



20 Years of Transformation

This first Quarterly Report of the Securities and Futures Commission for financial year 2009-10 covers the period from 1 April to 30 June. In issuing this publication, the SFC aims to enhance transparency and accountability of its operations.

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Office

8th Floor, Chater House
8 Connaught Road Central
Hong Kong

Telephone : (852) 2840 9222

Facsimile : (852) 2521 7836

Website : www.sfc.hk

InvestEd Website : www.InvestEd.hk

Chief Executive Officer's Message

We continued to witness our firm enforcement and disciplinary actions bear fruit during the quarter. A couple of entities were convicted of insider dealing charges, resulting in the first immediate jail term and the eighth and ninth convictions for such offences in Hong Kong. Meanwhile, the High Court disqualified two directors of a listed firm from being a director or being involved in the management of any listed company for six years without court approval.

We also secured court clarification on certain key issues. In our first intervention in court proceedings about the privatisation of PCCW Ltd, the Court of Appeal (CA) ruled that share splitting for the purpose of manipulating the outcome is a form of abuse. Separately, in a ground-breaking judgment, the CA offered authoritative guidance on the nature and scope of the law, under which we may seek court approval to act against those contravening the Securities and Futures Ordinance.

In addition, the Securities and Futures Appeals Tribunal backed our decision to discipline three persons for unlicensed leveraged foreign exchange trading.

We reached an agreement with a second brokerage on the mis-selling of Lehman Brothers Minibonds, under which it would buy back from eligible clients the notes at their original value. The case was followed by our latest repurchase agreement with 16 banks.

During the quarter, Hong Kong and the Mainland signed Supplement VI to the Closer Economic Partnership Arrangement, allowing securities firms on both sides to set up joint ventures for advisory business in Guangdong. Also, both markets will actively explore introducing exchange-traded funds (ETFs) of Hong Kong-listed stocks to the Mainland. We are working with the relevant Mainland authorities on the implementation details of these initiatives.

The total number of Hong Kong-listed ETFs rose to 30 at the quarter-end, following the listing of six more ETFs tracking regional stocks and China A shares. Our exchange of a Side Letter with the Taiwan Financial Supervisory Commission in May also allowed the first Hong Kong ETFs approved for offering in Taiwan and the first Taiwan ETF approved to list in Hong Kong via a feeder fund.

In terms of investor education, we launched the first photo competition, which drew over 1,000 entries. In the next quarter, we look forward to equally enthusiastic response to our third Investment Story Competition.

Separately, we began a review of various codes for retail investment products to update and modernise the current provisions to offer a flexible framework that is on a par with international practices. Numerous soft consultation sessions on the review have been held with industry participants.

Martin Wheatley
Chief Executive Officer



Operational Review

Regulation

Firm enforcement actions taken

We took vigorous enforcement and disciplinary actions to deter market misconduct.

The top-down approach applied in the settlement with Sun Hung Kai Investment Services Ltd (Sun Hung Kai) last December enabled us to reach another agreement on mis-selling of Lehman Brothers (LB) Minibonds in April, this time, with KGI Asia Ltd (KGI).

KGI was reprimanded and made a voluntary offer to repurchase all outstanding Minibonds subscribed or bought by its clients at a price equal to the principal amount invested by them. The brokerage also agreed to review its internal control systems, on the understanding that if the SFC finds similar internal controls concerns of a materially serious nature in 18 months after the review is completed, its licence may be suspended for up to three years.

The buybacks by Sun Hung Kai and KGI of the outstanding Minibonds from their respective eligible clients were completed in July. A total of 329 clients recovered their initial investments in full, signifying a triple-win situation whereby the clients were adequately compensated, the brokerages could start anew, and the SFC could fulfil its statutory regulatory functions.

Continued investigations into the mis-selling of LB Minibonds throughout the quarter resulted in a repurchase arrangement with 16 banks to let eligible Minibond holders recover at least 60% to 70% of the original nominal value of their investment.

This quarter saw the SFC exercising its statutory power for the first time to intervene in a court proceeding. We successfully sought permission from the Court of First Instance (CFI) to intervene and be heard in proceedings commenced by PCCW Ltd (PCCW) for approval of a scheme of arrangement proposing the delisting and privatisation of PCCW.

Immediately after the CFI approved the privatisation scheme on 6 April, we appealed the case. Subsequently on 22 April, the Court of Appeal (CA) ruled in favour of the SFC and published the reason on 11 May, making it clear that share splitting for the purpose of manipulating the outcome in a scheme of arrangement is a form of abuse.

PCCW, Pacific Century Developments Ltd and Starvest Ltd have sought leave to appeal to the Court of Final Appeal (CFA). Their applications will be heard in August.

Action taken against other misconduct

Our efforts in combating insider dealing paid off during this quarter, resulting in the conviction of a number of entities.

