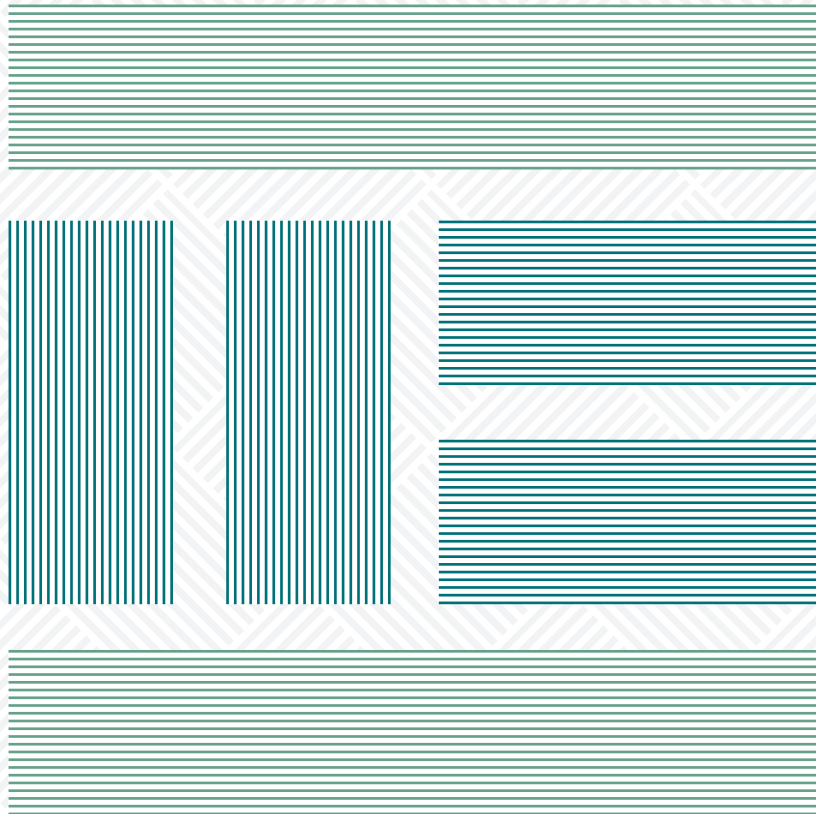




SECURITIES AND
FUTURES COMMISSION

證券及期貨事務監察委員會



Regulation for Quality Markets

Quarterly Report
October - December 2017

This third Quarterly Report of the Securities and Futures Commission for financial year 2017-18 covers the period from 1 October to 31 December 2017.

Contents

2	Highlights
4	Operational Review
4	Intermediaries
7	Investment products
9	Listings and takeovers
10	Market infrastructure and trading
11	Enforcement
13	Global regulatory engagement
15	Stakeholder communication
16	Corporate Developments
17	Activity Data
21	Financial Statements
21	Securities and Futures Commission
29	Investor Compensation Fund
36	Unified Exchange Compensation Fund

Highlights

Regulatory enhancements

- **Asset management:** We concluded a consultation on proposals to enhance asset management regulation and point-of-sale transparency whilst commencing a further consultation on disclosure requirements for discretionary accounts.
- **Cybersecurity:** We issued consultation conclusions on hacking risks associated with internet trading along with a set of guidelines and a circular on good practices for risk management and cybersecurity.
- **OTC derivatives and conduct risks:** We launched a public consultation on proposals to refine the over-the-counter (OTC) derivatives regime and strengthen the management of financial and conduct risks.
- **Funds:** To update the regulatory regime for SFC-authorized funds and address emerging risks, we launched a consultation on proposed amendments to the Code on Unit Trusts and Mutual Funds.

Listings and takeovers

- **GEM review:** Following the SFC's approval, Hong Kong Exchanges and Clearing Limited published conclusions to a consultation on GEM and changes to the Listing Rules.
- **Listing applications:** We reviewed 40 new listing applications, up 5.3% year-on-year.
- **Takeovers matters:** We publicly censured one individual for breach of the Takeovers Code.

Intermediaries

- **Licensees and registrants:** As at 31 December 2017, the number of licensees and registrants reached 44,169, up 3.5% year-on-year, and the number of licensed corporations increased 10.3% to 2,660. Both were record highs.
- **Senior management accountability:** The Manager-In-Charge (MIC) regime was fully implemented following a six-month transition period, when about 10,000 individuals were appointed by licensed corporations as MICs responsible for managing important functions.
- **Inspections:** We conducted 71 risk-based on-site inspections of licensed corporations to review their compliance with regulatory requirements.
- **Promoting Compliance:** We published 18 circulars to update and remind industry participants of various regulatory matters.

Market surveillance

- **Investor identification:** We reached an agreement with the China Securities Regulatory Commission (CSRC) on the implementation of investor identification for Northbound trading under Stock Connect.
- **Requests to intermediaries:** We made 1,644 requests for trading and account records from intermediaries following our surveillance of untoward price and turnover movements.

Enforcement

- **Systemic failures in product sales:** The Securities and Futures Appeal Tribunal upheld our disciplinary action against HSBC Private Bank (Suisse) SA which was fined a record \$400 million.
- **Guidance note on cooperation:** We issued an updated guidance note to highlight the benefits of cooperation in our investigation and enforcement proceedings.
- **Disciplinary actions:** We disciplined two corporations and five licensed representatives for internal control failures, unauthorised trading in clients' accounts or conducting transactions without written client authorisation.

Regulatory collaboration

- **Futures markets:** We entered into a memorandum of understanding with the CSRC to facilitate regulatory and enforcement cooperation in the Mainland and Hong Kong futures markets.
- **EU-Asia Pacific Forum:** We hosted the second EU-Asia Pacific Forum where cross-border regulatory issues were discussed.

Stakeholder communication

- **Fintech Day:** We co-organised a full-day programme with the Hong Kong Monetary Authority to discuss regulatory issues related to financial technology.
- **Industry publication:** The inaugural issue of the *SFC Compliance Bulletin: Intermediaries* highlighted the importance of managing conflicts of interest in selling practices and asset management.

Intermediaries

Licence applications

In the quarter, we received 1,924 licence applications¹, down 9.6% from the last quarter and up 7.7% year-on-year. The number of corporate applications rose 50.8% from the last quarter to 98, up 18.1% year-on-year.

As at 31 December 2017, the number of licensees and registrants totalled 44,169, up 3.5% from last year, and the number of licensed corporations grew 10.3% to 2,660. Both were record highs.

Senior management accountability

On 17 October, we announced the full implementation of the Manager-In-Charge (MIC) regime² following a six-month transition period, during which about 10,000 individuals³ were appointed by licensed corporations as MICs responsible for managing important functions. The announcement also reminded registered institutions to submit relevant management information and organisational charts⁴ to both the Hong Kong Monetary Authority (HKMA) and the SFC by 16 April 2018.

Cybersecurity

On 27 October, we issued conclusions to a consultation on proposals to reduce and mitigate hacking risks associated with internet trading, along with related guidelines and a circular to licensed intermediaries. One key control, two-factor authentication for clients to login to their internet trading accounts, will take effect on 27 April 2018, with all other requirements taking effect on 27 July 2018.

Point-of-sale transparency

On 16 November, we published consultation conclusions to enhance asset management regulation and point-of-sale transparency, including the disclosure of non-quantifiable monetary benefits (eg, trailer fees). We also commenced a two-month consultation on proposed requirements for the disclosure of monetary and non-monetary benefits to discretionary account clients.

OTC derivatives and conduct risks

On 20 December, we launched a two-month consultation on proposals to refine the over-the-counter (OTC) derivatives regime and to require licensed corporations to properly manage financial exposures to connected persons. The proposals refine the scope of certain regulated activities to provide more clarity on the OTC derivatives licensing regime in response to market comments. The consultation also includes proposals related to risk mitigation, client clearing, record keeping and other conduct requirements for OTC derivatives transactions, as well as licensing fees, insurance, competence and training requirements under the new regime.

Intermediary monitoring

During the quarter, we conducted 71 risk-based on-site inspections of licensed corporations to review their compliance with regulatory requirements.

¹ The figure does not include applications for provisional licences. See the table on licensing applications on page 6 for details.

² Under the MIC regime, licensed corporations and corporate licence applicants are required to submit up-to-date management structure information and organisational charts to the SFC.

³ Around 40% are not licensed persons as they do not conduct regulated activities and are primarily responsible for managing operations and control functions.

⁴ See the HKMA's 16 October 2017 circular.

Intermediaries

Promoting compliance

We published the first issue of the *SFC Compliance Bulletin: Intermediaries* in December to highlight the importance of managing conflicts of interest in selling practices and asset management and provide an overview of industry demographics.

Risk management

On 10 October, we issued a circular to licensed corporations providing securities margin financing to remind them to vigilantly monitor risks and adopt prudent margin lending and risk management policies in light of volatility in small-cap stocks and some licensed corporations' excessive exposure to securities collateral which was highly concentrated and illiquid.

