | 2                           |
| \$6,500,001 to \$7,000,000 | 1                           | -                           |
|                            | <b>12</b>                   | <b>16</b>                   |

c The five highest paid individuals during the year were all directors of the SFC, the aggregate remuneration of whom has been included in 5(a) and (b) above.

## Notes to the Financial Statements (cont'd)

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

### 5. Staff Costs (cont'd)

- d Retirement benefits are provided to all staff through a defined contribution scheme. For general grade staff, the SFC makes monthly contributions equal to 12% of the basic pay of each staff. Forfeited contributions in respect of general grade staff who leave the SFC prior to qualifying for 100% disbursement of the contributions are reinvested into the total pool of contributions and shared by the existing members in the scheme at the end of the scheme year. The amount so reinvested during the year was \$453,000 (1999: \$238,000).

For professional staff, effective from 1 March 2000, the SFC makes monthly contributions equal to 5% of their fixed pay but subject to a cap. Forfeited contributions in respect of professional staff who leave the SFC prior to qualifying for 100% disbursement of the contributions are used to offset the SFC's future contributions. There was no forfeiture during the year.

### 6. Other Expenses

Other expenses comprise:

|  | 2000<br>\$'000 | 1999<br>\$'000 |
|--|----------------|----------------|
| Training and development                       | 7,113          | 7,230          |
| Legal and professional services                | 34,368         | 36,468         |
| Legal claims and costs awarded                 | 2,500          | 770            |
| Information and systems services               | 10,439         | 9,408          |
| Auditors' remuneration                         | 152            | 148            |
| General office and insurance                   | 8,063          | 4,597          |
| Funding for the Hong Kong Securities Institute | 2,000          | 3,000          |
| Funding for the Investment Resources Centre    | -              | 3,500          |
| Loss on disposal of fixed assets               | 159            | -              |
|  | <b>64,794</b>  | <b>65,121</b>  |

## Notes to the Financial Statements (cont'd)

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

### 7. Fixed Assets

|                           | Furniture,<br>Fixtures and<br>Leasehold<br>Improvements<br>\$'000 | Office<br>Equipment<br>\$'000 | Mainframe<br>Computers<br>and<br>Application<br>Systems<br>\$'000 | Personal<br>Computers<br>and<br>Software<br>\$'000 | Motor<br>Vehicles<br>\$'000 | Total<br>\$'000      |
|---------------------------|---|-------------------------------|---|--|-----------------------------|----------------------|
| <b>Cost</b>               |   |                               |   |  |                             |                      |
| At 1 April 1999           | 24,873  | 6,973                         | 29,414  | 17,106   | 1,456                       | 79,822               |
| Additions during the year | 5,730   | 1,081                         | 13,414  | 3,988  | -                           | 24,213               |
| Disposals during the year | -   | (196)                         | (798)   | (5,369)  | -                           | (6,363)              |
| At 31 March 2000          | <u>30,603</u>   | <u>7,858</u>                  | <u>42,030</u>   | <u>15,725</u>                                      | <u>1,456</u>                | <u>97,672</u>        |
| <b>Depreciation</b>       |   |                               |   |  |                             |                      |
| At 1 April 1999           | 19,619  | 4,730                         | 19,555  | 14,446   | 608                         | 58,958               |
| Charge for the year       | 5,805   | 1,254                         | 7,187   | 3,047  | 364                         | 17,657               |
| Written back on disposals | -   | (196)                         | (798)   | (5,182)  | -                           | (6,176)              |
| At 31 March 2000          | <u>25,424</u>   | <u>5,788</u>                  | <u>25,944</u>   | <u>12,311</u>                                      | <u>972</u>                  | <u>70,439</u>        |
| <b>Net book value</b>     |   |                               |   |  |                             |                      |
| At 31 March 2000          | <u><b>5,179</b></u>   | <u><b>2,070</b></u>           | <u><b>16,086</b></u>  | <u><b>3,414</b></u>                                | <u><b>484</b></u>           | <u><b>27,233</b></u> |
| <b>Net book value</b>     |   |                               |   |  |                             |                      |
| At 31 March 1999          | <u>5,254</u>  | <u>2,243</u>                  | <u>9,859</u>  | <u>2,660</u>                                       | <u>848</u>                  | <u>20,864</u>        |