We saw the first immediate jail term for insider dealing in Hong Kong. Ma Hon Yeung, former Vice President of BNP Paribas Peregrine Capital Ltd, now known as BNP Paribas Capital (Asia Pacific) Ltd, and his girlfriend and three other family members were found guilty of insider dealing in the shares of Egana Jewellery & Pearls Ltd. Ma was sentenced to 26 months' imprisonment and his girlfriend received 12 months. The family members were each ordered to serve 200 hours of community services. All of them were fined.

We obtained the eighth and ninth convictions for insider dealing in a year. Allen Lam Kar Fai, a former Director of Investment Banking at CLSA Equity Capital Markets Ltd, and Ryan Fong Yen-hwung, a former portfolio fund manager at HSZ (Hong Kong) Ltd, were each convicted of a charge of insider dealing concerning a proposed acquisition by JCDecaux Pearl & Dean Ltd of Media Partners International Holding Inc. Fong and Lam were fined and sentenced to jail terms of 12 months and six months respectively.

Separately, the High Court in May granted order to disqualify two directors of Wah Sang Gas Holdings Ltd (now renamed as Binhai Investment Co, Ltd). They were banned from being a director or being involved in the management of any listed company for six years for failing to exercise reasonable skill, care and diligence, to act in the best interests of the firm and its members and to ensure the firm accurately disclosed its business activities in financial statements.



In May, the court ordered to continue the appointment of administrators over Descartes Investment Management Ltd, Descartes Global Asset Management Ltd, Descartes Finance Ltd and Descartes Athena Fund SPC (Athena Fund) and to continue the injunction orders over a group of companies and individuals related to Athena Fund, a private hedge fund operating in Hong Kong that had raised more than US\$100 million from overseas investors and a number of entities.

The court also handed down judgments crucial to the SFC's regulatory work.

The CA in May delivered a ground-breaking judgment to allow an SFC appeal, re-imposing an injunction against three defendants for alleged insider dealing. The judgment was significant as it provided authoritative guidance on the nature and scope of applicability of section 213 of the Securities and Futures Ordinance (SFO) (under which the SFC may apply to the CFI for various orders against any person who has contravened a provision under the SFO). The trio has applied for leave to appeal to the CFA. Also, in a declaration, the CFI confirmed that carrying on grey-market trading is illegal unless the operator is licensed as a securities dealer by the SFC.

Outside the court room, we took disciplinary actions, including life-long ban, against three individuals and one company for various breaches, including unauthorised and negligent trading, dishonest appropriation of client's money, "front running" (using confidential information about a client's trading intention to make profit at the client's expense) and failure to ensure staff compliance with cold-calling laws.

In May, the Securities and Futures Appeals Tribunal (SFAT) confirmed our decision to discipline three people involved in unlicensed leveraged foreign exchange (forex) trading through Cosmos Hantec Investment (NZ) Ltd, a New Zealand company not licensed by the SFC. The SFAT agreed that leveraged forex trading by nature is of high risk and is subject to strict regulation in Hong Kong and that such acts had deprived Hong Kong investors of their statutory protection under local law.

Following the Takeovers Panel's rejection in April of the re-opening of a general offer by Nam Tai Electronics, Inc (NTEI) to acquire Nam Tai Electronic & Electrical Products Ltd (NTEEP) after the announcement of the lapse of the offer, NTEEP in May announced a proposed voluntary winding-up. As Koo Ming Kown, the only non-executive director of NTEEP and the only executive director of NTEI, made the announcement in full knowledge that the proposal constituted serious breaches of the Takeovers Code, the Executive imposed a "cold shoulder order" on Koo denying him direct or indirect access to the Hong Kong securities markets for two years and publicly censured Koo for his actions in the matter. Koo consented to the disciplinary action taken against him. Following further discussions, an application was submitted and a consent was granted under Rule 31.1 of the Takeovers Code for NTEI to make a further general offer for all the shares in NTEEP.

Market closely monitored

During the quarter we monitored the market closely on the international and local fronts.

We supported the global call for effective short-selling regulation. An International Organization of Securities Commissions (IOSCO) task force led by SFC Chief Executive Officer Mr Martin Wheatley completed a public consultation. A final report approved by the IOSCO Technical Committee recommended that short selling be subject to: 1) appropriate controls to minimise potential risks that could affect the functioning and stability of financial markets; 2) a reporting regime that provides timely information; and 3) an effective compliance and enforcement system. It also held that short-selling regulation should allow appropriate exceptions for certain types of transactions.

As a member of the IOSCO Task Force on Unregulated Financial Markets and Products, the SFC contributed to a consultation report that was issued in May 2009, which aimed to introduce greater transparency and oversight in the credit default swaps and securitisation markets and improve investor confidence in, and the quality of, these markets.

In April and July we issued two circulars to urge licensed corporations to put in place necessary measures and precautions to limit the potential impact of influenza A H1N1 (human swine influenza) on their operations and workforce.

Operational Review

To raise industry awareness of anti-money laundering (AML) compliance, we organised two seminars in May jointly with the Financial Services and the Treasury Bureau, attracting 600 management and compliance staff of intermediaries. They were updated on the latest international and domestic developments of AML regulations.

