Independent auditor's report
To the Securities and Futures Commission

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

Opinion

What we have audited

The consolidated financial statements of Securities and Futures Commission (the SFC) and its subsidiaries (the Group) set out on pages 101 to 129, which comprise:

- the consolidated statement of financial position as at 31 March 2018;
- the consolidated statement of profit or loss and other comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated cash flow statement for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 March 2018, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards (HKFRSs) issued by the Hong Kong Institute of Certified Public Accountants (HKICPA).

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (HKSAs) issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Group in accordance with the HKICPA's Code of Ethics for Professional Accountants (the Code), and we have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters identified in our audit are summarised as follows:

- Transition as auditor
- Valuation and classification of investments

Transition as auditor

Initial audit engagements involve a number of considerations in addition to recurring audits, which require a higher degree of auditor attention and effort. We identified the audit transition, including the audit of opening balances as a key audit matter as this involves additional planning activities and considerations necessary to gain sufficient understanding of the Group's operations, control environment, information systems, and application of accounting policies, in order to establish an appropriate audit plan and strategy.

How our audit addressed the Key Audit Matter

We prepared a detailed transition plan prior to start of the audit, and performed the following procedures:

- Discussion with senior management to gain knowledge of the Group and its operations, control environment and information systems;

Independent auditor's report (continued)
To the Securities and Futures Commission

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

- Communicating our transition plan and the results of our procedures performed with the Audit Committee;
- Reviewing the documentation of policies and procedures around the Group's financial reporting and control processes;
- Evaluating the selection and application of accounting policies;
- Meeting the predecessor auditor to understand their risk assessment and areas of focus; and
- Obtaining external confirmations to test the accuracy and existence of bank and investment balances as at 31 March 2017, on a sample basis.

We have not identified any material issues in relation to our transition as the auditor of the Group.

Valuation and classification of investments

Refer to notes 3(b), 9, 10 and 21(e)(i) to the consolidated financial statements.

As at 31 March 2018 the aggregate value of the Group's investment portfolio was HK$3,289 million, which represented 45% of consolidated assets as at that date.

The investment portfolio comprised debt and equity investments with a total value of HK$1,707 million which were designated as at fair value through profit or loss, under the Level 1 and 2 fair value hierarchy, and debt investments with a total value of HK$1,582 million which were designated as held-to-maturity investments.

The Group's debt and equity investments designated as at fair value through profit or loss are valued based on a combination of market observable inputs and valuation models.

For held-to-maturity investments, management is required to demonstrate their intention and ability to hold such investments to maturity in order to classify these debt investments as held-to-maturity investments.

We identified valuation and classification of investments as a key audit matter because of the size of these items in the financial statements and judgements made by management in classifying debt investments as held-to-maturity investments.

How our audit addressed the Key Audit Matter

Our audit procedures to address the valuation and classification of investments included:

- Assessing the internal control reports prepared by the independent service auditors of the Group's external investment managers who assessed the design, implementation and operating effectiveness of the investment managers' internal controls over investment authorisation, purchases, sales and payments, valuation and assessing the independent service auditor's reputation, professional competence and independence;
- Performing independent valuations for financial instruments designated as at fair value through profit or loss with the assistance of our internal valuation specialists. We compared the fair values applied by the Group with publicly available market data. For Level 2 financial instruments, with the involvement of our internal valuation specialists, we performed independent valuations, on a sample basis, by developing models, identifying and obtaining relevant inputs from publicly available market data and comparing the results against fair values recorded by the Group; and

Independent auditor's report (continued)
To the Securities and Futures Commission
(Established in Hong Kong under the Securities and Futures Commission Ordinance)

- Assessing the ongoing appropriateness of the "held-to-maturity" classification for certain debt investments through checking the movements in the "held-to-maturity" portfolio and assessing the Group's financial condition and liquidity management to evaluate the Group's intention and ability to hold such investments to maturity.

Based on the procedures we performed, we found that the valuation and classification of investments are supported by available evidence.