On 18 December, we issued a circular to provide licensed corporations with additional guidance and examples of good practices for establishing and maintaining prudential risk management practices for client money, liquidity and the concentration risks of funding sources from affiliated entities.

Conflicts of interest

Together with the HKMA, we issued a joint circular on 24 November to share observations and good practices noted in our joint thematic review of potential conflicts of interest arising from the sale of in-house products by intermediaries within the same financial group. The circular also reminded intermediaries about the regulators' expected standards of conduct regarding conflicts of interest.

Cryptocurrencies

We issued a circular on 11 December to remind intermediaries about the legal and regulatory requirements for providing financial services in relation to Bitcoin futures contracts and other cryptocurrency-related products. This followed the launch by futures and commodities exchanges in the United States of Bitcoin futures contracts which can be traded by Hong Kong investors through an intermediary. The circular also cautioned investors of the substantial risks associated with cryptocurrency-related products, including high price volatility and illiquidity.

Corporate transaction valuations

On 13 December, we issued frequently asked questions on the application of our 15 May 2017 circular to financial advisers on valuations in corporate transactions.

Anti-money laundering

In November and December, we met with 10 industry associations, including the Hong Kong Investment Funds Association, Alternative Investment Management Association, Asia Securities Industry and Financial Markets Association and seven major broker associations, to brief them on proposed amendments to the Guideline on Anti-Money Laundering and Counter-Terrorist Financing⁵.

We issued seven circulars during the quarter to promote compliance with anti-money laundering and counter-terrorist financing requirements. In addition, we gave a presentation at an industry association training seminar in October and hosted three seminars in November and December for more than 900 staff of licensed corporations.

⁵ These amendments arise from proposed changes to the provisions of the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance relating to financial institutions in the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) (Amendment) Bill 2017.

Intermediaries

Licenses and registrants

	As at 31.12.2017	As at 31.3.2017	Change (%)	As at 31.12.2016	YoY change (%)
Licensed corporations	2,660	2,484	7.1	2,411	10.3
Registered institutions	119	121	-1.7	121	-1.7
Licensed individuals	41,390	40,267	2.8	40,133	3.1
Total	44,169	42,872	3.0	42,665	3.5

Licensing applications

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
Applications to conduct new regulated activity	5,526	16,992	16,491	3
Applications for SFC licences [#]	1,924	5,750	5,880	-2.2

[#] Figures do not include applications for provisional licences. During the quarter, we received 942 provisional licence applications compared with 804 in the same quarter last year.

Intermediary inspection

	Quarter ended 31.12.2017	Quarter ended 30.9.2017	Change (%)	Quarter ended 31.12.2016	YoY change (%)
Risk-based on-site inspections conducted	71	80	-11.3	89	-20.2

Investment products

Authorisations

As of 31 December, there were 2,789 SFC-authorized collective investment schemes (CIS) on offer to the public. During the quarter, we authorised 36 CIS, all of which were unit trusts and mutual funds. We also authorised 18 unlisted structured investment products for public offering.

Renminbi products

As of 31 December, there were 59 renminbi-denominated SFC-authorized unlisted funds and 29 exchange-traded funds (ETFs) investing onshore in the Mainland securities markets¹, with total assets under management of RMB40.8 billion.

Mutual recognition of funds (MRF)

Mainland China

Under the Mainland-Hong Kong MRF scheme, as of 31 December, we had authorised a total of 50 Mainland funds (including two umbrella funds), and the China Securities Regulatory Commission had approved ten Hong Kong funds.

Switzerland

As of 31 December, four SFC-authorized funds were approved by the Swiss Financial Market Supervisory Authority for distribution to retail investors in Switzerland under the Switzerland-Hong Kong MRF arrangement.

Asset management regulation

On 16 November, we published consultation conclusions on proposed enhancements to asset management regulation and point-of-sale transparency. These enhancements ensure our regulations are properly benchmarked to evolving international standards and strengthen Hong Kong's position as a major asset management centre. We also launched a further consultation on disclosure requirements applicable to discretionary accounts.

Code on Unit Trusts and Mutual Funds

To update the regulatory regime for SFC-authorized funds and address risks posed by financial innovation and fast-moving market developments, we launched a three-month consultation on proposed amendments to the Code on Unit Trusts and Mutual Funds on 18 December.

The proposals strengthen requirements for key operators, provide greater flexibility and enhanced safeguards for funds' investment activities and introduce new fund types, including active ETFs. The consultation will close on 19 March 2018.

Expansion of online submissions

During the quarter, we announced that information under section 110(1) of the Securities and Futures Ordinance (SFO)² may be submitted electronically via the SFC Online Portal from 24 November onwards.

¹ These unlisted funds and ETFs primarily invest in the Mainland securities markets through the Renminbi Qualified Foreign Institutional Investor quota, Stock Connect, Bond Connect and the China Interbank Bond Market.

² Under section 110(1) of the SFO, an authorised financial institution, a bank incorporated outside of Hong Kong and other specified persons are required to submit certain prescribed information to the SFC within 10 business days (or such longer period as is prescribed by rules made under section 397 of the SFO) after the issue of any advertisement, invitation or document referred to in section 103(3)(e), (f) or (g) of the SFO relating to the issue of certificates of deposit or other specified instruments.

Investment products

Authorised CIS^a

	As at 31.12.2017	As at 31.3.2017	Change (%)	As at 31.12.2016	YoY change (%)
Unit trusts and mutual funds	2,205	2,203	0.1	2,196	0.4
Investment-linked assurance schemes	299	300	-0.3	300	-0.3
Pooled retirement funds	34	34	0	34	0
Mandatory provident fund (MPF) schemes	31	35	-11.4	35	-11.4
MPF pooled investment funds	194	182	6.6	188	3.2
Others	26 ^b	26	0	26	0
Total	2,789	2,780	0.3	2,779	0.4

^a Excluding unlisted structured investment products.

^b Comprising 15 paper gold schemes and 11 real estate investment trusts.

Unlisted structured investment products

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
Unlisted structured investment products ^a	18	105	83	26.5
Authorisations granted under section 105 of the SFO ^b	11	68	62	9.7

^a On a "one product per key facts statement" basis, the number of unlisted structured investment products authorised during the period, most of which were equity-linked investments and deposits.

^b Offering documents and advertisements for unlisted structured investment products offered to the Hong Kong public.

Listings and takeovers

GEM review and New Board proposal

On 15 December, following approval by the SFC, Hong Kong Exchanges and Clearing Limited published conclusions to a consultation on the review of GEM and changes to GEM and Main Board Listing Rules. The changes, which took effect on 15 February 2018, include removing the streamlined process for GEM transfers to the Main Board; introducing a mandatory public offering requirement of at least 10% of the total offer size for all GEM initial public offerings (IPOs); increasing the minimum cash flow requirement for GEM applicants from \$20 million to \$30 million, and increasing the minimum market capitalisation of Main Board applicants at the time of listing from \$200 million to \$500 million.

On the same day, The Stock Exchange of Hong Kong Limited (SEHK) announced conclusions to the New Board Concept Paper published in June 2017. In response to market feedback, SEHK proposed that the existing listing regime should be expanded by introducing two new chapters to the Main Board Listing Rules to allow the listing of companies from emerging and innovative sectors, including biotechnology companies which are pre-profit or pre-revenue and companies with weighted voting rights structures.

IPO applications

We reviewed 40 new listing applications during the quarter, up 5.3% from 38 in the same quarter last year. The number of listing applications in the nine months from April to December was 236, up 22.3% compared to the same period in 2016.

During the quarter, we issued one “letter of mindedness to object” directly to a listing applicant¹. Four listing applications were returned² and an eight-week moratorium³ imposed because the respective application proofs were not substantially complete.

Corporate conduct

We conduct a daily review of corporate announcements under the statutory corporate conduct and inside information disclosure provisions. In six cases during the quarter, we felt it appropriate to issue section 179⁴ directions to gather additional information. The underlying concerns were varied and included whether a corporate action had been conducted in a manner which is oppressive or unfairly prejudicial to shareholders.

Takeovers matters

In December, we publicly censured Zhang Qiang for acquiring shares in Feishang Non-metal Materials Technology Limited within six months after the close of an offer at above the offer price in contravention of the Takeovers Code⁵.

Listings applications and takeovers activities

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
Listings applications	40	236	193	22.3
Takeovers and share buy-back transactions	99	339	356	-4.8

¹ The SFC may object to a listing of securities based on one or more of the grounds set out in section 6(2) of the Securities and Futures (Stock Market Listing) Rules. A letter of mindedness to object sets out the SFC’s substantive concerns along with detailed reasons.

² One of the return decisions was subsequently overturned by the Listing Committee.

³ The applicant can only submit a new listing application with a new application proof more than eight weeks after the return.