Market standards advanced

To meet increasing demand from the investing public for enhanced transparency and disclosure in offering documents and marketing materials of retail investment products, the SFC continued to adopt various measures and maintain dialogues with the industry to provide guidance.

Since July, marketing materials of retail funds and investment-linked assurance schemes (ILAS) have been required in general to comply fully with the revised advertising guidelines and the enhanced disclosure requirements. We held various meetings and briefings with industry practitioners to help them resolve practical difficulties in complying with such requirements by 30 June. We formed a working group with the Hong Kong Investment Funds Association to provide guidance and advice on the "Recommended Practices on the Presentation of the "Risk Disclosure Box" for authorised retail unit trusts and mutual funds". Also, we granted a one-month extension from strict compliance to individual issuers of ILAS regarding a limited number of pre-existing marketing materials, in light of the practical difficulties of ILAS issuers to comply by 30 June.

Investor concerns addressed

We continued to receive complaints related to LB but the volume dipped. As of 30 June, we had received 8,534 complaints, 282 of which were received in the second quarter.

Development

Product and market development promoted

We commenced a review of the various codes applicable to retail investment products for consultation. The revisions will update and modernise the current provisions to provide a flexible framework reflecting international practices. The aim is to offer a context for developing and offering a wide range of products in Hong Kong, while at the same time affording appropriate protection to investors.

The SFC is committed to enhancing the exchange-traded fund (ETF) platform in Hong Kong to turn it into the ETF hub in Asia and to provide an efficient means for Mainland capital to capture investment opportunities presented by different markets, sectors and asset classes.

During the quarter, six ETFs tracking the performance of regional stocks and China A shares were listed, bringing the total number of Hong Kong-listed ETFs to 30. We authorised six other ETFs during the quarter, five of which were listed in July and the remainder pending issuer's listing plan.

Analysis of complaints of market malpractices

Nature of complaints	As at 30/06/2009	As at 31/03/2009	As at 30/06/2008
Conduct of licensed intermediaries and registered institutions	242	156	95
Listing-related matters and disclosure of interests	89	168	113
Market misconduct	81	119	147
Products	5	7	23
Other financial activities	88	82	67
Miscellaneous	5	6	7
Subtotal	510	538	452
Complaints related to Lehman Brothers	282	532	0
Total	792	1,070	452



Number of authorised investment products

	As at 30/06/2009	As at 30/06/2008
Unit trusts and mutual funds	2,008	2,210
Investment-linked assurance schemes	235	232
Pooled retirement funds	35	36
MPF master trust schemes	37	36
MPF pooled investment funds	306¹	296
Others	124²	147
Total	2,745	2,957

¹ In this category, 131 of the funds were offered both as retail unit trusts as well as pooled investment funds for MPF purposes.

² Other schemes comprised 104 investment-linked deposits, 13 paper gold schemes and seven REITs.

On 22 May, we signed a Side Letter to a bilateral memorandum of Understanding with the Taiwan Financial Supervisory Commission (FSC) to facilitate the cross listing of ETFs in the two markets, marking a milestone in our regulatory co-operation with Taiwan and reinforcing Hong Kong as a preferred ETF platform with exposure to markets in Greater China. Lately, the FSC approved the offering of the first Hong Kong ETFs in Taiwan and we approved the first Taiwan ETF to cross-list in Hong Kong via a feeder fund.

Meanwhile, we also authorised for registration the prospectus of the first unlisted renminbi-denominated bonds for offer to the Hong Kong public since the collapse of LB. In reviewing the prospectus of this bond issued by The Bank of East Asia (China) Ltd, we sought to implement measures applicable to investment products as mentioned in our report to the Financial Secretary last December.

The measures included the inclusion of 1) the suitability warning as required in a Hong Kong Monetary Authority circular, appropriately adjusted to cater for the fact that renminbi bonds are not structured products; and 2) a “key facts” statement in the front portion of the prospectus to explain key risks and features of the bonds.

Process efficiency enhanced

Following discussions with Hong Kong Exchanges and Clearing Ltd (HKEx) in April, we approved on 18 May proposed rule amendments that aimed to streamline how Exchange Participants

provide information to the exchanges, including changes to company name, changes in directors, responsible officers and principal and branch addresses.

Meanwhile, the development of the SFC On-line Portal was near completion and various tests were being conducted to ensure the system’s readiness. The Portal would enable licensees, registrants and associated entities to view messages from the SFC and to submit annual returns (for licensees only) and other notifications to the SFC via the Internet.

During the quarter, we received 2,039 new licence applications, down a slight 1% from the previous quarter.

The one-off annual licence fee waiver for some 37,000 intermediaries came into effect on 1 April. We projected the measure to result in a reduction in our licensing revenue of approximately \$138 million.

Communication with Mainland participants strengthened

Since the implementation of Supplement II to the Closer Economic Partnership Arrangement (CEPA II), a number of Mainland futures companies have established their operations in Hong Kong.