Other information

The directors of the SFC (the directors) are responsible for the other information. The other information comprises all of the information included in the annual report other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors and those charged with governance for the consolidated financial statements

The directors are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with Section 16(3) of the Securities and Futures Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

Independent auditor's report (continued)
To the Securities and Futures Commission

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Peter Po-ting Li.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 1 June 2018

Consolidated Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Income			
Levies	2(a)	1,549,460	1,017,453
Fees and charges		153,985	142,990
Investment income	5	278,884	202,623
Less: custody and advisory expenses		(7,735)	(5,894)
Investment income net of third party expenses		271,149	196,729
Recoveries from Investor Compensation Fund		5,729	5,574
Other income	6	34,593	525
		2,014,916	1,363,271
Expenses			
Staff costs and directors' emoluments	7	1,282,393	1,201,936
Premises			
Rent		204,381	208,744
Rates, management fees and others		47,413	49,888
Other expenses	8	207,687	211,594
Depreciation	11(a)	30,178	46,749
		1,772,052	1,718,911
Surplus/(loss) and total comprehensive income for the year		242,864	(355,640)

The notes on pages 106 to 129 form part of these financial statements.

Consolidated Statement of Financial Position

At 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Non-current assets			
Fixed assets	11(a)	71,923	63,455
Held-to-maturity debt securities	9	1,546,613	–
		1,618,536	63,455
Current assets			
Held-to-maturity debt securities	9	35,503	30,003
Financial assets designated at fair value through profit or loss			
Debt securities	10	772,300	716,403
Pooled funds	10	934,768	941,911
Debtors, deposits and prepayments	16	219,778	158,450
Fixed deposits with banks	12	3,713,477	5,107,808
Cash at bank and in hand	12	33,353	75,462
		5,709,179	7,030,037
Current liabilities			
Fees received in advance		8,810	9,210
Creditors and accrued charges	14	113,317	128,218
		122,127	137,428
Net current assets		5,587,052	6,892,609
Total assets less current liabilities		7,205,588	6,956,064
Non-current liabilities	15	40,824	34,164
Net assets		7,164,764	6,921,900
Funding and reserves			
Initial funding by Government	17	42,840	42,840
Reserve for property acquisition	23	3,000,000	3,000,000
Accumulated surplus		4,121,924	3,879,060
		7,164,764	6,921,900

Approved and authorised for issue by the SFC on 1 June 2018 and signed on its behalf by

Carlson Tong
Chairman

Ashley Alder
Chief Executive Officer

The notes on pages 106 to 129 form part of these financial statements.

Statement of Financial Position

At 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Non-current assets			
Fixed assets	11(b)	71,859	63,167
Held-to-maturity debt securities	9	1,546,613	–
		1,618,472	63,167
Current assets			
Held-to-maturity debt securities	9	35,503	30,003
Financial assets designated at fair value through profit or loss			
Debt securities	10	772,300	716,403
Pooled funds	10	934,768	941,911
Debtors, deposits and prepayments	16	221,338	158,516
Fixed deposits with banks		3,713,477	5,107,808
Cash at bank and in hand		21,171	71,262
		5,698,557	7,025,903
Current liabilities			
Fees received in advance		8,810	9,210
Creditors and accrued charges	14	102,631	123,796
		111,441	133,006
Net current assets		5,587,116	6,892,897
Total assets less current liabilities		7,205,588	6,956,064
Non-current liabilities	15	40,824	34,164
Net assets		7,164,764	6,921,900
Funding and reserves			
Initial funding by Government	17	42,840	42,840
Reserve for property acquisition	23	3,000,000	3,000,000
Accumulated surplus		4,121,924	3,879,060
		7,164,764	6,921,900

Approved and authorised for issue by the SFC on 1 June 2018 and signed on its behalf by

Carlson Tong
Chairman

Ashley Alder
Chief Executive Officer

The notes on pages 106 to 129 form part of these financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	Initial funding by Government $'000	Reserve for property acquisition $'000	Accumulated surplus $'000	Total $'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 year	–	–	(355,640)	(355,640)
Balance at 31 March 2017 and 1 April 2017	**42,840**	**3,000,000**	**3,879,060**	**6,921,900**
Surplus and total comprehensive income for the year	**–**	**–**	**242,864**	**242,864**
Balance at 31 March 2018	**42,840**	**3,000,000**	**4,121,924**	**7,164,764**