### 8. Held-to-Maturity Debt Securities

|                          |                            | 2000<br>\$'000        | 1999<br>\$'000 |
|--------------------------|----------------------------|-----------------------|----------------|
| Maturing after one year  | - unlisted                 | <b>360,192</b>        | 505,503        |
|                          | - listed in Hong Kong      | <b>80,105</b>         | 5,919          |
|                          | - listed outside Hong Kong | <b>36,992</b>         | -              |
|                          |                            | <u><b>477,289</b></u> | <u>511,422</u> |
| Maturing within one year | - unlisted                 | <b>217,873</b>        | 236,406        |
|                          | - listed in Hong Kong      | -                     | 40,025         |
|                          |                            | <u><b>217,873</b></u> | <u>276,431</u> |
|                          |                            | <u><b>695,162</b></u> | <u>787,853</u> |
| Market value at 31 March | - unlisted                 | <b>580,206</b>        | 742,513        |
|                          | - listed in Hong Kong      | <b>80,162</b>         | 46,031         |
|                          | - listed outside Hong Kong | <b>37,096</b>         | -              |
|                          |                            | <u><b>697,464</b></u> | <u>788,544</u> |

During the year, held-to-maturity debt securities, with an amortized cost of \$484,207,000, 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 \$86,971,000 were disposed of because of deterioration in the credit rating of the issuer. The aggregate profit on the disposal amounted to \$1,826,000.

## Notes to the Financial Statements (cont'd)

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

### 9. Debtors, Deposits and Prepayments

Included in debtors, deposits and prepayments is an interest-free loan to an executive for initial settling-in purpose amounting to \$108,000 (1999 : nil). The loan is repayable in equal installments over six months.

The maximum balance of outstanding loans to executives during the year was \$217,000 (1999 : nil).

### 10. Initial Funding by Government

This represents funds provided by Government to pay for the SFC's non-recurrent and capital expenditure when it was established. These funds are not repayable to Government.

### 11. Capital Commitments

Capital commitments outstanding at 31 March 2000 not provided for in the financial statements were as follows:

|                                   | 2000<br>\$'000 | 1999<br>\$'000 |
|-----------------------------------|----------------|----------------|
| Contracted for                    | <b>21,665</b>  | <b>5,270</b>   |
| Authorized but not contracted for | <b>8,489</b>   | <b>24,220</b>  |

### 12. Operating Lease Commitments

At 31 March 2000 the SFC had commitments under an operating lease in respect of its premises to make payments in the next year as follows:

|                               | 2000<br>\$'000 | 1999<br>\$'000 |
|-------------------------------|----------------|----------------|
| Lease expiring within 5 years | <b>17,227</b>  | <b>31,436</b>  |

### 13. Funds Held in Escrow

At 31 March 2000 the SFC held \$146,942,000 in escrow (1999 : \$139,811,000). These funds are not included in the financial statements as they are not beneficially owned by the SFC.

## Notes to the Financial Statements (cont'd)

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

### **14. Related Party Transactions**

As a result of the turmoil in the Asian markets in late 1997, and the subsequent failure of certain institutions connected with the securities markets, the Government, the SFC and the Stock Exchange of Hong Kong Limited (the Exchange) announced on 26 January 1998 that they would review the statutory limit of the Unified Exchange Compensation Fund (the Fund), which is established and maintained by the SFC, in the case of CA Pacific Securities Limited (CA Pacific). On 10 June 1998, the Exchange and the SFC announced that compensation to each claimant of CA Pacific would be allowed up to the higher of \$150,000 or the pro rata share of the statutory limit of \$8 million. The legislative amendments for such arrangements were enacted on 20 November 1998. In the financial year ended 31 March 1999, the Exchange and the SFC committed to make a contribution of \$150 million to the Fund. In addition, the SFC recorded its agreement to contribute a further \$150 million to the Fund as a contingent liability, subject to a similar contribution of \$150 million by the Exchange. This further contribution of \$150 million was fully provided for at 31 March 2000.