⁴ Section 179 of the Securities and Futures Ordinance gives the SFC the power to compel the production of records and documents from persons related to a listed company.

⁵ The Code on Takeovers and Mergers.

Market infrastructure and trading

Investor identification

We worked with the China Securities Regulatory Commission (CSRC) and Hong Kong Exchanges and Clearing Limited (HKEX) on the implementation of investor identification for Northbound trading under Stock Connect to facilitate market surveillance. On 30 November, HKEX issued an information paper, *Investor ID Model for Northbound Trading Under Stock Connect*, which provided market participants with the operational details of the regime in preparation for its launch in the third quarter of 2018. A similar regime for Southbound trading will be introduced as soon as possible after the regime for Northbound trading is implemented.

Futures markets cooperation

On 29 December, the SFC and the CSRC jointly announced that they entered into a Memorandum of Understanding¹ which facilitates regulatory and enforcement cooperation in the Mainland and Hong Kong futures markets and enhances supervisory assistance and information exchange on cross-boundary derivatives, futures exchanges and brokers and other matters.

Automated trading services

	As at 31.12.2017	As at 31.03.2017	Change (%)	As at 31.12.2016	YoY change (%)
Under Part III	52	49	6.1	49	6.1
Under Part V	24	24	0	24	0

Extension of after-hours trading session

In September, the SFC approved HKEX's proposal to extend trading of the Hang Seng Index and Hang Seng China Enterprises Index futures contracts (including mini contracts) during the after-hours trading session from 11:45 pm to 1:00 am the next day. The extended trading hours became effective on 6 November.

Iron ore futures contract

In September, the SFC approved the launch of a cash-settled, index-linked iron ore futures contract proposed by HKEX. Trading commenced on 13 November.

Automated trading services

As of 31 December, the number of automated trading services (ATS)² authorisations under Part III of the Securities and Futures Ordinance (SFO) was 52, while 24 corporations, including 16 dark pool operators, were licensed under Part V of the SFO to provide ATS.

¹ Memorandum of Understanding on Supervisory and Enforcement Cooperation on Matters concerning Futures.

² Under the SFO, two regimes regulate ATS providers. Typically, those that offer facilities similar to those of a traditional exchange or a clearing house are authorised under Part III of the SFO. Intermediaries which provide dealing services with ATS as an added facility are licensed under Part V of the SFO.

Enforcement

Securities and Futures Appeal Tribunal (SFAT)

The SFAT upheld our disciplinary action against HSBC Private Bank (Suisse) SA which was fined a record sum of \$400 million. The SFAT affirmed our findings that there were material systemic failures in the bank's sale and marketing of Lehman Brothers-related investment products.

Court proceedings

The Court of First Instance (CFI) dismissed a judicial review lodged by Tang Hanbo against our search warrant obtained for an ongoing investigation into suspected breaches of the Takeovers Code and suspected offences under the Securities and Futures Ordinance (SFO), and our subsequent transmission of some materials to the China Securities Regulatory Commission.

The Court of Appeal (CA) upheld the decision of the CFI which ruled in our favour in an insider dealing and fraud case brought against two solicitors, Betty Young Bik Fung and Eric Lee Kwok Wa, and Lee's two sisters. The CA ruled that the Hong Kong courts had jurisdiction to hear this case because a substantial measure of activities constituting the contravention took place in Hong Kong, and that the application of section 300 of the SFO¹ would not be limited to a case in which the counterparties in the securities transaction were the victims of the fraud. The significance of this ruling is that the SFC can now take action against insider dealings of securities listed outside Hong Kong, so long as a substantial measure of the constituting fraudulent acts are perpetrated in Hong Kong.

The CFI allowed our appeal against the Eastern Magistrates' Court's acquittal of Wong Hung and ordered that the case, of illegal short selling in the shares of five listed companies, be remitted to the Magistrates' Court for a re-trial by a different magistrate.

Disciplinary actions

We disciplined two corporations and five licensed representatives during the quarter.

Internal control failures

- FXCM Asia Limited² was reprimanded and fined \$2 million for regulatory breaches and internal control failures relating to under-segregation of client monies.
- Standard Chartered Securities (Hong Kong) Limited was reprimanded and fined \$2.6 million for internal control failures relating to short-selling orders.

Unauthorised trading

- Danny Fung Kwong Shing, a former account executive at Fulbright Securities Limited, was banned from re-entering the industry for life and fined over \$542,000 and Yeung Leung Yuen Marvin, a former relationship manager of Citibank (Hong Kong) Limited, was banned for three years, both for conducting unauthorised transactions in clients' accounts.

Breach of Code of Conduct³

- Ng Chau, a former account executive at Get Nice Securities Limited, was banned from re-entering the industry for six months for conducting transactions in a client's accounts without written authorisation.
- Abbie Yip Ka Ying, a former trader at BNP Paribas in Hong Kong, was banned for 18 months for her attempts to conceal a trade execution error.
- Xu Tao, a former investment consultant at China International Capital Corporation Hong Kong Securities Limited, was banned for four months for using his mobile phone and instant messaging to accept order instructions.

¹ Section 300 of the SFO prohibits the use of fraudulent or deceptive schemes in transactions involving securities listed in Hong Kong or overseas.

² Now known as Rakuten Securities Hong Kong Limited.

³ Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

Enforcement

Updated Guidance Note on Cooperation with the SFC

We issued an updated guidance note⁴ and a set of frequently-asked questions to highlight the benefits of cooperation in our investigation and enforcement proceedings⁵. The new measures are designed to encourage cooperative conduct to achieve timely and desirable enforcement outcomes.

Market surveillance

We made 1,644 requests for trading and account records from intermediaries in the quarter. In addition, we posted eight high shareholding concentration announcements on our website to remind investors to exercise caution when trading shares in companies where a small number of shareholders hold a high concentration of shares.

Enforcement activities

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
S179 ^a inquiries commenced	5	20	18	11.1
S181 ^b inquiries commenced (number of letters sent)	51 (1,644)	199 (6,561)	207 (6,488)	1.1
S182 ^c directions issued	55	203	313	-35.1
Investigations started	62	215	317	-32.2
Investigations completed	62	174	457	-61.9
Individuals/corporations charged in criminal proceedings	1	11	4	175
Criminal charges laid	2	44	15	193.3
Notices of Proposed Disciplinary Action ^d issued	6	22	42	-47.6
Notices of decision ^e issued	7	19	39	-51.3
Individuals/corporations subject to ongoing civil proceedings ^f	110	110	109	0.9
Compliance advice letters issued	53	215	409	-47.4
Cases with search warrants executed	4	19	24	-20.8

^a Section 179 of the SFO gives the SFC the power to compel the production of records and documents from persons related to a listed company in relation to fraud or other misconduct.

^b Section 181 of the SFO gives the SFC the power to require information from intermediaries about trading transactions, including information identifying the ultimate clients, the particulars and instructions relating to the transactions.

^c Section 182 of the SFO gives the SFC the power to investigate SFO offences, market misconduct, fraud, misfeasance and disciplinary misconduct.

^d A notice issued by the SFC to regulated persons that it proposes to exercise its disciplinary powers, on grounds that they appear to be guilty of misconduct or not fit and proper.

^e A notice that sets out the SFC's decision and its reasons to take disciplinary action against regulated persons.

^f As of the last day of the period.

⁴ The updated guidance note replaces the previous version issued in March 2006.

⁵ These include disciplinary proceedings under Part IX of the SFO, civil court proceedings initiated by the SFC under sections 213 or 214 of the SFO and Market Misconduct Tribunal proceedings initiated by the SFC under Parts XIII or XIVA of the SFO. The guidance note does not apply to criminal cases as the Department of Justice has unfettered discretion over criminal prosecutions.

Global regulatory engagement

IOSCO

We are actively involved in international policy making. Mr Ashley Alder, our Chief Executive Officer (CEO), chairs the Board of the International Organization of Securities Commissions (IOSCO) and we participate in all eight of its policy committees. We work closely with the IOSCO Secretariat to enhance the relevance of IOSCO's work to the Board and to the wider membership, to coordinate the policy work of IOSCO and the Financial Stability Board (FSB) and to promote interaction between members from emerging and developed economies.

Mr Alder chaired the IOSCO Board meeting in October which discussed European Union (EU) data privacy regulations, central counterparty risks, derivatives reforms and cyber resilience. The IOSCO Board also issued a statement to IOSCO members on the risks related to initial coin offerings.

We hosted the second EU-Asia Pacific Forum which was co-chaired by Mr Alder on 1 December in Hong Kong. Regulators representing the EU and IOSCO Asia-Pacific Regional Committee discussed cross-border regulatory issues arising out of EU regulations which have an impact on Hong Kong and the region, developments in sustainable finance, financial technologies (Fintech) and the cross-border implications of asset management and funds passporting.

Financial Stability Board

Mr Alder attended the FSB Plenary meeting in October which considered its 2018 work plan and discussed matters which may have an impact on financial stability, including cybersecurity, misconduct risks and market-based finance.