The notes on pages 106 to 129 form part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Cash flows from operating activities			
Surplus/(loss) for the year		242,864	(355,640)
Adjustments for:			
Depreciation		30,178	46,749
Investment income		(278,884)	(202,623)
Exchange difference		(23,336)	(2,069)
Loss on disposal of fixed assets		719	7
		(28,459)	(513,576)
Increase in debtors, deposits and prepayments		(54,406)	(26,861)
(Decrease)/increase in fees received in advance		(400)	805
(Decrease)/increase in creditors and accrued charges		(14,901)	6,249
Increase in non-current liabilities		6,660	8,317
Net cash used in operating activities		(91,506)	(525,066)
Cash flows from investing activities			
Decrease in fixed deposits other than cash and cash equivalents		1,051,818	63,022
Interest received		84,235	68,786
Debt securities designated at fair value through profit or loss purchased		(636,065)	(1,449,334)
Debt securities designated at fair value through profit or loss sold or redeemed		578,027	726,299
Pooled funds purchased		–	(155,133)
Pooled funds sold		216,100	2,448
Held-to-maturity debt securities purchased		(1,577,866)	–
Held-to-maturity debt securities redeemed at maturity		30,000	460,553
Fixed assets purchased		(39,365)	(36,964)
Net cash used in investing activities		(293,116)	(320,323)
Net decrease in cash and cash equivalents		(384,622)	(845,389)
Cash and cash equivalents at beginning of the year		676,727	1,522,116
Cash and cash equivalents at end of the year	12	292,105	676,727

Analysis of the balance of cash and cash equivalents

	2018 $'000	2017 $'000
Fixed deposits with banks	258,752	601,265
Cash at bank and in hand	33,353	75,462
	292,105	676,727

The notes on pages 106 to 129 form part of these financial statements.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

1. Status and principal activities

The Securities and Futures Commission (SFC) is governed by Part II of the Hong Kong Securities and Futures Ordinance (SFO). Under the SFO, the SFC has a duty to ensure an efficient, fair and transparent market and to promote public confidence and investor awareness in Hong Kong's securities, futures and related financial markets. In performing its duty, the SFC is required to act in the interest of the public and ensure that improper and illegal market activities are properly investigated. The registered office and principal place of business of the SFC is 35/F Cheung Kong Center, 2 Queen's Road Central, Hong Kong.

2. Income

Details of the funding of the SFC are set out in Section 14 and Sections 394 to 396 of the SFO. Major sources of funding include:

(a) levies collected by The Stock Exchange of Hong Kong Limited (SEHK) and Hong Kong Futures Exchange Limited (HKFE) on transactions recorded on the Exchanges at rates specified by the Chief Executive in Council.

(b) fees and charges in relation to its functions and services according to the provision of subsidiary legislation.

The SFC also generates investment income from fixed deposits, debt securities and pooled funds.

3. Significant accounting policies

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards (HKFRSs), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (HKASs) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (HKICPA) and accounting principles generally accepted in Hong Kong. Significant accounting policies adopted by the Group are set out below.

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for the current accounting period of the Group. Note 3(q) provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these financial statements.

We have not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 24).

(b) Basis of preparation

We have prepared these financial statements using the historical cost as the measurement basis except that financial assets designated at fair value through profit or loss are stated at their fair value (see note 3(h)). The accounting policies have been applied consistently by the Group entities.

We prepare the financial statements in conformity with HKFRSs which require management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. We make estimates and associated assumptions based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

Critical accounting estimates and judgements are those items that will have a significant effect on the Group's reported results and financial position.

The classification of held-to-maturity securities requires significant judgement. In making this judgement, we evaluate our intention and ability to hold such investment to maturity. The measurement of fair value for financial instruments is determined by using either publicly available market data or valuation models. We use our judgement to select the appropriate method for fair value measurement (see note 3(h)).

We review the estimates and underlying assumptions on an ongoing basis. We recognise the revisions to accounting estimates in the period in which the estimates are revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(c) Basis of consolidation

Subsidiaries are entities controlled by the SFC. The SFC controls an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect these returns through its power over the entity. When assessing whether the SFC has power, only substantive rights are considered.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases.