### **15. Comparative Figures**

The presentation and classification of items in the financial statements have been changed due to the adoption of the requirements of SSAP 1 (revised) "Presentation of financial statements" and SSAP 24 "Accounting for investments in securities". As a result, additional line items have been included on the face of the income and expenditure account and balance sheet as required by SSAP 1 (revised).

# Unified Exchange Compensation Fund Financial Statements

## Report of the Securities 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 the Unified Exchange Compensation Fund (the Fund)**

The Fund was established for the purpose set out in Part X of the Securities Ordinance (Chapter 333).

### **2. Financial Results**

The financial results are set out in the financial statements presented on pages 71 to 80.

### **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 Alec Tsui

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 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 Unified Exchange Compensation Fund (the Fund) established under Section 99 of the Hong Kong Securities Ordinance set out on pages 71 to 80 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

### Respective Responsibilities of the SFC and Auditors

The Hong Kong Securities 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 and cash flows 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                 |
|--|------|----------------------|----------------------|
| <b>Income</b>  |      |                      |                      |
| Interest and investment income   | 4    | \$ 21,696,925        | \$ 33,173,011        |
| Gain on disposal of held-to-maturity debt securities   | 4    | 117,034              | –                    |
|  |      | <u>\$ 21,813,959</u> | <u>\$ 33,173,011</u> |
| <b>Expenditure</b>   |      |                      |                      |
| Auditors' remuneration   |      |                      |                      |
| – current year   |      | \$ 38,900            | \$ 37,000            |
| – under provision in respect of previous year  |      | 25,000               | –                    |
| Premium on investments amortized   | 4    | 324,971              | 479,252              |
| Loss on disposal of held-to-maturity debt securities   | 4    | –                    | 65,100               |
| Bank charges   |      | 146,532              | 195,700              |
| Legal and professional fees  |      | 132,000              | 2,248,828            |
| Sundry expenses  |      | 57,798               | 20,935               |
|  |      | <u>\$ 725,201</u>    | <u>\$ 3,046,815</u>  |
| <b>Surplus of Income Over Expenditure Before Appropriations</b>  |      | <b>\$ 21,088,758</b> | <b>\$ 30,126,196</b> |
| <b>Balance Brought Forward</b>   |      | <b>\$ –</b>          | <b>\$ –</b>          |
| <b>Appropriations</b>  |      |                      |                      |
| Payment to The Stock Exchange of Hong Kong Limited pursuant to S105(2)(a) of the Securities Ordinance, Chapter 333(2000 - Nil, 1999 - 5.3915%) |      | –                    | 857,625              |
| Transfer to Compensation Fund Account  | 12   | 21,088,758           | 29,268,571           |
| <b>Balance Carried Forward</b>   |      | <b>\$ –</b>          | <b>\$ –</b>          |

The notes on pages 76 to 80 form an integral part of the financial statements.

## Balance Sheet

As at 31 March 2000 (Expressed in HK dollars)