In June, we organised a regulatory seminar for 30 executives of Mainland-related futures firms to help them better understand our regulatory requirements and encourage their compliance. The seminar covered various compliance topics, including

Number of licensees and registrants

	As at 30/06/2009	As at 31/03/2009	% Change	As at 30/06/2008	% Change
Licensed Corporations	1,569	1,565	0.25%	1,476	6.30%
Registered Institutions	102	101	0.99%	103	(0.97%)
Individuals	34,952	35,745	(2.20%)	34,283	1.95%
Total	36,623	37,411	(2.10%)	35,862	2.10%

licensing, financial resources requirements, asset handling and risk management matters. HKEx representatives were invited to discuss products offered by Hong Kong Futures Exchange (HKFE) and the role and operation of HKFE participants. Officials from the Department of Futures Supervision of the China Securities Regulatory Commission (CSRC) attended the activity as observers. Given the encouraging feedback from participants, we will explore rolling out the initiative to other sectors such as securities brokers and asset managers.

Closer ties with the Mainland sought

In support of the Government, we took part in various rounds of discussions with Mainland authorities to finalise the securities sector proposals under CEPA VI.

Signed on 9 May 2009, CEPA VI continued in the direction of economic liberalisation between Hong Kong and the Mainland. Under the supplement, eligible securities companies from Hong Kong and the Mainland may set up joint ventures to offer securities investment advisory service in Guangdong province. In addition, both markets will actively explore introducing ETFs of Hong Kong-listed stocks in the Mainland.

On 5 June, we discussed with the CSRC the detailed implementation plans of measures laid down in CEPA VI, specifically, the arrangement for allowing Hong Kong brokers to set up joint-venture investment advisory firms in Guangdong. Afterwards, we updated the industry on the progress of discussion.

Mainland's integration with world economy capitalised

We worked on a renminbi internationalisation proposal to analyse the implications of such a move on the Mainland and Hong Kong and to formulate certain recommendations and proposals for implementation.

We conducted a review of the Mainland's 11th Five-year Plan, which assessed the implementation of Hong Kong-related policies in the current plan, and how Hong Kong should be positioned in the next Five-year Plan.

We were also involved in various proposals on strengthening co-operation within the Pearl River Delta Region.

Hong Kong's status as financial centre reviewed

To maintain Hong Kong's status as an international financial centre, we conducted a strategic review of Hong Kong's economy and financial sector by comparing it with its competitors, analysing its strengths and weaknesses, and preparing proposals for consideration.

Communication with industry continues

Through various periodical publications, we informed the market of our initiatives in regulating and developing the financial markets.

We published the ninth issue of the Takeovers Bulletin in June. Apart from the Takeovers Panel's decision and subsequent disciplinary action in the NTEEP case, the Bulletin carried two new Practice Notes on special deals and exempt share repurchases as well as a reminder that the Executive's clearance of documents does not provide immunity.



The latest issue of the Dual Filing Update was published in June. We commented on 11 out of 21 cases referred by The Stock Exchange of Hong Kong Ltd in the half year ended March 2009. Various deficiencies in the draft prospectus suggested that the sponsors might not have exercised due care in advising on the preparation of the listing applications.

Education

We continued to maximise the effective use of a combination of mass-media and interactive approaches in our investor education initiatives, reaching as many audiences as possible.

On 12 March, we launched our first photo competition entitled “Why am I investing?” as part of our “Be Smart, Ask First” campaign. Contestants would have to present the reason why they invest in a photograph. The contest attracted more than 1,000 entries, offering various reasons for investing, including the family, retirement and travels. An exhibition of the 28 winning entries was held at Maritime Square, Tsing Yi, on 27 and 28 June, along with two seminars on financial planning and a children’s singing contest of our television commercial’s theme song.

On 27 May, our third Investment Story Competition kicked off, with Commercial Radio One, Hong Kong Economic Journal and Cable TV as media partners. By inviting the public to share their investment experiences through telling their own story, we aim to promote a healthy investment attitude and stress the importance of understanding risks before making investment decisions. To foster a correct investment attitude among the younger generation, students were also invited to take part in a newly created Student Group.

Using mass-media channels, including a weekly column in Headline Daily and talk shows on Radio Television Hong Kong and Metro Radio, we explained a range of investment topics. More specifically, we covered stock trading procedures, features and risks of callable bull/bear contracts, the need for portfolio rebalancing and ongoing monitoring of fund investments, on-line search of investment product information, and the SFC’s licensing and other investor protection work.

Eight short videos on topics related to dealing with investment advisers’ recommendations on products, risk disclosure of structured products and trading risks in a volatile market were re-run on buses in April and May.

As a recommendation in our report to the Financial Secretary on the LB incident, we posted on our InvestEd website a list of investment products with the primary objective of allowing public access to products’ offering documents that have been authorised by the SFC for issuance under the SFO or for registration under the Companies Ordinance.

A total of 14 talks, seminars and university courses were organised for around 2,000 attendees during the quarter. One of the events featured a full-day of seminars open to the public on the economic outlook of Hong Kong and the Mainland, organised in partnership with the Hong Kong Society of Financial Analysts.

Organisational Matters

We had 489 staff members as at 30 June, compared with 448 a year ago.