(d) Recognition of income

We recognise income in the statement of profit or loss and other comprehensive income provided it is probable that the economic benefits will flow to the Group and we can measure reliably the revenue and costs. We record our income as follows:

(i) Levies

We record levies from SEHK and HKFE as income on an accrual basis.

(ii) Fees and charges

We recognise annual fees as income on a straight-line basis over the periods to which they relate. We record other fees and charges as income when they are receivable.

(iii) Interest income

We record interest income as it accrues using the effective interest method. It comprises (a) interest earned on bank deposits and debt securities; and (b) the amortisation of premiums or discounts on purchases of held-to-maturity debt securities.

(iv) Revaluation gain/loss

Gains and losses from changes in fair value of financial assets are recognised in profit or loss as they arise.

(e) Operating leases

We treat the rent payable under operating leases as an expense in equal instalments over the accounting periods covered by the lease term. We recognise lease incentives received in the statement of profit or loss and other comprehensive income as an integral part of the aggregate net lease payments made.

(f) Employee benefits

We make accruals for salaries and allowances, annual leave and contributions to defined contribution schemes in the year in which the associated services are rendered by employees. Other benefits for services received are accrued when a contractual or constructive obligation arises for the Group.

(g) Fixed assets and depreciation

We state fixed assets at cost less accumulated depreciation and any impairment losses (see note 3(o)). We charge depreciation to the statement of profit or loss and other comprehensive income to write off the costs of fixed assets using the straight-line method over the estimated useful lives as follows:

Leasehold improvements	–	5 years or, if shorter, the life of the respective leases
Furniture and fixtures	–	3 to 5 years
Office equipment	–	5 years
Personal computers and software	–	3 years
Computer application systems	–	4 years
Motor vehicles	–	4 years

We capitalise subsequent expenditure only when it increases the future economic benefits embodied in the fixed assets. We recognise all other expenditure in the statement of profit or loss and other comprehensive income as an expense as incurred.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(g) Fixed assets and depreciation (cont'd)

We recognise gains or losses arising from the retirement or disposal of an item of fixed assets, being the difference between the net disposal proceeds and the carrying amount of the item, in the statement of profit or loss and other comprehensive income on the date of retirement or disposal.

(h) Financial instruments

(i) Initial recognition

We classify our financial instruments into different categories at inception, depending on the purpose for which the assets were acquired. The categories are: fair value through profit or loss, held-to-maturity, loans and receivables and other financial liabilities.

Investments in debt securities and equity funds are initially stated at fair value, which is their transaction price unless it is determined that the fair value at initial recognition differs from the transaction price and that fair value is evidenced by a quoted price in an active market for an identical asset or liability based on a valuation technique that uses only data from observable markets. Cost includes attributable transaction costs, except where indicated otherwise below. These investments are subsequently accounted for as follows, depending on their classification:

Investments in debt securities and equity funds that we manage, evaluate and report internally on a fair value basis are designated at fair value through profit or loss upon initial recognition and classified as current assets. Any attributable transaction costs are recognised in the statement of profit or loss and other comprehensive income as incurred. At the end of each reporting period the fair value is remeasured, with any resultant gain or loss being recognised in the statement of profit or loss and other comprehensive income. The net gain or loss recognised in the statement of profit or loss and other comprehensive income does not include any interest earned on these investments as these are recognised in accordance with the policies set out in note 3(d)(iii).

Dated debt securities that we have the positive ability and intention to hold to maturity are classified as held-to-maturity securities. Held-to-maturity securities are stated at amortised cost less impairment losses (see note 3(o)).

We use settlement date accounting to record regular purchase or sale of financial assets. From this date, we record in our books any gains and losses arising from changes in fair value of the financial assets held at fair value through profit or loss.

(ii) Fair value measurement principles

We determine the fair value of financial instruments based on their quoted market prices on a recognised stock exchange or a price from a broker/dealer for non-exchange-traded financial instruments at the end of the reporting period without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices. Unlisted equity investments are shares in equity funds. The fair value is determined based on the Group's share in the net assets of the equity funds as determined by the custodian.

(iii) Derecognition

We derecognise a financial asset when the contractual rights to receive the cash flows from the financial asset expire or where the financial asset together with substantially all the risks and rewards of ownership have been transferred.