|  | Note | 2000                   | 1999                   |
|--|------|------------------------|------------------------|
| <b>Non current held-to-maturity debt securities</b>                      | 4&5  | \$ 22,096,617          | \$ 187,271,810         |
| <b>Current Assets</b>  |      |                        |                        |
| Current held-to-maturity debt securities                                 | 4&5  | \$ 142,033,530         | \$ 182,102,034         |
| Contributions receivable   | 11   | 100,000,000            | 300,000,000            |
| Interest receivable  |      | 2,244,468              | 3,705,637              |
| Bank fixed and call deposits   |      | 175,751,462            | 29,250,549             |
| Cash at bank   |      | 125,582                | 145,651                |
|  |      | <u>\$ 420,155,042</u>  | <u>\$ 515,203,871</u>  |
| <b>Current Liabilities</b>   |      |                        |                        |
| Accounts payable and accrued charges                                     |      | \$ 1,028,418           | \$ 521,844             |
| Interest payable   |      | -                      | 857,625                |
| Provision for compensation   | 4    | 177,950,000            | 435,619,591            |
|  |      | <u>\$ 178,978,418</u>  | <u>\$ 436,999,060</u>  |
| <b>Net Current Assets</b>  |      | <u>\$ 241,176,624</u>  | <u>\$ 78,204,811</u>   |
| <b>Net Assets</b>  |      | <u>\$ 263,273,241</u>  | <u>\$ 265,476,621</u>  |
| Representing:  |      |                        |                        |
| <b>Compensation Fund</b>   |      |                        |                        |
| Contributions from The Stock Exchange of<br>Hong Kong Limited (the SEHK) | 6    | \$ 46,450,000          | \$ 46,450,000          |
| less: Compensation paid  | 4&7  | (68,815,176)           | (59,339,040)           |
| Provision for compensation   | 4    | (26,658,386)           | (11,984,522)           |
| add: Recovery under subrogation  | 4&8  | 3,530,920              | 936,529                |
| Replenishment from the SEHK  | 4&9  | 12,732,698             | 7,327,089              |
|  |      | <u>\$ (32,759,944)</u> | <u>\$ (16,609,944)</u> |
| Excess transaction levy from the SEHK                                    | 10   | \$ 353,786,882         | \$ 353,786,882         |
| Special Contribution   |      | 3,500,000              | 3,500,000              |
| Additional contributions from the SEHK and the SFC                       | 11   | 300,000,000            | 300,000,000            |
| Income and expenditure account   | 12   | 159,551,489            | 138,462,731            |
|  |      | <u>\$ 816,838,371</u>  | <u>\$ 795,749,613</u>  |
| less: Compensation paid  | 4&7  | (369,513,572)          | (90,027,979)           |
| Provision for compensation   | 4    | (151,291,614)          | (423,635,069)          |
|  |      | <u>\$ 296,033,185</u>  | <u>\$ 282,086,565</u>  |
|  |      | <u>\$ 263,273,241</u>  | <u>\$ 265,476,621</u>  |

Approved by the Securities 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

Alec Tsui  
Committee Member

## Statement of Recognized Gains and Losses

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

|  | Note | 2000                   | 1999                    |
|--|------|------------------------|-------------------------|
| Recovery under subrogation                               | 8    | \$ 2,594,391           | \$ –                    |
| Replenishment received from the SEHK                     | 9    | 5,405,609              | –                       |
| Additional contributions from the SEHK and the SFC       | 11   | –                      | 300,000,000             |
| Decrease / (increase) in provision for compensation      |      | 257,669,591            | (395,619,591)           |
| Compensation paid out of the Fund                        | 7    | (288,961,729)          | (118,043,457)           |
| <b>Net losses not recognized in the income statement</b> |      | <b>\$ (23,292,138)</b> | <b>\$ (213,663,048)</b> |
| Net surplus for the year                                 |      | 21,088,758             | 30,126,196              |
| <b>Total recognized losses</b>                           |      | <b>\$ (2,203,380)</b>  | <b>\$ (183,536,852)</b> |

The notes on pages 76 to 80 form an integral part of the financial statements.

## Cash Flow Statement

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

|  | Note | 2000            | 1999             |
|--|------|-----------------|------------------|
| Net cash inflow / (outflow) from operating activities                | a    | \$ 106,344      | \$ (2,487,441)   |
| Returns on investments and servicing of finance                      |      |                 |                  |
| Interest received  |      | \$ 23,158,094   | \$ 34,046,856    |
| Interest paid  |      | (857,625)       | (2,155,125)      |
| Net cash inflow from returns on investments and servicing of finance |      | \$ 22,300,469   | \$ 31,891,731    |
| Investing activities   |      |                 |                  |
| Receipts from redemption of held-to-maturity debt securities         |      | \$ 137,000,000  | \$ 84,000,000    |
| Proceeds from disposal of held-to-maturity debt securities           |      | 90,172,160      | 20,955,974       |
| Payments to acquire held-to-maturity debt securities                 |      | (22,136,400)    | (5,097,000)      |
| Net cash inflow from investing activities                            |      | \$ 205,035,760  | \$ 99,858,974    |
| Financing  |      |                 |                  |
| Recovery under subrogation   | b    | \$ 2,594,391    | \$ -             |
| Replenishment received from the SEHK                                 | b    | 5,405,609       | -                |
| Additional contributions received from the SEHK and the SFC          | b    | 200,000,000     | -                |
| Compensation paid  | b    | (288,961,729)   | (118,043,457)    |
| Net cash outflow from financing                                      |      | \$ (80,961,729) | \$ (118,043,457) |
| Increase in cash and cash equivalents                                |      | \$ 146,480,844  | \$ 11,219,807    |
| Cash and cash equivalents at beginning of the year                   |      | 29,396,200      | 18,176,393       |
| Cash and cash equivalents at end of the year                         | c    | \$ 175,877,044  | \$ 29,396,200    |