Total revenue for the quarter was \$472 million, compared with \$501 million in the same period last year and \$330 million in the past quarter. Expenditure reached \$177 million, 13% below our approved budget. This resulted in a surplus of \$295 million for the quarter, compared with \$348 million a year ago and \$135 million in the previous quarter. As at 30 June, our reserves stood at \$5.2 billion.

The Government appointed Mr Wong Kai-man to succeed Dr York Liao as Non-Executive Director for a two-year term from 26 May 2009. We thank Dr Liao for his contribution to the SFC over the past six years. In the same quarter, the Government appointed and re-appointed members to the SFC Advisory Committee for two years from 1 June 2009.

Consolidated income and expenditure account

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

	Note	Unaudited quarter ended	
		30 June 2009	30 June 2008
		\$'000	\$'000
Income			
Levies		387,139	407,495
Fees and charges		47,373	51,015
Investment income		35,537	41,427
Less : custody and advisory expenses		(529)	(475)
Investment income net of third party expenses		35,008	40,952
Recoveries from Investor Compensation Fund		1,009	1,079
Other income		1,923	728
		472,452	501,269
Expenses			
Staff costs and directors' emoluments		135,245	122,047
Premises			
rent		14,506	8,648
other		5,648	5,219
Other expenses		15,832	13,827
Depreciation		6,077	3,821
		177,308	153,562
Surplus	2	295,144	347,707
Accumulated surplus brought forward		4,910,643	3,898,361
Accumulated surplus carried forward		5,205,787	4,246,068

The notes on pages 13 to 14 form part of these condensed financial statements.

Consolidated balance sheet

At 30 June 2009
(Expressed in Hong Kong dollars)

	Note	Unaudited	Audited
		At 30 June 2009	At 31 March 2009
		\$'000	\$'000
Non-current assets			
Fixed assets		46,275	42,015
Held-to-maturity debt securities	3	3,504,308	3,588,538
		3,550,583	3,630,553
Current assets			
Held-to-maturity debt securities	3	1,241,874	858,870
Debtors, deposits and prepayments		225,465	181,908
Bank deposits		387,342	454,140
Cash at bank and in hand		3,141	2,264
		1,857,822	1,497,182
Current liabilities			
Fees received in advance		44,585	65,582
Creditors and accrued charges		79,402	70,704
		123,987	136,286
Net current assets			
		1,733,835	1,360,896
Total assets less current liabilities			
		5,284,418	4,991,449
Non-current liabilities			
	4	35,791	37,966
Net assets			
		5,248,627	4,953,483
Funding and reserves			
Initial funding by Government			
		42,840	42,840
Accumulated surplus			
	2	5,205,787	4,910,643
		5,248,627	4,953,483

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

The notes on pages 13 to 14 form part of these condensed financial statements.

Balance sheet

At 30 June 2009
(Expressed in Hong Kong dollars)

	Note	Unaudited	Audited
		At 30 June 2009	At 31 March 2009
		\$'000	\$'000
Non-current assets			
Fixed assets		46,240	41,977
Held-to-maturity debt securities	3	3,504,308	3,588,538
		3,550,548	3,630,515
Current assets			
Held-to-maturity debt securities	3	1,241,874	858,870
Debtors, deposits and prepayments		225,173	181,734
Bank deposits		387,342	454,140
Cash at bank and in hand		2,508	1,784
		1,856,897	1,496,528
Current liabilities			
Fees received in advance		44,585	65,582
Creditors and accrued charges		78,442	70,012
		123,027	135,594
Net current assets		1,733,870	1,360,934
Total assets less current liabilities		5,284,418	4,991,449
Non-current liabilities	4	35,791	37,966
Net assets		5,248,627	4,953,483
Funding and reserves			
Initial funding by Government		42,840	42,840
Accumulated surplus	2	5,205,787	4,910,643
		5,248,627	4,953,483

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

The notes on pages 13 to 14 form part of these condensed financial statements.

Consolidated cash flow statement

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

	Unaudited quarter ended	
	30 June 2009	30 June 2008
	\$'000	\$'000
Cash flows from operating activities		
Surplus	295,144	347,707
Adjustments for:		
Depreciation	6,077	3,821
Investment income	(35,537)	(41,427)
Profit on disposal of fixed assets	–	(54)
	265,684	310,047
(Increase)/decrease in debtors, deposits and prepayments	(59,444)	34,682
Increase in creditors and accrued charges	8,698	56,487
Increase in fees received in advance	(20,997)	(7,217)
Decrease in non-current liabilities	(2,175)	(2,266)
Net cash generated from operating activities	191,766	391,733
Cash flows from investing activities		
Interest received	63,025	40,332
Held-to-maturity debt securities bought	(475,424)	(770,830)
Held-to-maturity debt securities sold	–	94,798
Held-to-maturity debt securities redeemed at maturity	165,049	314,312
Fixed assets bought	(10,337)	(19,514)
Fixed assets sold	–	63
Net cash used in investing activities	(257,687)	(340,839)
Net increase in cash and cash equivalents	(65,921)	50,894
Cash and cash equivalents at beginning of the quarter	456,404	88,337
Cash and cash equivalents at end of the quarter	390,483	139,231
Analysis of the balance of cash and cash equivalents:		
	Unaudited	
	At 30 June 2009	At 30 June 2008
	\$'000	\$'000
Bank deposits	387,342	135,440
Cash at bank and in hand	3,141	3,791
	390,483	139,231

Notes to the consolidated financial statements

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

1. Basis of preparation

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

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2009 included in this report does not constitute the SFC's statutory accounts for that financial year but is derived from those financial statements.