(iv) Offsetting

We offset the financial assets and financial liabilities and report the net amount in the statement of financial position where there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(i) Related parties

For the purpose of these financial statements, we consider that the following are related parties of the Group:

(a) A person, or a close member of that person's family, is related to the Group if that person:

(i) has control or joint control over the Group;

(ii) has significant influence over the Group; or

(iii) is a member of the key management personnel of the Group.

(b) An entity is related to the Group if any of the following conditions applies:

(i) the entity and the Group are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

(iii) Both entities are joint ventures of the same third party.

(iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(v) The entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group.

(vi) The entity is controlled or jointly controlled by a person identified in (a).

(vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the Group.

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity. As the SFC is a statutory body with its Board members appointed by the Chief Executive of the Government of the Hong Kong Special Administrative Region under the SFO, any transactions with other government departments and agencies under normal dealings are not necessarily regarded as related party transactions in the context of HKAS 24 *Related party disclosures*.

(j) Translation of foreign currencies

We translate foreign currency transactions during the year into Hong Kong dollars at the exchange rates ruling at the transaction dates. We translate monetary assets and liabilities denominated in foreign currencies into Hong Kong dollars at the exchange rates ruling at the end of the reporting period. We recognise exchange gains and losses on translation in the statement of profit or loss and other comprehensive income.

(k) Debtors and other receivables

We state debtors and other receivables initially at their fair value and thereafter at amortised cost less impairment losses. We review the carrying amount of debtors and other receivables at the end of each reporting period to determine whether there is objective evidence of impairment. If any such evidence exists, we reduce the carrying amount to the estimated recoverable amount by means of a charge to the statement of profit or loss and other comprehensive income (see note 3(o)).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(l) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand, demand deposits with banks and other financial institutions.

(m) Creditors and accrued charges

We state creditors and accrued charges initially at fair values and thereafter at amortised cost unless the effect of discounting would be material, in which case they are stated at cost.

(n) Investment in subsidiaries

We state investment in a subsidiary at cost less any impairment losses in the statement of financial position.

(o) Impairment

We review the carrying amounts of the Group's assets at the end of each reporting period to determine whether there is any objective evidence of impairment. If any such evidence exists, we estimate the asset's recoverable amount, which is the higher of its net selling price and value in use. We recognise in the statement of profit or loss and other comprehensive income the difference between the asset's carrying amount and the recoverable amount as an impairment loss whenever the carrying amount of an asset exceeds its recoverable amount.

For held-to-maturity investments carried at amortised cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (ie, the effective interest rate computed at initial recognition of these assets), where the effect of discounting is material.

We reverse an impairment loss in respect of an asset in a subsequent period if the circumstances and events that are objectively linked to the write down or write-off cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future. We reverse an impairment loss only to the extent that the asset's carrying amount does not exceed the carrying amount that we should have determined, net of depreciation and amortisation, if we had not recognised any impairment loss.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(p) Provisions and contingent liabilities

We recognise a provision in the statement of financial position when the Group has a legal or constructive obligation of uncertain timing or amount as a result of a past event, and it is probable that the Group will require an outflow of economic benefits to settle the obligation and the amount can be estimated reliably.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, we disclose the obligation as a contingent liability, unless the probability of outflow of economic benefits is remote. We also disclose possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events as contingent liabilities unless the probability of outflow of economic benefits is remote.

(q) Changes in accounting policies

The HKICPA has issued a number of amendments to HKFRSs that are first effective for the current accounting period of the Group. None of these developments have had a material effect on how the Group's results and financial position for the current or prior periods have been prepared or presented.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

4. Taxation

Section 3(3) of the SFO exempts the SFC from Hong Kong taxes.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

5. Investment income

	2018 $'000	2017 $'000
Interest income fom bank deposits	62,439	62,501
Interest income from financial assets designated at fair value through profit or loss	14,930	11,124
Interest income from held-to-maturity debt securities	13,788	4,293
Realised (loss)/gain on disposal of equity securities	(6,966)	483
Loss on redemption/disposal of debt securities	(512)	(230)
Gain on revaluation of equity securities	206,167	132,484
Loss on revaluation of debt securities	(9,894)	(6,857)
Amortisation of premium on held-to-maturity debt securities	(1,366)	(1,175)
Amortisation of discount on held-to-maturity debt securities	298	–
	278,884	202,623