## Cash Flow Statement (cont'd)

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

(a) Reconciliation of surplus of income over expenditure to net cash inflow / (outflow) from operating activities:

|   | 2000              | 1999                  |
|---|-------------------|-----------------------|
| Surplus of income over expenditure for the year               | \$ 21,088,758     | \$ 30,126,196         |
| Interest income   | (21,696,925)      | (33,173,011)          |
| Premium on investments amortized                              | 324,971           | 493,860               |
| Discount on investments accreted                              | –                 | (14,608)              |
| (Gain) / loss on disposal of held-to-maturity debt securities | (117,034)         | 65,100                |
| Increase in creditors and accrued charges                     | 506,574           | 15,022                |
| Net cash inflow / (outflow) from operating activities         | <u>\$ 106,344</u> | <u>\$ (2,487,441)</u> |

(b) Analysis of changes in financing:

|   | Recovery<br>under<br>subrogation | Replenishment<br>received | Additional<br>contributions<br>received from<br>the SEHK and<br>the SFC | Compensation<br>paid    |
|---|----------------------------------|---------------------------|---|-------------------------|
| Balance at 1 April 1998                   | \$ 936,529                       | \$ 7,327,089              | \$ –  | \$ (31,323,562)         |
| Cash outflow from financing               | –                                | –                         | –   | (118,043,457)           |
| Balance at 31 March 1999                  | <u>\$ 936,529</u>                | <u>\$ 7,327,089</u>       | <u>\$ –</u>   | <u>\$ (149,367,019)</u> |
| Balance at 1 April 1999                   | \$ 936,529                       | \$ 7,327,089              | \$ –  | \$ (149,367,019)        |
| Cash inflow /<br>(outflow) from financing | 2,594,391                        | 5,405,609                 | 200,000,000   | (288,961,729)           |
| Balance at 31 March 2000                  | <u>\$ 3,530,920</u>              | <u>\$ 12,732,698</u>      | <u>\$ 200,000,000</u>   | <u>\$ (438,328,748)</u> |

(c) Analysis of the balance of cash and cash equivalents as shown in the balance sheet:

|                              | 2000                  | 1999                 |
|------------------------------|-----------------------|----------------------|
| Cash at bank                 | \$ 125,582            | \$ 145,651           |
| Bank fixed and call deposits | 175,751,462           | 29,250,549           |
|                              | <u>\$ 175,877,044</u> | <u>\$ 29,396,200</u> |

## Notes to the Financial Statements

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

### 1. Status Change of the SEHK Members

As a result of a scheme of arrangement, on 6 March 2000 the Stock Exchange of Hong Kong Limited (the SEHK) became a wholly owned subsidiary of Hong Kong Exchanges and Clearing Limited (HKEx), and the ownership of shares in the SEHK was separated from access to its trading facilities. The existing members of the SEHK ceased to be shareholders of the SEHK and became either exchange participants or holders of a trading right only. To become an exchange participant of the SEHK, 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 way of deposits by the SEHK in respect of the trading rights, by way of excess transaction levy from the SEHK in accordance with an agreement between the SFC and the SEHK (see note 10), by way of money lawfully paid into the Fund pursuant to Section 101(1) of the Securities Ordinance (Chapter 333) (SO) and from return or profit on the investment of surplus funds.