We consolidated the financial results of Investor Compensation Company Limited in the SFC's condensed financial statements made up to 30 June 2009. We eliminate 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 2009 to the interim financial report.

There were no significant changes in the operation of the SFC for the quarter ended 30 June 2009.

2. Accumulated surplus

The Group and the SFC

Movements of accumulated surplus during the quarter ended 30 June 2009 are as follows:

	Unaudited \$'000
Balance at 31 March 2009	4,910,643
Surplus for the quarter	295,144
Balance at 30 June 2009	5,205,787

3. Held-to-maturity debt securities

The Group and the SFC

As of 30 June 2009, the total market value of held-to-maturity debt securities amounted to \$4,815,301,000 (31 March 2009 : \$4,508,399,000), which was above the total carrying cost of \$4,746,182,000 (31 March 2009 : \$4,447,408,000).

4. Non-current liabilities

The Group and the SFC

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

5. Ageing analysis of debtors and creditors

There was no material overdue debtor balance and creditor balance included in "debtors, deposits and prepayments" and "creditors and accrued charges" respectively as at 30 June 2009. Therefore we do not provide an ageing analysis of debtors and creditors.

6. Exchange fluctuation

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

7. Investments in subsidiaries

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

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

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

Both companies are wholly owned subsidiaries of the SFC. As at 30 June 2009, the investments in subsidiaries, which are stated at cost less any impairment losses, amounted to \$2.2. The balance is too small to appear on the balance sheet which is expressed in thousands of dollars.

The balance sheet of FinNet as at 30 June 2009 was immaterial and its expenses have been paid by the SFC. We have not therefore consolidated FinNet in the Group's financial statements.

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

8. Related party transactions

We have related party relationships with the Unified Exchange Compensation Fund, the Investor Compensation Fund, the Securities Ordinance (Chapter 333) - Dealers' Deposits Fund, the Commodities Trading Ordinance (Chapter 250) - Dealers' Deposits Fund and the Securities Ordinance (Chapter 333) - Securities Margin Financiers' Security Fund. 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 Investor Compensation Fund for all the ICC's expenses amounting to \$1,009,000 (2008 : \$1,079,000), in accordance with section 242(1) of the Securities and Futures Ordinance.

(b) Remuneration for key management personnel (including all directors) comprised :

	Unaudited three months ended	
	30 June 2009	30 June 2008
	\$'000	\$'000
Short-term employee benefits	7,155	6,762
Post employment benefits	671	502
	7,826	7,264

(c) Included in creditors and accrued charges is an amount due to Investor Compensation Fund amounting to \$668,000 (At 31 March 2009 : \$477,000).

Report of the Investor Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the quarter ended 30 June 2009.

1. Establishment of the Fund

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

2. Financial results

The Committee presents the financial results which are set out in the financial statements on pages 16 to 20.

3. Members of the Committee

The members of the Committee during the quarter ended 30 June 2009 and up to the date of this report were : -

Mr Keith Lui (Chairman)

Mr Gerald Greiner

Mr Kenneth H W Kwok, BBS, SC

Mrs Alexa Lam

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 quarter.

On behalf of the Committee

Keith Lui

Chairman

23 July 2009

Income and expenditure account

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

	Note	Unaudited quarter ended	
		30 June 2009 \$'000	30 June 2008 \$'000
Income			
Net investment income / (loss)		51,598	(20,441)
Exchange difference		(48)	1,856
		51,550	(18,585)
Expenses			
Investor Compensation Company expenses	2	1,009	1,079
Compensation expense / (write backs)		162	(273)
Auditor's remuneration		21	21
Bank charges		201	201
Professional fees		725	781
Sundry expenses		-	1
		2,118	1,810
Surplus/(deficit)		49,432	(20,395)
Accumulated surplus brought forward		711,964	756,185
Accumulated surplus carried forward		761,396	735,790

The notes on pages 19 to 20 form part of the condensed financial statements.