Mr Keith Lui, Executive Director, Supervision of Markets, attended the December meeting of the FSB Regional Consultative Group for Asia, which considered Fintech, macro-prudential policies and financial market integrity. We remained active in the FSB Standing Committee on Standards Implementation which considered the effects of reforms and discussed future thematic peer reviews.

We continued to work with the Hong Kong Monetary Authority, the Insurance Authority and the Government on the FSB peer review of Hong Kong and the FSB's annual monitoring exercise on shadow banking.

Mainland China

In November, together with Mr Paul Chan, Financial Secretary, and Mr James Lau, Secretary for Financial Services and the Treasury, we met with Mr Liu Shiyu, Chairman of China Securities Regulatory Commission (CSRC), in Beijing to discuss the development of Hong Kong's financial market and regulatory cooperation with the Mainland. We also received a high-level CSRC delegation to discuss ongoing cooperation between the two regulators.

During the quarter, we signed a Memorandum of Understanding (MoU) with the CSRC to enhance supervisory and enforcement cooperation in the futures markets. We also worked closely with the CSRC on the H-share full circulation pilot scheme.

We organised a case study training exercise with the CSRC in Xiamen in December. Investigators from both regulators shared their experiences in investigating fraudulent offerings, market manipulation and breaches of disclosure rules.

We also organised training programmes for senior executives from Mainland authorities to enhance their understanding of our regulatory work. During the quarter, we met with the People's Bank of China, State Administration of Foreign Exchange and China Foreign Exchange Trading System to discuss Mainland monetary policy and two-way capital flows.

In October, we participated in the 9th Meeting of the Expert Group on Guangdong-Hong Kong Financial Cooperation. In November, we attended the Beijing-Hong Kong Economic Cooperation Symposium and delivered a speech stressing the importance of cross-boundary regulatory cooperation between the Mainland and Hong Kong as well as opportunities presented by the Belt and Road initiative.

Global regulatory engagement

Other regulatory engagement

During the quarter, we participated in various international meetings including the Policy Standing Group and the Implementation Monitoring Standing Group established by the Committee on Payments and Market Infrastructures and IOSCO. We held meetings to discuss regulatory issues and market developments with overseas regulators, institutions and government representatives, including the US Securities and Exchange Commission, US Commodity Futures Trading Commission, European Commission, European Securities and Markets Authority, France Autorité des Marchés Financiers (AMF) and the International Monetary Fund. We also met with the Hong Kong Financial Reporting Council to discuss corporate governance and audit-related standards.

At the 9th MoU meeting with the Taiwan Financial Supervisory Commission in November, we discussed topics including anti-money laundering and Fintech regulation.

We maintained close contact with local and overseas regulatory counterparts to keep abreast of developments in emerging regulatory and financial technologies.

We also responded to various requests for technical assistance and training from overseas regulators and other authorities.

Stakeholder communication

We engage with a broad range of stakeholders in a proactive manner to provide timely regulatory updates and to help them better understand our work.

In December, we launched a public consultation on amendments to the Code on Unit Trusts and Mutual Funds. We also published a consultation paper on refinements to the over-the-counter derivatives regime and conduct requirements to address risks posed by financial exposures to group affiliates.

We concluded a consultation in October on proposals to reduce and mitigate hacking risks associated with internet trading and published new guidelines on the subject. In November, we released consultation conclusions on asset management regulation and point-of-sale transparency, together with a further consultation on disclosure requirements applicable to discretionary accounts.

On 25 October, our senior executives spoke at a full-day programme we organised with the Hong Kong Monetary Authority to discuss regulatory issues related to the development of financial technology (Fintech). The programme was part of Hong Kong Fintech Week sponsored by InvestHK.

Additionally, our senior executives spoke at 17 local and international conferences during the quarter to share our regulatory approach in several areas. We also supported six industry events.

In December, we published the first edition of the *SFC Compliance Bulletin: Intermediaries* using case studies identified in our recent on-site inspections and off-site monitoring to remind intermediaries and market practitioners of the importance of managing conflicts of interest in selling practices and asset management. The December issue of the *Takeovers Bulletin* discussed a recent public censure and provided an update on our takeovers work.

We issued 18 circulars informing industry participants about a wide range of matters, including securities margin financing, anti-money laundering, managing conflicts of interest in financial groups, establishing liquidity risk management practices to safeguard client assets and regulated activities involving cryptocurrency-related investment products and derivatives.

Publications and other communications

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016
Press releases	36	111	98
Consultation papers	3	8	4
Consultation conclusions	2	6	1
Industry-related publications	2	11	9
Codes and guidelines ¹	2	8	2
Circulars to industry	18	61	55
Corporate website average daily page views ²	63,992	67,825	57,455
General enquiries	1,784	5,354	4,671

¹ Includes updates to previous versions.

² The average number of web pages browsed per day during the reporting period.

Corporate Developments

The Financial Secretary reappointed Ms Mary Ma and Mr Lester Huang as Non-Executive Directors for two-year terms effective 15 November.

Our income for the quarter was \$530 million, 12% higher than the previous quarter. Average daily turnover in Hong Kong's securities market was \$110 billion in the quarter, 16% higher than the \$95 billion recorded in the previous quarter. Our expenditure was \$439 million, 2% lower than that in the last quarter. We recorded a surplus of \$91 million this quarter. At 31 December, our reserves stood at \$7 billion, of which \$3 billion was set aside for the possible future acquisition of office premises.

We concluded a study which established a new technology blueprint to centralise all electronic data submission in a new online portal and make the process more user-friendly. We also launched a new system to expedite alerts of suspected market misconduct for enforcement purposes and enhanced our system for managing the post-authorisation processing of investment products.

As of 31 December, we had 880 staff members, up from 867 a year ago.

Finances

(\$ million)	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
Income	530	1,429	943	52%
Expenses including depreciation	439	1,310	1,269	3%
Surplus / (loss)	91	119	(326)	N/A

Activity Data

Table 1 Breaches noted during on-site inspections

Nature of breaches	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016 ¹	YoY change (%)
Failure to comply with Securities and Futures (Financial Resources) Rules	3	8	9	-11.1
Failure to safekeep client securities	13	34	42	-19
Failure to maintain proper books and records	7	25	29	-13.8
Failure to safekeep client money	14	46	47	-2.1
Unlicensed dealing and other registration issues	4	15	12	25
Breach of licensing conditions	2	7	4	75
Breach of requirements of contract notes/statements of account/receipts	15	47	64	-26.6
Failure to make filing/notification	0	1	5	-80
Breach of margin requirements	1	4	4	0
Marketing malpractices	0	0	1	-100
Illegal short selling of securities	0	0	0	0
Dealing malpractices	2	2	7	-71.4
Breach of Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ²	79	252	359	-29.8
Breach of Corporate Finance Adviser Code of Conduct	0	5	16	-68.8
Breach of Fund Manager Code of Conduct	23	73	52	40.4
Breach of regulation of online trading	1	4	7	-42.9
Non-compliance with anti-money laundering guidelines	56	128	168	-23.8
Breach of other rules and regulations of the Exchanges ³	3	9	12	-25
Breach of other rules and regulations of the Mandatory Provident Fund Schemes Authority	0	0	0	0
Internal control weaknesses ⁴	127	374	461	-18.9
Others	29	61	61	0
Total	379	1,095	1,360	-19.5

¹ Adjustments have been made for the period.

² Commonly related to risk management, record keeping, client agreements, safeguarding of client assets and management responsibilities.

³ The Stock Exchange of Hong Kong Limited and Hong Kong Futures Exchange Limited.

⁴ Deficiencies in management review and supervision, operational controls over the handling of client accounts, segregation of duties, information management and adequacy of audit trail for internal control purposes, among other weaknesses.

Activity Data

Table 2 Authorised unit trusts and mutual funds – by type

	Number as at 31.12.2017	Number as at 31.3.2017	Change (%)	Number as at 31.12.2016	YoY change (%)
Bond	441	430	2.6	425	3.8
Equity	1,029	1,018	1.1	1,028	0.1
Diversified	168	162	3.7	161	4.3
Money market	45	44	2.3	44	2.3
Fund of funds	117	113	3.5	113	3.5
Index ¹	155	182	-14.8	170	-8.8
Guaranteed	4	3	33.3	3	33.3
Hedge	1	2	-50	2	-50
Other specialised ²	5	7	-28.6	10	-50
Sub-total	1,965	1,961	0.2	1,956	0.5
Umbrella structures	240	242	-0.8	240	0
Total	2,205	2,203	0.1	2,196	0.4

¹ Including leveraged and inverse products.

² Including futures and options funds, structured funds and funds which invest in financial derivative instruments.