6. Other income

	2018 $'000	2017 $'000
Investigation costs awarded	379	258
Sale of SFC publications	129	250
Exchange gain	33,410	–
Others	675	17
	34,593	525

7. Staff costs and directors' emoluments

	2018 $'000	2017 $'000
Salaries and allowances	1,166,333	1,093,961
Retirement benefits	76,620	71,253
Medical and life insurance	32,757	30,718
Staff functions	1,724	1,787
Recruitment	3,318	2,669
Registration and membership fees	1,641	1,548
	1,282,393	1,201,936

The total number of staff as at 31 March 2018 was 912 (887 for the SFC, 22 for the Investor Education Centre and three for the Investor Compensation Company Limited) (as at 31 March 2017: the total number of staff was 891 comprising 866 for the SFC, 22 for the Investor Education Centre and three for the Investor Compensation Company Limited).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

7. Staff costs and directors' emoluments (cont'd)

Directors' emoluments included in the above comprised:

	Directors' fee $'000	Salaries, allowances and benefits in kind $'000	Discretionary pay $'000	Retirement scheme contributions[1] $'000	2018 Total $'000	2017 Total $'000
Chief Executive Officer						
Ashley Alder, JP	–	6,976	2,302	697	9,975	9,731
Executive Directors						
Thomas Atkinson (appointed 3 May 2016)	–	4,500	1,170	450	6,120	5,500
Christina Choi (appointed 1 August 2016)	–	4,200	1,092	420	5,712	3,808
Brian Ho	–	4,725	1,181	472	6,378	6,378
Julia Leung, SBS[2]	–	4,552	1,282	455	6,289	6,368
Keith Lui	–	4,725	1,181	472	6,378	6,378
James Shipton (retired 19 June 2016)	–	–	–	–	–	1,435
	–	29,678	8,208	2,966	40,852	39,598
Non-executive Chairman						
Carlson Tong, SBS, JP	1,012	–	–	–	1,012	1,012
Non-executive Directors						
Au Siu Cheung, Albert, BBS	253	–	–	–	253	253
Professor Leonard Cheng Kwok-hon, JP (retired 31 December 2016[3])	–	–	–	–	–	190
Edward Cheng Wai-sun, SBS, JP (appointed 1 January 2017)	253	–	–	–	253	63
Lester Garson Huang, JP	253	–	–	–	253	253
Teresa Ko, JP	253	–	–	–	253	253
Mary Ma Xuezheng	253	–	–	–	253	253
Dr Kelvin Wong Tin-yau, JP	253	–	–	–	253	253
Dr William Wong Ming-fung	253	–	–	–	253	253
	2,783	–	–	–	2,783	2,783
Total directors' emoluments	2,783	29,678	8,208	2,966	43,635	42,381

1 This represents net contribution expenses accrued during the year ended 31 March 2018 in accordance with the accounting policy set out in note 3(f) on page 107. The future payment of contributions is subject to completion of a vesting period, which is based on total years of service with the SFC. The amount vested as at 31 March 2018 was $1,920,000 (as at 31 March 2017: $1,595,000).

2 Ms Julia Leung is re-appointed as Executive Director (Intermediaries) and Deputy Chief Executive Officer with effect from 2 March 2018. Her 2017/18 discretionary pay covered the period from 1 April 2017 to 1 March 2018.

3 Retired having completed his appointment period of six years.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

7. Staff costs and directors' emoluments (cont'd)

The aggregate of the emoluments of the five highest paid individuals in 2017/18, representing the emoluments of the Chief Executive Officer and four Executive Directors, was $35,140,000 (2016/17: $34,355,000) with the breakdown as follows:

	2018 $'000	2017 $'000
Salaries, allowances and benefits in kind	25,478	24,855
Discretionary pay	7,116	7,051
Retirement scheme contributions	2,546	2,449
	35,140	34,355

Their emoluments are within the following bands:

	2018 No. of individuals	2017 No. of individuals
$5,500,001 to $6,000,000	0	1
$6,000,001 to $6,500,000	4	3
$6,500,001 to $7,000,000	0	0
$7,000,001 to $7,500,000	0	0
$7,500,001 to $8,000,000	0	0
$8,000,001 to $8,500,000	0	0
$8,500,001 to $9,000,000	0	0
$9,000,001 to $9,500,000	0	0
$9,500,001 to $10,000,000	1	1

Employee benefits

We provide retirement benefits to our staff through a defined contribution scheme under the Occupational Retirement Schemes Ordinance (ORSO Scheme) and a Mandatory Provident Fund Scheme (MPF Scheme). Prior to the inception of the MPF Scheme, all general grade staff were included in the Group's ORSO Scheme. Following the introduction of the MPF Scheme in December 2000, new general grade staff have since been covered under the MPF Scheme while executive staff have been allowed to opt for either the Group's ORSO Scheme or the MPF Scheme.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

7. Staff costs and directors' emoluments (cont'd)

Employee benefits (cont'd)

(a) ORSO Scheme

(i) General grade staff

For general grade staff, we make monthly contributions equal to 12% of the fixed pay, subject to a vesting scale with the benefit fully vested upon completion of 10 years' service. We reinvest forfeited contributions for general grade staff who leave the Group prior to qualifying for 100% disbursement of the contributions into the total pool of contributions that will be shared by the existing members in the scheme at the end of the scheme year. The amount so reinvested during the year was nil (2017: nil).

(ii) Executive staff

For executive staff, we make monthly contributions between 5% to 10% of the fixed pay. We use forfeited contributions in respect of executive staff who leave the Group prior to qualifying for 100% disbursement of the contributions to offset the Group's future contributions. The amount so forfeited during the year was $5,020,000 (2017: $2,182,000) and the amount so forfeited available at the end of the reporting period was $2,793,000 (2017: $416,000).

This scheme has obtained an exemption under Section 5 of the MPF Schemes Ordinance.

(b) MPF Scheme

We have participated in a master trust MPF Scheme since December 2000 and made contributions to the MPF Scheme in accordance with the statutory requirements of the MPF Schemes Ordinance.

8. Other expenses

	2018 $'000	2017 $'000
Learning and development	7,877	6,728
Legal and professional services	80,760	82,999
Information and systems services	56,578	49,558
Auditor's remuneration	790	762
Funding for the Financial Reporting Council	8,092	7,706
Funding for the Hong Kong Securities and Investment Institute and other training initiatives	–	7,000
Funding for the International Financial Reporting Standards Foundation	392	389
General office and insurance	8,837	8,779
Investor and other education programme costs to the Investor Education Centre	32,294	33,754
Overseas travelling, regulatory meeting expenses and others	11,348	12,322
Exchange loss	–	1,590
Loss on disposal of fixed assets	719	7
	207,687	211,594

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

9. Held-to-maturity debt securities

The Group and the SFC

		2018 $'000	2017 $'000
Maturing after one year in the second to sixth years	– unlisted	**78,844**	–
	– listed in Hong Kong	**344,171**	–
	– listed outside Hong Kong	**1,123,598**	–
		1,546,613	–
Maturing within one year	– unlisted	**35,503**	30,003
		35,503	30,003
		1,582,116	30,003
Amortised cost at 31 March	– unlisted	**114,347**	30,003
	– listed in Hong Kong	**344,171**	–
	– listed outside Hong Kong	**1,123,598**	–
		1,582,116	30,003
Market value at 31 March	– unlisted	**112,219**	30,006
	– listed in Hong Kong	**340,161**	–
	– listed outside Hong Kong	**1,107,059**	–
		1,559,439	30,006

The average yield to maturity of the debt securities was 3.0% as at 31 March 2018 (2017: 1.6%).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

10. Financial assets designated at fair value through profit or loss

	2018 $'000	2017 $'000
(a) Debt securities		
(i) Listing status		
Listed – outside Hong Kong	354,464	409,624
Listed – in Hong Kong	30,285	18,444
Unlisted	387,551	288,335
	772,300	716,403
(ii) Maturity profile		
Within one year	99,335	201,264
After one year but within two years	310,433	157,288
After two years but within five years	344,569	347,274
After five years	17,963	10,577
	772,300	716,403
(iii) The weighted average effective interest rate of debt securities on 31 March 2018 was 2.3% (2017: 1.8%).		
(b) Pooled funds – unlisted	934,768	941,911