Balance sheet

At 30 June 2009
(Expressed in Hong Kong dollars)

	Unaudited At 30 June 2009	Audited At 31 March 2009
	\$'000	\$'000
Current assets		
Financial assets designated at fair value through profit or loss		
– Debt securities	1,547,892	1,554,614
– Equity securities	144,641	113,112
Interest receivable	17,641	20,253
Unsettled regular purchases of financial assets	15,469	-
Fair value adjustment on unsettled trades	117	(129)
Due from Investor Compensation Company	668	477
Fixed and call deposits with banks	145,419	116,037
Cash at bank	266	20,074
	1,872,113	1,824,438
Current liabilities		
Provision for compensation	6,270	8,032
Accounts payable and accrued charges	806	801
	7,076	8,833
Net current assets	1,865,037	1,815,605
Net assets	1,865,037	1,815,605
Representing:		
<u>Compensation fund</u>		
Contributions from Unified Exchange Compensation Fund	994,718	994,718
Contributions from Commodity Exchange Compensation Fund	108,923	108,923
Accumulated surplus	761,396	711,964
	1,865,037	1,815,605

We have not prepared a separate Statement of Changes in Equity as the surplus/(deficit) for the quarter would be the only component of such a statement.

The notes on pages 19 to 20 form part of the condensed financial statements.

Cash flow statement

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

	Unaudited quarter ended	
	30 June 2009	30 June 2008
	\$'000	\$'000
Cash flows from operating activities		
Surplus / (deficit) for the quarter	49,432	(20,395)
Net investment (income) / loss	(51,598)	20,441
Exchange difference	48	(1,856)
Increase in amount due from Investor Compensation Company	(191)	(236)
(Increase) / decrease in unsettled regular purchase of financial assets	(15,469)	46,987
Decrease in provision for compensation	(1,762)	(13,335)
Increase / (decrease) in accounts payable and accrued charges	5	(14)
Net cash (used in) / from operating activities	(19,535)	31,592
Cash flows from investing activities		
Purchase of debt securities	(493,149)	(495,894)
Sale or maturity of debt securities	504,183	570,410
Sale of equity securities	137	253
Interest received	17,938	22,110
Net cash from investing activities	29,109	96,879
Net increase in cash and cash equivalents	9,574	128,471
Cash and cash equivalents at beginning of the quarter	136,111	109,700
Cash and cash equivalents at end of the quarter	145,685	238,171

Analysis of the balance of cash and cash equivalents:

	Unaudited	
	At 30 June 2009	At 30 June 2008
	\$'000	\$'000
Fixed and call deposits with banks	145,419	238,157
Cash at bank	266	14
	145,685	238,171

Notes to the condensed financial statements

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

1. Basis of preparation

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

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2009 included in this report does not constitute the Fund’s statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2009 to the interim financial report.

2. ICC expenses

The SFC formed the Investor Compensation Company Limited (ICC) in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the Securities and Futures Ordinance (SFO). The Fund is responsible for funding the establishment and operation of ICC. For the quarter ended 30 June 2009, ICC incurred \$1,009,000 for its operation (For the quarter ended 30 June 2008 : \$1,079,000).

3. Provision for compensation

	\$'000
Balance as at 1 April 2008	22,978
Add: provision made during the year ended 31 March 2009	4,679
Less: provision reversed during the year ended 31 March 2009	(3,685)
Less: compensation paid during the year ended 31 March 2009	(15,940)
Balance as at 31 March 2009	8,032
Add: provision made during the quarter ended 30 June 2009	162
Less: compensation paid during the quarter ended 30 June 2009	(1,924)
Balance as at 30 June 2009	6,270

We maintained provision for liabilities arising from claims received resulting from three default cases for which ICC has published a notice calling for claims pursuant to Section 3 of the Securities & Futures (Investor Compensation-Claims) Rules. The maximum liability of the Fund to claims for these cases is set at the lower of \$150,000 per claimant or the amount claimed. As at 30 June 2009 all provisions were expected to be paid within one year.

4. Related party transactions

We have related party relationships with the SFC, the ICC, the SEHK, the HKFE and the UECF. During the quarter, there were no significant related party transactions other than those disclosed in the financial statements.

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 in respect of these claims is \$443,000 (31 March 2009: \$450,000). This is determined based on the lower of the maximum compensation limit of \$150,000 per claimant or the amount claimed.

In September 2008, following the Lehman Brothers group's default, the SFC approved the issue of restriction notices on four entities of Lehman Brothers in Hong Kong to preserve the assets of the companies and their clients, and to protect the interests of these clients and the investing public. At the date of this report, the assessment of whether and to which extent an obligation of the Fund exists under the SFO in respect of such default, if any, has not been completed, and therefore it is not practical to estimate any financial effect at this stage. No claims in respect of the Lehman Brothers' companies in Hong Kong have been received up to the date of this report.

Report of the Securities Compensation Fund Committee (the Committee)

The members of the Committee present their quarterly report and the unaudited condensed financial statements for the quarter ended 30 June 2009.

1. Establishment of the Fund

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

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

2. Financial results

The Committee presents the financial results which are set out in the financial statements on pages 22 to 27.

3. Members of the Committee

The members of the Committee during the quarter ended 30 June 2009 and up to the date of this report were : -

Mr Keith Lui (Chairman)

Mr Gerald Greiner

Mrs Alexa Lam

Mr Kenneth H W Kwok, BBS, SC

Mr Eric Yip

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 quarter.