Table 3 Authorised unit trusts and mutual funds – by type and assets under management

	Total NAV (US\$ million) as at 31.12.2017	Total NAV (US\$ million) as at 31.3.2017	Change (%)	Total NAV (US\$ million) as at 31.12.2016	YoY change (%)
Bond	573,417	466,096 ¹	23	438,219	30.9
Equity	772,060	638,848	20.9	599,102	28.9
Diversified	171,133	137,454	24.5	120,538	42
Money market	20,920	21,014	-0.4	20,076	4.2
Fund of funds	22,850	19,865	15	18,530	23.3
Index ²	99,742	92,069	8.3	86,165	15.8
Guaranteed	116	127	-8.7	64	81.3
Hedge	26	28	-7.1	29	-10.3
Other specialised ³	1,060	1,288	-17.7	1,380 ⁴	-23.2
Total	1,661,324	1,376,789¹	20.7	1,284,104^{4, 5}	29.4

¹ These figures differ from those disclosed in the *Annual Report 2016-17* and the *Quarterly Report April-June 2017* due to revised figures reported after those reports' issuance.

² Including leveraged and inverse products.

³ Including futures and options funds, structured funds and funds which invest in financial derivative instruments.

⁴ These figures differ from those disclosed in the *Quarterly Report October-December 2016* due to revised figures reported after that report's issuance.

⁵ Figure does not add up to total due to rounding.

Activity Data

Table 4 Authorised unit trusts and mutual funds – by origin

	Number as at 31.12.2017	Number as at 31.3.2017	Change (%)	Number as at 31.12.2016	YoY change (%)
Hong Kong	755	735	2.7	707 ¹	6.8
Luxembourg	1,023	1,009	1.4	1,008	1.5
Ireland	247	256	-3.5	264	-6.4
United Kingdom	69	64	7.8	69	0
Mainland China	50	49	2	48	N/A
Other Europe	3	3 ²	0	3	N/A
Bermuda	3	5	-40	5	-40
Cayman Islands	47	74	-36.5	84 ¹	-44
Others	8	8 ²	0	8	0
Total	2,205	2,203	0.1	2,196	0.4

¹ These figures differ from those disclosed in the *Quarterly Report October-December 2016* due to the re-categorisation of funds' places of origin after that report's issuance.

² These figures differ from those disclosed in the *Annual Report 2016-17* due to different categorisation of funds' places of origin.

Table 5 Authorised unit trusts and mutual funds – by origin and assets under management

	Total NAV (US\$ million) as at 31.12.2017	Total NAV (US\$ million) as at 31.3.2017	Change (%)	Total NAV (US\$ million) as at 31.12.2016	YoY change (%)
Hong Kong	159,247	131,605	21	122,732 ¹	29.8
Luxembourg	1,085,333	910,351	19.2	850,708	28
Ireland	235,916	173,212 ²	36.2	155,488	51.7
United Kingdom	108,609	90,987	19.4	90,499	20
Mainland China	20,438	17,056	19.8	15,406	32.7
Other Europe	122	94 ³	29.8	87	40.2
Bermuda	194	217	-10.6	230	-15.7
Cayman Islands	8,507	11,546	-26.3	11,161 ⁴	-24
Others	42,958	41,721 ³	3	37,793	13.7
Total	1,661,324	1,376,789	20.7	1,284,104⁵	29.4

¹ This figure differs from that disclosed in the *Quarterly Report October-December 2016* due to the re-categorisation of funds' places of origin after that report's issuance.

² These figures differ from those disclosed in the *Annual Report 2016-17* and the *Quarterly Report April-June 2017* due to revised figures reported after those reports' issuance.

³ These figures differ from those disclosed in the *Annual Report 2016-17* due to the different categorisation of funds' places of origin.

⁴ This figure differs from that disclosed in the *Quarterly Report October-December 2016* due to a revised figure reported and the re-categorisation of funds' places of origin after that report's issuance.

⁵ See footnotes 1 and 4.

Activity Data

Table 6 Takeovers activities

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
Codes on Takeovers and Mergers and Share Buy-backs				
General and partial offers under Code on Takeovers and Mergers	17	49	56	-12.5
Privatisations	1	10	10	0
Whitewash waiver applications	12	35	26	34.6
Other applications under Code on Takeovers and Mergers ¹	68	244	260	-6.2
Off-market and general offer share buy-backs	1	1	2	-50
Other applications under Code on Share Buy-backs ¹	0	0	2	-100
Total	99	339	356	-4.8
Executive Statements				
Sanctions imposed with parties' agreement ²	1	4	4	0
Takeovers and Mergers Panel				
Meetings for review of Codes on Takeovers and Mergers and Share Buy-backs	1	1	0	0
Hearings before the Panel (disciplinary and non-disciplinary)	0	1	2	-50
Statements issued by the Panel ³	0	1	2	-50

¹ Including stand-alone applications and those made during the course of a code-related transaction.

² Pursuant to section 12.3 of the Introduction to the Codes on Takeovers and Mergers and Share Buy-backs.

³ Pursuant to section 16.1 of the Introduction to the Codes on Takeovers and Mergers and Share Buy-backs.

Table 7 Complaints against intermediaries and market activities

	Quarter ended 31.12.2017	Nine months ended 31.12.2017	Nine months ended 31.12.2016	YoY change (%)
Conduct of licensees	85	248	278	-10.8
Conduct of registered institutions	6	17	32	-46.9
Listed companies and disclosure of interests	197	593	571	3.9
Market misconduct ¹	105	227	154	47.4
Product disclosure	4	7	7	0
Unlicensed activities	44	102	92	10.9
Breach of offers of investments	8	43	79	-45.6
Boiler rooms and suspicious websites	69	231	223	3.6
Scams and frauds ²	37	111	104	6.7
Other financial activities ³	112	260	168	54.8
Total	667	1,839	1,708	7.7

¹ Primarily, alleged market manipulation and insider dealing.

² Such as identity fraud and impersonation.

³ For example, bullion trading and banking services.

Securities and Futures Commission

Condensed consolidated statement of profit or loss and other comprehensive income

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited Nine months ended		Unaudited Three months ended	
		31 Dec 2017 \$'000	31 Dec 2016 \$'000	31 Dec 2017 \$'000	31 Dec 2016 \$'000
Income					
Levies		1,019,101	744,321	390,758	242,102
Fees and charges		120,278	105,992	45,662	37,900
Investment income		271,939	91,901	90,638	3,696
Less : custody and advisory expenses		(5,726)	(4,220)	(1,984)	(1,537)
Investment income net of third party expenses		266,213	87,681	88,654	2,159
Recoveries from the Investor Compensation Fund		4,314	4,133	1,431	1,353
Other income		18,490	452	3,350	11
		1,428,396	942,579	529,855	283,525
Expenses					
Staff costs and directors' emoluments	8(b)	961,033	903,634	318,721	301,679
Premises					
rent		154,209	156,333	49,807	52,411
rates, management fees and others		36,036	37,305	11,147	12,474
Other expenses		136,802	137,692	51,981	51,486
Depreciation		21,810	33,485	7,635	12,140
		1,309,890	1,268,449	439,291	430,190
Surplus / (deficit) and total comprehensive income for the period		118,506	(325,870)	90,564	(146,665)

The notes on pages 26 to 28 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Condensed consolidated statement of financial position

At 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Non-current assets			
Fixed assets		63,598	63,455
Held-to-maturity debt securities	2	878,000	–
		941,598	63,455
Current assets			
Held-to-maturity debt securities	2	–	30,003
Financial assets designated at fair value through profit or loss			
Debt securities		767,066	716,403
Pooled funds		1,053,367	941,911
Debtors, deposits and prepayments		182,935	158,450
Fixed deposits with banks		4,344,250	5,107,808
Cash at bank and in hand		46,676	75,462
		6,394,294	7,030,037
Current liabilities			
Fees received in advance		8,011	9,210
Creditors and accrued charges		247,704	128,218
		255,715	137,428
Net current assets		6,138,579	6,892,609
Total assets less current liabilities		7,080,177	6,956,064
Non-current liabilities	4	39,771	34,164
Net assets		7,040,406	6,921,900
Funding and reserves			
Initial funding by Government		42,840	42,840
Reserve for property acquisition		3,000,000	3,000,000
Accumulated surplus		3,997,566	3,879,060
		7,040,406	6,921,900

The notes on pages 26 to 28 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Condensed statement of financial position

At 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Non-current assets			
Fixed assets		63,483	63,167
Held-to-maturity debt securities	2	878,000	–
		941,483	63,167
Current assets			
Held-to-maturity debt securities	2	–	30,003
Financial assets designated at fair value through profit or loss			
Debt securities		767,066	716,403
Pooled funds		1,053,367	941,911
Debtors, deposits and prepayments		189,261	158,516
Fixed deposits with banks		4,344,250	5,107,808
Cash at bank and in hand		31,131	71,262
		6,385,075	7,025,903
Current liabilities			
Fees received in advance		8,011	9,210
Creditors and accrued charges		238,370	123,796
		246,381	133,006
Net current assets		6,138,694	6,892,897
Total assets less current liabilities		7,080,177	6,956,064
Non-current liabilities	4	39,771	34,164
Net assets		7,040,406	6,921,900
Funding and reserves			
Initial funding by Government		42,840	42,840
Reserve for property acquisition		3,000,000	3,000,000
Accumulated surplus		3,997,566	3,879,060
		7,040,406	6,921,900