### 3. Purpose, Limitation and Principal Activity

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

The total amount of compensation including interest that may be paid to claimants consequent upon the default of any one exchange participant committed after 7 October 1992 is normally limited to \$8,000,000 (before 7 October 1992 the limit was \$2,000,000) pursuant to the amendment made to Section 109(3) of the SO that came into operation on 7 October 1992. If the aggregate of the allowed claims in respect of an exchange participant exceeds the \$8,000,000 limit, that amount shall be apportioned among claimants as determined to be equitable by the SEHK. Further amendment to Section 113 of the SO was enacted on 20 November 1998 to empower the SFC to approve the SEHK to allow the total amount of compensation payable to claimants in respect of the default of an exchange participant to exceed the \$8,000,000 limit after considering the circumstances of the default and the financial position of the Fund.

Should defaults at any given time on the part of exchange participants of the SEHK 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 120(1) of the SO, 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 and investment income is recognized in the financial statements on an accruals basis.
- (ii) Premium or discount on the purchase of the 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 the 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 should be written back to income when the circumstances and events that lead to the write-down cease to exist and there is prominent 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 118 of the SO, and replenishment from the SEHK pursuant to Section 107 of the SO, are recognized in the financial statements on a cash basis and taken directly to the Fund.
- (vi) As a result of the enactment of the amendments to Section 113 of the SO in November 1998, the maximum liability of the Fund to claims for each default case can exceed the normal \$8,000,000 limit. In order to more appropriately reflect the liability of the Fund for outstanding claims in respect of default cases, provision for compensation is made for known liabilities arising from claims which have been received up to the date on which the financial statements are approved by the Committee for pecuniary losses suffered by persons as a result of defaults on the part of the SEHK's exchange participants for which the SEHK has published a notice calling for claims pursuant to Section 112 of the SO. Compensation payments and provisions for each default are charged to the contributions from the SEHK as required pursuant to Sections 104 and 106 of the SO to the limit of \$8,000,000. Any excesses over the \$8,000,000 limit are charged to other components of 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  | – unlisted            | \$ 22,096,617         | \$ 187,271,810        |
| Maturing within one year | – listed in Hong Kong | \$ –                  | \$ 33,014,246         |
|                          | – unlisted            | 142,033,530           | 149,087,788           |
|                          |                       | <u>\$ 142,033,530</u> | <u>\$ 182,102,034</u> |
|                          |                       | <u>\$ 164,130,147</u> | <u>\$ 369,373,844</u> |
| Market value at 31 March | – listed in Hong Kong | \$ –                  | \$ 33,093,600         |
|                          | – unlisted            | 164,336,800           | 335,640,300           |
|                          |                       | <u>\$ 164,336,800</u> | <u>\$ 368,733,900</u> |

During the year, held-to-maturity debt securities, with an amortized cost of \$68,052,080, were disposed of (in order to meet liquidity needs) to pay compensation to claimants. In addition, due to the depletion of funds resulting from significant compensation payments made during the year, some holdings of the investment portfolio exceeded the country exposure limit specified in the Fund's investment policies and guidelines. In order to restore the country exposure of the portfolio to within the limit, held-to-maturity debt securities with an amortized cost of \$22,003,046 were disposed of. The aggregate profit on the disposal amounted to \$117,034.

## 6. Contributions from the SEHK

- a Before 6 March 2000, in accordance with Sections 104 and 106 of the SO, the SEHK was required to deposit with the SFC a sum of \$50,000 in respect of each membership of the SEHK not later than one month after membership was taken up. In the absence of claims or other provisions as set out in Section 106 of the SO, the SFC was required to refund to the SEHK from the Fund such deposit within six months after membership ceases.

The SEHK advised the SFC of thirty four (34) memberships having been taken up during the six (6) months to 6 March 2000. However, the SEHK had not at 6 March 2000 deposited with the SFC a sum of \$50,000 in respect of each such membership. The liability of the SEHK to the Fund in this respect has not been taken up in these financial statements. Any monetary liability of the SEHK that may have existed due to memberships taken up prior to six (6) months before 6 March 2000 would be extinguished by the requirement of the Fund to refund to the SEHK deposits of ceased memberships in accordance with Section 106(1) of the SO, as the number of new members equalled the number of members leaving the SEHK during the period.