On behalf of the Committee

Keith Lui

Chairman

23 July 2009

Income and expenditure account

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

	Note	Unaudited quarter ended	
		30 June 2009	30 June 2008
		\$'000	\$'000
Income			
Interest income		87	239
Recoveries	2	146	(28)
		233	211
Expenses			
Auditor's remuneration		9	9
Sundry expenses		-	1
		9	10
Surplus		224	201
Accumulated surplus brought forward		15,103	13,910
Accumulated surplus carried forward		15,327	14,111

The notes on pages 26 to 27 form part of the condensed financial statements.

Balance sheet

At 30 June 2009
(Expressed in Hong Kong dollars)

	Unaudited	Audited
	At 30 June 2009	At 31 March 2009
	\$'000	\$'000
Current assets		
Equity securities received under subrogation	442	307
Interest receivable	31	44
Fixed and call deposits with banks	67,770	67,270
Cash at bank	296	334
	68,539	67,955
Current liabilities		
Accounts payable and accrued charges	10,241	10,281
	58,298	57,674
	58,298	57,674
Representing:		
<u>Compensation fund</u>		
Contributions from the SEHK	47,400	47,000
Excess transaction levy from the SEHK	353,787	353,787
Special contribution	3,500	3,500
Additional contribution from the SEHK	300,000	300,000
Additional contribution from the SFC	330,000	330,000
Special levy surplus	3,002	3,002
Accumulated surplus	15,327	15,103
	1,053,016	1,052,392
Contributions to Investor Compensation Fund	(994,718)	(994,718)
	58,298	57,674

The notes on pages 26 to 27 form part of the condensed financial statements.

Statement of changes in equity

For the quarter ended 30 June 2009

(Expressed in Hong Kong dollars)

	Unaudited quarter ended	
	30 June 2009	30 June 2008
	\$'000	\$'000
Compensation fund balance as at 1 April	57,674	56,031
Surplus for the quarter	224	201
Net contributions received from the SEHK	400	250
Compensation fund balance as at 30 June	58,298	56,482

The notes on pages 26 to 27 form part of the condensed financial statements.

Cash flow statement

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

	Unaudited quarter ended	
	30 June 2009	30 June 2008
	\$'000	\$'000
Cash flows from operating activities		
Surplus for the quarter	224	201
Interest income	(87)	(239)
(Increase)/decrease in equity securities received under subrogation	(135)	34
Decrease in accounts payable and accrued charges	(40)	(26)
Net cash used in operating activities	(38)	(30)
Cash flows from investing activities		
Interest received	100	259
Net cash from investing activities	100	259
Cash flows from financing activities		
Net contributions from the SEHK	400	250
Net cash from financing activities	400	250
Net increase in cash and cash equivalents	462	479
Cash and cash equivalents at beginning of the quarter	67,604	59,596
Cash and cash equivalents at end of the quarter	68,066	60,075

Analysis of the balance of cash and cash equivalents:

	Unaudited	
	At 30 June 2009	At 30 June 2008
	\$'000	\$'000
Fixed and call deposits with banks	67,770	59,431
Cash at bank	296	644
	68,066	60,075

Notes to the condensed financial statements

For the quarter ended 30 June 2009
(Expressed in Hong Kong dollars)

1. Basis of preparation

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

The interim financial report is unaudited and the financial information relating to the financial year ended 31 March 2009 included in this report does not constitute the Fund's statutory accounts for that financial year but is derived from those accounts.

We applied the same accounting policies adopted in the financial statements for the year ended 31 March 2009 to the interim financial report.

2. Recoveries

In relation to the share distribution from C.A. Pacific Securities Ltd. and C.A. Pacific Finance Ltd., the liquidators had advised the Securities and Futures Commission (SFC) that shares were allocated to the Fund under its subrogation rights, subject to paying a processing fee to the liquidators. The Fund recognised as recoveries the sale proceeds and the remaining shares at market value as of 30 June 2009 after deducting relevant processing fees and charges for collecting and selling the securities 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 IAS 39. At each balance sheet date the fair value is remeasured, with any resultant gain or loss being recognised in "Recoveries". Dividend income, if any, is also recognised in "Recoveries".

	Quarter ended	
	30 June 2009	30 June 2008
	\$'000	\$'000
Recoveries received in cash (including stock dividend)	11	6
Revaluation gain / (loss) on shares received from subrogation	135	(34)
Recoveries recognised during the quarter	146	(28)

3. Contributions from the SEHK

During the quarter, deposits of \$550,000 in respect of eleven new trading rights were received from the SEHK and deposits of \$150,000 in respect of three relinquished trading rights were refunded to the SEHK.

4. Related party transactions

The Fund has related party relationships with the ICF, the SFC and the SEHK. During the quarter, there were no significant related party transactions other than those disclosed in the financial statements.

5. Contingent liabilities

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

Shares were allocated to the Fund under its subrogation rights in relation to the C.A. Pacific case (refer to note 2). As at 30 June 2009, shares with a market value \$442,000, which are listed on the SEHK, remained unsold. Any excess of recovered amounts (if any) after disposal of these remaining shares 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.