The notes on pages 26 to 28 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Condensed consolidated statement of changes in equity

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Initial funding by Government \$'000	Unaudited		Total \$'000
		Reserve for property acquisition \$'000	Accumulated surplus \$'000	
Balance at 1 April 2016	42,840	–	7,234,700	7,277,540
Transfer to reserve for property acquisition	–	3,000,000	(3,000,000)	–
Loss and total comprehensive income for the period	–	–	(325,870)	(325,870)
Balance at 31 December 2016	42,840	3,000,000	3,908,830	6,951,670
Balance at 1 April 2017	42,840	3,000,000	3,879,060	6,921,900
Surplus and total comprehensive income for the period	–	–	118,506	118,506
Balance at 31 December 2017	42,840	3,000,000	3,997,566	7,040,406

Highlights

Operational Review

Corporate Developments

Activity Data

Financial Statements

The notes on pages 26 to 28 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Condensed consolidated statement of cash flows

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited Nine months ended	
		31 Dec 2017 \$'000	31 Dec 2016 \$'000
Cash flows from operating activities			
Surplus / (deficit) for the period		118,506	(325,870)
Adjustments for :			
Depreciation		21,810	33,281
Investment income		(271,939)	(91,901)
Exchange difference		(10,293)	1,819
Loss on disposal of fixed assets		719	7
		(141,197)	(382,664)
(Increase) / decrease in debtors, deposits and prepayments		(20,111)	453
Increase in creditors and accrued charges		119,486	112,890
Decrease in fees received in advance		(1,199)	(765)
Increase in non-current liabilities		5,607	5,575
<i>Net cash used in operating activities</i>		(37,414)	(264,511)
Cash flows from investing activities			
Decrease / (increase) in fixed deposits other than cash and cash equivalents		1,091,420	(636,644)
Interest received		61,417	49,951
Held-to-maturity debt securities purchased		(879,337)	-
Held-to-maturity debt securities redeemed at maturity		30,000	460,553
Debt securities designated at fair value through profit or loss purchased		(487,785)	(1,267,501)
Debt securities designated at fair value through profit or loss sold or redeemed		438,565	502,830
Pooled funds purchased		-	(155,133)
Pooled funds sold		104,882	1,824
Fixed assets purchased		(22,672)	(24,009)
<i>Net cash generated from / (used in) investing activities</i>		336,490	(1,068,129)
Net increase / (decrease) in cash and cash equivalents		299,076	(1,332,640)
Cash and cash equivalents at beginning of the nine-month period		676,727	1,522,116
Cash and cash equivalents at end of the nine-month period	3	975,803	189,476

Analysis of the balance of cash and cash equivalents

	Unaudited	
	At 31 Dec 2017 \$'000	At 31 Dec 2016 \$'000
Fixed deposits with banks	929,127	149,856
Cash at bank and in hand	46,676	39,620
	975,803	189,476

The notes on pages 26 to 28 form part of the condensed consolidated financial statements.

Securities and Futures Commission

Notes to the condensed consolidated financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

1. Basis of preparation

We have prepared the condensed consolidated interim financial information in accordance with Hong Kong Accounting Standard (HKAS) 34, *Interim financial reporting* adopted by the Hong Kong Institute of Certified Public Accountants (HKICPA).

This condensed consolidated interim financial information contains condensed consolidated financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the SFC since the annual financial statements for the year ended 31 March 2017. The condensed consolidated interim financial statements and notes thereon do not include all of the information required for full set of financial statements prepared in accordance with Hong Kong Financial Reporting Standards (HKFRSs).

The condensed consolidated interim financial information is unaudited and the financial information relating to the financial year ended 31 March 2017 included in this report does not constitute the SFC's statutory annual financial statements for that financial year but is derived from those financial statements.

We consolidated the financial results of the Investor Compensation Company Limited (ICC) and Investor Education Centre (IEC) in the SFC's condensed financial statements made up to 31 December 2017. We eliminated all material intragroup balances and transactions in preparing the condensed consolidated financial statements. We have applied the same accounting policies adopted in the consolidated financial statements for the year ended 31 March 2017 to the condensed consolidated interim financial information.

There were no significant changes in the operations of the SFC for the nine months ended 31 December 2017.

2. Held-to-maturity debt securities

As of 31 December 2017, the total carrying cost of held-to-maturity debt securities amounted to \$878,000,000 (at 31 March 2017: \$30,003,000), with a market value of \$869,091,000 (at 31 March 2017: \$30,006,000).

3. Cash and cash equivalents

Reconciliation with the condensed consolidated statement of financial position

	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Cash at bank and in hand	46,676	75,462
Fixed deposits with banks	4,344,250	5,107,808
Amounts shown in the condensed consolidated statement of financial position	4,390,926	5,183,270
Less : Amounts with an original maturity of beyond three months	(3,415,123)	(4,506,543)
Cash and cash equivalents in the consolidated statement of cash flows	975,803	676,727

4. Non-current liabilities

Non-current liabilities represent deferred lease incentives and provision for premises reinstatement cost. Deferred lease incentives consist of incentives granted by our landlord in connection with the lease of our office premises. We recognise the deferred lease incentives in our condensed consolidated statement of profit or loss and other comprehensive income on a straight line basis over the lease period ranging from 2017 to 2020 as an integral part of rental expense.

Securities and Futures Commission

Notes to the condensed consolidated financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

5. Ageing analysis of debtors and creditors

There was no material overdue debtor balance and creditor balance included in "debtors, deposits and prepayments" and "creditors and accrued charges" respectively as at 31 December 2017. Therefore we do not provide an ageing analysis of debtors and creditors.

6. Exchange fluctuation

The SFC's investment guidelines for our investment portfolio only allow investments in assets denominated in Hong Kong dollars, US dollars and renminbi. Exposure in renminbi should not exceed 5% of the investment portfolio. As the majority of the financial assets are denominated in either US dollars or Hong Kong dollars which are closely pegged, we do not consider we are exposed to significant exchange rate risk.

7. Investments in subsidiaries

The SFC formed the ICC on 11 September 2002 with an issued share capital of \$0.2. On 20 November 2012, the SFC launched the IEC as a company limited by guarantee and not having a share capital. Both companies are wholly owned subsidiaries of the SFC and are incorporated in Hong Kong.

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

The objective of the IEC is to improve the financial knowledge and capability of the general public and to assist them in making informed financial decisions.

As at 31 December 2017, the investment in subsidiaries, which is stated at cost less any impairment losses, amounted to \$0.2 (at 31 March 2017: \$0.2). The balance is too small to appear on the condensed statement of financial position which is expressed in thousands of dollars.

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

8. Related party transactions

We have related party relationships with the ICF, the Unified Exchange Compensation Fund, the Securities Ordinance (Chapter 333) - Dealers' Deposits Fund, the Commodities Trading Ordinance (Chapter 250) - Dealers' Deposits Fund and the Securities Ordinance (Chapter 333) - Securities Margin Financiers' Security Fund. In addition to the transactions and balances disclosed elsewhere in these financial statements, the Group entered into the following material related party transactions:

- (a) During the period, we received reimbursement from the ICF for all the ICC's expenses amounting to \$4,314,000 (2016: \$4,133,000), which is in accordance with section 242(1) of the SFO. As at 31 December 2017, the amount due to the ICF from the ICC was \$172,000 (at 31 March 2017: \$75,000).

Securities and Futures Commission

Notes to the condensed consolidated financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

8. Related party transactions (cont'd)

(b) Remuneration for key management personnel comprised:

	Unaudited Nine months ended	
	31 Dec 2017 \$'000	31 Dec 2016 \$'000
Directors' fees and salaries, allowances and benefits in kind	24,264	23,354
Retirement scheme contributions	2,218	2,092
	26,482	25,446

The total remuneration is included in "staff costs and directors' emoluments" on page 21. Discretionary pay is not included above as the decision to pay is subject to the approval process towards the end of the financial year and therefore is not determined until then.

9. Commitment to pay rents for offices

At 31 December 2017 the minimum amount we are committed to pay in rent for our offices up to 31 August 2020, being the rent review date as set out in the lease agreements, are as follows:

	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Payable next year	200,617	205,077
Payable in one to five years	334,199	477,534
Payable in more than five years	–	–
	534,816	682,611

During the period, \$154,209,000 net of lease incentives, was recognised as an expense in the condensed consolidated statement of profit or loss and other comprehensive income in respect of operating leases (2016: \$156,333,000).

Investor Compensation Fund

Report of the Investor Compensation Fund Committee

The members of the Investor Compensation Fund Committee (the Committee) present their quarterly report and the unaudited condensed financial statements for the nine months ended 31 December 2017.