- b After 6 March 2000, pursuant to Sections 104 and 106 of the SO, the SEHK is required to deposit with the SFC a sum of \$50,000 in respect of each trading right of the SEHK not later than 1 month after the need to deposit \$50,000 for a trading right arises. In the absence of claims or other provisions as set out in Section 106 of the SO, the SFC is required to refund to the SEHK from the Fund such deposit in respect of a person who has ceased to be a holder of a trading right within six months after the cessation. During the period from 6 March 2000 to 31 March 2000, the SEHK advised the SFC of no change in the number of trading rights.

## Notes to the Financial Statements (cont'd)

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

### 7. Compensation Paid

|  | 2000                  | 1999                  |
|--|-----------------------|-----------------------|
| Compensation paid up to the \$8 million limit as set out by Section 109(3) of the SO       |                       |                       |
| Balance brought forward  | \$ 59,339,040         | \$ 31,323,562         |
| Add: Compensation paid during the year   | 9,476,136             | 28,015,478            |
| Balance carried forward  | \$ 68,815,176         | \$ 59,339,040         |
| Compensation paid in excess of the \$8 million limit pursuant to Section 113(5A) of the SO |                       |                       |
| Balance brought forward  | \$ 90,027,979         | \$ –                  |
| Add: Compensation paid during the year   | 279,485,593           | 90,027,979            |
| Balance carried forward  | \$ 369,513,572        | \$ 90,027,979         |
| <b>Total compensation paid</b>   | <b>\$ 438,328,748</b> | <b>\$ 149,367,019</b> |

The total amount of compensation including interest in respect of each defaulted exchange participant is normally limited to \$8 million pursuant to Section 109(3) of the SO. In respect of the claims against C.A. Pacific Securities Ltd. (CA Pacific), the SEHK and the SFC announced on 10 June 1998 that compensation payable to each claimant would be allowed up to the higher of \$150,000 or the pro rata share of the statutory maximum limit of \$8 million. The legislative amendments for the aforesaid arrangements were enacted on 20 November 1998. The SEHK and the SFC have also decided to apply these compensation arrangements to claims against Forlux Securities Ltd. (Forlux), Foreground Securities Co. Ltd. (Foreground) and Chark Fung Securities Ltd. (Chark Fung).

During the year, compensation payments totalling \$288,961,729 were made in respect of three defaulting exchange participants, CA Pacific, Chark Fung and Forlux which have been determined within the \$150,000 limit per claimant under the aforesaid compensation arrangements.

### 8. Recovery under Subrogation

|   | 2000                | 1999              |
|---|---------------------|-------------------|
| Balance brought forward                 | \$ 936,529          | \$ 936,529        |
| Amount recovered during the year        | 2,594,391           | –                 |
| <b>Total recovery under subrogation</b> | <b>\$ 3,530,920</b> | <b>\$ 936,529</b> |

Under Section 118 of the SO, the SFC is entitled to receive in place of the claimant, all claims, remedies and distribution 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.

### 9. Replenishment from the SEHK

|  | 2000                 | 1999                |
|--|----------------------|---------------------|
| Balance brought forward                        | \$ 7,327,089         | \$ 7,327,089        |
| Amount replenished by the SEHK during the year | 5,405,609            | –                   |
| <b>Total replenished by the SEHK</b>           | <b>\$ 12,732,698</b> | <b>\$ 7,327,089</b> |

## Notes to the Financial Statements (cont'd)

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

### 9. Replenishment from the SEHK (cont'd)

When all relevant rights of action and other legal remedies conferred by Section 118 of the SO against the exchange participant in relation to which the claim arose have been exhausted, the SEHK shall under Section 107 of the SO, on being required to do so by the SFC, replenish the fund with an amount that is equal to that paid in connection with the satisfaction of the claim, including any legal and other expenses paid or incurred in relation to the claim.

### 10. Excess Transaction Levy from the SEHK

In accordance with an agreement reached in 1991 between the SFC and the SEHK, the SEHK was to remit to the Fund any excess of its transaction levy revenue over one third of its budgeted expenses and any income from the transaction levy when its reserves exceeded the sum of its immediately preceding two years' recurrent expenditure.

According to the 1994-95 budget of the SEHK approved by the Financial Secretary in August 1994, excess transaction levy revenue would be diverted to the reserves of the SEHK instead of the Fund after the Fund had reached \$400 million, which it did on 30 June 1994.

Accordingly, no excess transaction levy was transferred to the Fund during the year.

### 11. Additional Contributions from the SEHK and the SFC

In connection with the compensation arrangements announced in June 1998 (please refer to Note 7), the SEHK and the SFC had committed to make a contribution of \$150 million each to the Fund in the financial year 1998-99 and agreed to make a further contribution of \$150 million each should it become necessary. In respect of this commitment, a partial contribution of \$100 million each in relation to the first contribution of \$150 million was received from the SEHK and the SFC during the year.

### 12. Movement in Income and Expenditure Account

|                                       | 2000                  | 1999                  |
|---------------------------------------|-----------------------|-----------------------|
| Balance brought forward               | \$ 138,462,731        | \$ 109,194,160        |
| Add: Transfer of surplus for the year | 21,088,758            | 29,268,571            |
| Balance carried forward               | <u>\$ 159,551,489</u> | <u>\$ 138,462,731</u> |

### 13. Related Party Transactions

In the financial year 1998-99, the Fund recognized the initial contribution of \$150 million from the SFC regarding the compensation arrangements announced in June 1998. \$100 million of this initial contribution was received during the year.

### 14. Contingent Liabilities

As at the date of this report, claims against four exchange participants had been received by the SEHK. They are subject to the normal \$8,000,000 limit pursuant to Section 109 of the SO. The validity of these claims is under investigation. The maximum liabilities of the Fund to the claims is \$32 million. No provision has been made in these financial statements for these claims in respect of any of these cases.

# 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                |
|--|------|---------------------|---------------------|
| <b>Income</b>  |      |                     |                     |
| 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> |
| <b>Expenditure</b>   |      |                     |                     |
| 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>   |
| <b>Surplus of Income Over Expenditure Before Appropriations</b>  |      | <b>\$ 6,184,185</b> | <b>\$ 5,320,088</b> |
| <b>Balance Brought Forward</b>   |      | <b>-</b>            | <b>-</b>            |
| <b>Appropriations</b>  |      |                     |                     |
| Transfer to Compensation Fund Account<br>pursuant to S83(2)(a) of the Commodities<br>Trading Ordinance (Chapter 250) | 8    | 6,184,185           | 5,320,088           |
| <b>Balance Carried Forward</b>   |      | <b>\$ -</b>         | <b>\$ -</b>         |

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                 |
|---|------|-----------------------|----------------------|
| <b>Non current held-to-maturity debt securities</b> | 4&5  | \$ 64,576,698         | \$ 44,204,727        |
| <b>Current Assets</b>                               |      |                       |                      |
| 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> |
| <b>Current Liabilities</b>                          |      |                       |                      |
| Accounts payable and accrued charges                |      | 248,655               | 244,379              |
| <b>Net Current Assets</b>                           |      | <u>\$ 26,957,947</u>  | <u>\$ 34,688,614</u> |
| <b>Net Assets</b>                                   |      | <u>\$ 91,534,645</u>  | <u>\$ 78,893,341</u> |
| <b>Representing:</b>                                |      |                       |                      |
| <b>Compensation Fund</b>                            |      |                       |                      |
| 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)          |
| <b>Net gains not recognized in the income statement</b> |      | <b>\$ 6,457,119</b>  | <b>\$ 5,701,791</b>  |
| Net surplus for the year                                |      | 6,184,185            | 5,320,088            |
| <b>Total recognized gains</b>                           |      | <b>\$ 12,641,304</b> | <b>\$ 11,021,879</b> |

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.