Establishment of the Investor Compensation Fund

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

Financial statements

The financial performance of the Fund for the reporting period ended 31 December 2017 and the financial position of the Fund as at that date are set out in the unaudited condensed financial statements on pages 30 to 35.

Members of the Committee

The members of the Committee during the nine months ended 31 December 2017 and up to the date of this report were:

Mr Keith Lui (Chairman)

Ms Teresa Ko Yuk-yin, JP

Mr Lee Kwok Keung

Mr Thomas Allan Atkinson

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 end of the reporting period or at any time during the nine months.

On behalf of the Committee

Keith Lui
Chairman

20 February 2018

Investor Compensation Fund

Condensed statement of profit or loss and other comprehensive income

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited Nine months ended		Unaudited Three months ended	
		31 Dec 2017 \$'000	31 Dec 2016 \$'000	31 Dec 2017 \$'000	31 Dec 2016 \$'000
Income					
Net investment income		80,346	26,092	23,249	(28,438)
Exchange difference		9,836	(736)	1,413	(576)
Recovery income		–	1	–	1
		90,182	25,357	24,662	(29,013)
Expenses					
Investor Compensation Company Limited expenses	2	4,314	4,133	1,431	1,353
Compensation expenses	3	–	6	–	11
Auditor's remuneration		132	127	33	33
Bank charges		727	727	248	245
Professional fees		3,097	2,879	1,041	964
		8,270	7,872	2,753	2,606
Surplus/ (loss) and total comprehensive income for the period					
		81,912	17,485	21,909	(31,619)

Highlights

Operational Review

Corporate Developments

Activity Data

Financial Statements

The notes on page 34 to 35 form part of the condensed financial statements.

Investor Compensation Fund

Condensed statement of financial position

At 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Current assets			
Financial assets designated at fair value through profit or loss			
Debt securities		1,983,317	1,893,248
Pooled fund		351,630	330,386
Interest receivable		14,514	13,651
Due from Investor Compensation Company Limited		172	75
Fixed deposits with banks		11,407	26,201
Cash at bank		2,967	18,770
		2,364,007	2,282,331
Current liabilities			
Provision for compensation	3	300	476
Creditors and accrued charges		1,389	1,449
		1,689	1,925
Net current assets			
		2,362,318	2,280,406
Net assets			
		2,362,318	2,280,406
Representing :			
Compensation fund			
Contributions from Unified Exchange Compensation Fund		994,718	994,718
Contributions from Commodity Exchange Compensation Fund		108,923	108,923
Accumulated surplus		1,258,677	1,176,765
		2,362,318	2,280,406

The notes on page 34 to 35 form part of the condensed financial statements.

Investor Compensation Fund

Condensed statement of changes in equity

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Unaudited			Total \$'000
	Contributions from Unified Exchange Compensation Fund \$'000	Contributions from Commodity Exchange Compensation Fund \$'000	Accumulated surplus \$'000	
Balance at 1 April 2016	994,718	108,923	1,107,238	2,210,879
Surplus and total comprehensive income for the period	–	–	17,485	17,485
Balance at 31 December 2016	994,718	108,923	1,124,723	2,228,364
Balance at 1 April 2017	994,718	108,923	1,176,765	2,280,406
Surplus and total comprehensive income for the period	–	–	81,912	81,912
Balance at 31 December 2017	994,718	108,923	1,258,677	2,362,318

The notes on page 34 to 35 form part of the condensed financial statements.

Investor Compensation Fund

Condensed statement of cash flows

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Unaudited Nine months ended	
	31 Dec 2017 \$'000	31 Dec 2016 \$'000
Cash flows from operating activities		
Surplus for the period	81,912	17,485
Adjustments for:		
Net investment income	(80,346)	(26,092)
Exchange difference	(9,836)	736
	(8,270)	(7,871)
Increase in amount due from Investor Compensation Company Limited	(97)	(261)
Decrease in provision for compensation	(176)	(1,073)
(Decrease)/increase in creditors and accrued charges	(60)	68
<i>Net cash used in operating activities</i>	(8,603)	(9,137)
Cash flows from investing activities		
Purchase of debt securities	(919,710)	(407,885)
Sale or maturity of debt securities	825,678	341,989
Sale of equity securities	36,356	1,081
Interest received	35,682	35,509
<i>Net cash used in investing activities</i>	(21,994)	(29,306)
Net decrease in cash and cash equivalents	(30,597)	(38,443)
Cash and cash equivalents at beginning of the nine-month period	44,971	50,963
Cash and cash equivalents at end of the nine-month period	14,374	12,520

Analysis of the balance of cash and cash equivalents

	Unaudited	
	At 31 Dec 2017 \$'000	At 31 Dec 2016 \$'000
Fixed deposits with banks	11,407	9,195
Cash at bank	2,967	3,325
	14,374	12,520

The notes on page 34 to 35 form part of the condensed financial statements.

Investor Compensation Fund

Notes to the condensed financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

1. Basis of preparation

The Fund has prepared the condensed interim financial information in accordance with Hong Kong Accounting Standard (HKAS) 34, *Interim financial reporting* adopted by the Hong Kong Institute of Certified Public Accountants (HKICPA).

This condensed interim financial information contains condensed financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Fund since the annual financial statements for the year ended 31 March 2017. The condensed interim financial statements and notes thereon do not include all of the information required for full set of financial statements prepared in accordance with Hong Kong Financial Reporting Standards (HKFRSs).

The condensed interim financial information is unaudited and the financial information relating to the financial year ended 31 March 2017 included in this report does not constitute the Fund's statutory annual financial statements for that financial year but is derived from those financial statements.

We have applied the same accounting policies adopted in the financial statements for the year ended 31 March 2017 to the condensed interim financial information.

There were no significant changes in the operations of the Fund for the nine months ended 31 December 2017.

2. Investor Compensation Company Limited expenses

The Securities and Futures Commission (SFC) formed the Investor Compensation Company Limited (ICC) in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the Securities and Futures Ordinance (SFO). The Fund is responsible for funding the establishment and operation of the ICC. For the nine months ended 31 December 2017, the ICC incurred \$4,314,000 for its operations (for the nine months ended 31 December 2016: \$4,133,000).

3. Provision for compensation

	\$'000
Balance as at 1 April 2016	1,412
Add: compensation expenses during the year ended 31 March 2017	476
Less: compensation write-backs during the year ended 31 March 2017	(294)
Less: compensation paid during the year ended 31 March 2017	(1,118)
Balance as at 31 March 2017 and 1 April 2017	476
Less: compensation paid during the nine months ended 31 December 2017	(176)
Balance as at 31 December 2017	300

As at 31 December 2017, the provision for compensation relates to a number of claims received in respect of two default cases. The maximum liability of the Fund to claims for these cases is set at \$150,000 per claimant. The provision for compensation at 31 December 2017 was \$300,000 (31 March 2017: \$476,000). As at 31 December 2017, all provisions were expected to be paid within one year.

Investor Compensation Fund

Notes to the condensed financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

4. Material related party transactions

We have related party relationships with the SFC, the ICC and the Unified Exchange Compensation Fund. There were no significant related party transactions other than those disclosed in the condensed interim financial information of the Fund for the nine months ended 31 December 2016 and 2017.

5. Contingent liabilities

As at the date of this report, in addition to the provision made as described in note 3, there are other claims received for which currently there is insufficient information to determine the likely level of payment. The maximum liability of these claims is \$2,258,000 (31 March 2017: \$2,558,000). This is determined based on the lower of the maximum compensation limit of \$150,000 per claimant or the amount claimed.

Unified Exchange Compensation Fund

Report of the Securities Compensation Fund Committee

The members of the Securities Compensation Fund Committee (the Committee) present their quarterly report and the unaudited condensed financial statements for the nine months ended 31 December 2017.

Establishment of the Unified Exchange Compensation Fund

Part X of the repealed Securities Ordinance (Chapter 333) established the Unified Exchange Compensation Fund (the Fund). However, when the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect on 1 April 2003, a new single Investor Compensation Fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. Up to 31 December 2017, the Fund transferred \$994,718,000 to the ICF. After settlement of all claims against the Fund and its other liabilities, the Securities and Futures Commission (SFC) will eventually transfer the remaining balance of the Fund to the ICF.

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

Financial statements

The financial performance of the Fund for the reporting period ended 31 December 2017 and the financial position of the Fund as at that date are set out in the financial statements on pages 37 to 42.

Members of the Committee

The members of the Committee during the nine months ended 31 December 2017 and up to the date of this report were:

Mr Keith Lui (Chairman)
 Ms Mak Po Shuen
 Ms Teresa Ko Yuk-yin, JP
 Mr Lee Kwok Keung
 Mr Thomas Allan Atkinson

Interests in contracts

No contract of significance to which the Fund was a party and in which a Committee member of the Fund had a material interest, subsisted at the end of the reporting period or at any time during the nine months.

On behalf of the Committee

Keith Lui
 Chairman

5 February 2018

Unified Exchange Compensation Fund

Condensed statement of profit or loss and other comprehensive income

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Unaudited Nine months ended		Unaudited Three months ended	
	31 Dec 2017 \$'000	31 Dec 2016 \$'000	31 Dec 2017 \$'000	31 Dec 2016 \$'000
Income				
Interest income	456	375	164	129
Expenses				
Recoveries re-distributed	–	1,152	–	–
Auditors' remuneration	63	60	14	14
Sundry expenses	–	3	–	–
	63	1,215	14	14
Surplus/(loss) and total comprehensive income for the period	393	(840)	150	115

Highlights

Operational Review

Corporate Developments

Activity Data

Financial Statements

The notes on pages 41 to 42 form part of the condensed financial statements.

Unified Exchange Compensation Fund

Condensed statement of financial position

At 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Current assets			
Equity securities received under subrogation	2	1	1
Interest receivable		80	77
Accounts receivable		59	-
Fixed deposits with banks		85,708	83,744
Cash at bank		563	332
		86,411	84,154
Current liabilities			
Creditors and accrued charges		10,327	10,663
Relinquished trading rights payable to SEHK	4	700	600
		11,027	11,263
Net current assets			
		75,384	72,891
Net assets			
		75,384	72,891
Representing :			
Compensation fund			
Contributions from SEHK	4	53,300	51,200
Excess transaction levy from SEHK		353,787	353,787
Special contribution		3,500	3,500
Additional contribution from SEHK		300,000	300,000
Additional contribution from the SFC		330,000	330,000
Special levy surplus		3,002	3,002
Accumulated surplus		26,513	26,120
		1,070,102	1,067,609
Contributions to Investor Compensation Fund		(994,718)	(994,718)
		75,384	72,891

The notes on pages 41 to 42 form part of the condensed financial statements.

Unified Exchange Compensation Fund

Condensed statement of changes in equity

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Unaudited						Total
	Contributions from SEHK \$'000	Excess transaction levy from SEHK \$'000	Special contributions and special levy surplus \$'000	Additional contributions from SEHK and the SFC \$'000	Accumulated surplus \$'000	Contributions to Investor Compensation Fund \$'000	\$'000
Balance at 1 April 2016	49,050	353,787	6,502	630,000	26,790	(994,718)	71,411
Net contributions from SEHK	1,500	-	-	-	-	-	1,500
Loss and total comprehensive income for the period	-	-	-	-	(840)	-	(840)
Balance at 31 December 2016	50,550	353,787	6,502	630,000	25,950	(994,718)	72,071
Balance at 1 April 2017	51,200	353,787	6,502	630,000	26,120	(994,718)	72,891
Net contributions from SEHK	2,100	-	-	-	-	-	2,100
Surplus and total comprehensive income for the period	-	-	-	-	393	-	393
Balance at 31 December 2017	53,300	353,787	6,502	630,000	26,513	(994,718)	75,384

Highlights

Operational Review

Corporate Developments

Activity Data

Financial Statements

The notes on pages 41 to 42 form part of the condensed financial statements.

Unified Exchange Compensation Fund

Condensed statement of cash flows

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

	Note	Unaudited Nine months ended	
		31 Dec 2017 \$'000	31 Dec 2016 \$'000
Cash flows from operating activities			
Surplus/(loss) for the period		393	(840)
Adjustments for:			
Interest income		(456)	(375)
		(63)	(1,215)
Increase in accounts receivable		(59)	-
(Decrease)/increase in creditors and accrued charges		(336)	478
Increase/(decrease) in relinquished trading rights payable to SEHK		100	(200)
<i>Net cash used in operating activities</i>		(358)	(937)
Cash flows from investing activities			
Increase in fixed deposits other than cash and cash equivalents		(20,891)	-
Interest received		453	376
<i>Net cash (used in)/generated from investing activities</i>		(20,438)	376
Cash flows from financing activities			
Net contributions from SEHK		2,100	1,500
<i>Net cash generated from financing activities</i>		2,100	1,500
Net (decrease)/increase in cash and cash equivalents		(18,696)	939
Cash and cash equivalents at beginning of the nine-month period		84,076	82,457
Cash and cash equivalents at end of the nine-month period	3	65,380	83,396

Analysis of the balance of cash and cash equivalents

	Unaudited	
	At 31 Dec 2017 \$'000	At 31 Dec 2016 \$'000
Fixed deposits with banks	64,817	83,303
Cash at bank	563	93
	65,380	83,396

The notes on pages 41 to 42 form part of the condensed financial statements.

Unified Exchange Compensation Fund

Notes to the condensed financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

1. Basis of preparation

The Fund has prepared the condensed interim financial information in accordance with Hong Kong Accounting Standard (HKAS) 34, *Interim financial reporting* adopted by the Hong Kong Institute of Certified Public Accountants. As the Fund will eventually cease operation as a result of the Securities and Futures Ordinance which came into effect from 1 April 2003, the Fund has prepared the condensed interim financial information on a non-going concern basis. We expect that the operations of the Fund will be maintained until all claims and recoveries from liquidators in relation to the broker defaults that happened on or before 31 March 2003 have been fully settled.

This condensed interim financial information contains condensed financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Fund since the annual financial statements for the year ended 31 March 2017. The condensed interim financial statements and notes thereon do not include all of the information required for full set of financial statements prepared in accordance with Hong Kong Financial Reporting Standards (HKFRSs).

The condensed interim financial information is unaudited and the financial information relating to the financial year ended 31 March 2017 included in this report does not constitute the Fund's statutory annual financial statements for that financial year but is derived from those financial statements.

We have applied the same accounting policies adopted in the financial statements for the year ended 31 March 2017 to this condensed interim financial information.

There were no significant changes in the operations of the Fund for the nine months ended 31 December 2017.

2. Equity securities received under subrogation

In relation to the share distribution from C.A. Pacific Securities Ltd. and C.A. Pacific Finance Ltd., the liquidators had advised the SFC that shares were allocated to the Fund under its subrogation rights, subject to paying a processing fee to the liquidators. The Fund recognised as recoveries the payments from liquidators, the sale proceeds of shares allocated and the remaining shares at market value as of 31 December 2017 after deducting relevant processing fees and charges for collecting and selling the shares received.

The shares allocated to the Fund under its subrogation rights are classified as designated at fair value through profit and loss securities in accordance with the determination in HKAS 39, *Fair value measurement*. According to HKFRS 13, *Financial Instruments: Recognition and measurement*, these subrogated shares shall be classified as level 1 financial instruments as they all have quoted market price (unadjusted) in an active market for an identical instrument. At the end of each reporting period the fair value is remeasured, with any resultant gain or loss being recognised in "Recoveries". Dividend income, if any, is also recognised in "Recoveries".

3. Cash and cash equivalents

Reconciliation with the condensed statement of financial position

	Unaudited At 31 Dec 2017 \$'000	Audited At 31 Mar 2017 \$'000
Cash at bank	563	332
Fixed deposits with banks	85,708	83,744
Amounts shown in the condensed statement of financial position	86,271	84,076
Less : Amounts with an original maturity of beyond three months	(20,891)	-
Cash and cash equivalents in the condensed statement of cash flows	65,380	84,076

Unified Exchange Compensation Fund

Notes to the condensed financial statements

For the nine months ended 31 December 2017 (Expressed in Hong Kong dollars)

4. Contributions from SEHK / Relinquished trading rights payable to SEHK

According to section 104 of the repealed Securities Ordinance, The Stock Exchange of Hong Kong Limited (SEHK) contributes to the Fund in respect of each trading right at the rate of \$50,000 per trading right. In the absence of claims or other provisions as set out in section 106 of the repealed Securities Ordinance, the SFC must refund to SEHK the deposit within six months after the trading right was relinquished.

During the nine-month period, deposits of \$2,450,000 in respect of 49 new trading rights were received from SEHK and deposits of \$250,000 in respect of 5 relinquished trading rights were refunded to SEHK.

At 31 December 2017, there were 14 trading rights in total of \$700,000 that have been relinquished but not yet refunded (at 31 March 2017: 12). The net contributions from SEHK at 31 December 2017, excluding the relinquished trading rights payable, amounted to \$53,300,000 (at 31 March 2017: \$51,200,000).

5. Material related party transactions

We have related party relationships with the Investor Compensation Fund and the SFC. There were no significant related party transactions other than those disclosed in the condensed interim financial information of the Fund for the nine months ended 31 December 2016 and 2017.

6. Contingent liabilities

As at the date of this report, there is no outstanding claim against the Fund.

In relation to the default cases, any excess of recovered amounts (refer to note 2) will be re-distributed to claimants. As the timing of re-distribution and amount of these potential excess amounts are uncertain at the date of this report, we disclose this as a contingent liability.

Securities and Futures Commission

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