The pooled funds comprise mainly listed equity securities.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

11. Fixed assets

(a) The Group

	Furniture, fixtures and leasehold improvements $'000	Office equipment $'000	Computer application systems $'000	Personal computers and software $'000	Motor vehicles $'000	Total $'000
Cost						
At 1 April 2017	122,301	10,482	211,563	122,347	2,411	469,104
Additions	6,576	490	24,439	7,536	324	39,365
Disposals	(2,687)	(212)	(890)	(3,909)	–	(7,698)
At 31 March 2018	126,190	10,760	235,112	125,974	2,735	500,771
Accumulated depreciation						
At 1 April 2017	110,280	8,884	179,757	104,317	2,411	405,649
Charge for the year	4,907	598	13,560	11,045	68	30,178
Written back on disposals	(1,989)	(191)	(890)	(3,909)	–	(6,979)
At 31 March 2018	113,198	9,291	192,427	111,453	2,479	428,848
Net book value						
At 31 March 2018	12,992	1,469	42,685	14,521	256	71,923
Cost						
At 1 April 2016	118,584	10,007	191,836	113,130	2,411	435,968
Additions	3,728	554	20,075	12,607	–	36,964
Disposals	(11)	(79)	(348)	(3,390)	–	(3,828)
At 31 March 2017	122,301	10,482	211,563	122,347	2,411	469,104
Accumulated depreciation						
At 1 April 2016	89,936	7,653	166,407	96,565	2,160	362,721
Charge for the year	20,355	1,309	13,698	11,136	251	46,749
Written back on disposals	(11)	(78)	(348)	(3,384)	–	(3,821)
At 31 March 2017	110,280	8,884	179,757	104,317	2,411	405,649
Net book value						
At 31 March 2017	12,021	1,598	31,806	18,030	–	63,455

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

11. Fixed assets (Cont'd)

(b) The SFC

	Furniture, fixtures and leasehold improvements $'000	Office equipment $'000	Computer application systems $'000	Personal computers and software $'000	Motor vehicles $'000	Total $'000
Cost						
At 1 April 2017	122,286	10,413	211,563	120,974	2,411	467,647
Additions	6,575	490	24,439	7,505	324	39,333
Disposals	(2,687)	(212)	(890)	(3,750)	–	(7,539)
At 31 March 2018	126,174	10,691	235,112	124,729	2,735	499,441
Accumulated depreciation						
At 1 April 2017	110,264	8,821	179,757	103,227	2,411	404,480
Charge for the year	4,907	592	13,560	10,795	68	29,922
Written back on disposals	(1,989)	(191)	(890)	(3,750)	–	(6,820)
At 31 March 2018	113,182	9,222	192,427	110,272	2,479	427,582
Net book value						
At 31 March 2018	12,992	1,469	42,685	14,457	256	71,859
Cost						
At 1 April 2016	118,569	9,938	191,836	111,770	2,411	434,524
Additions	3,728	554	20,075	12,594	–	36,951
Disposals	(11)	(79)	(348)	(3,390)	–	(3,828)
At 31 March 2017	122,286	10,413	211,563	120,974	2,411	467,647
Accumulated depreciation						
At 1 April 2016	89,920	7,592	166,407	95,744	2,160	361,823
Charge for the year	20,355	1,307	13,698	10,867	251	46,478
Written back on disposals	(11)	(78)	(348)	(3,384)	–	(3,821)
At 31 March 2017	110,264	8,821	179,757	103,227	2,411	404,480
Net book value						
At 31 March 2017	12,022	1,592	31,806	17,747	–	63,167

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

12. Bank deposits and cash at bank

The effective interest rate on bank deposits as at 31 March 2018 ranged from 0.5% to 2.25% (2017: 0.15% to 3.6%). These balances mature within one year as at both 31 March 2018 and 31 March 2017.

Reconciliation with the consolidated statement of financial position

	2018 $'000	2017 $'000
Cash at bank and in hand	33,353	75,462
Fixed deposits with banks	3,713,477	5,107,808
Amounts shown in the consolidated statement of financial position	3,746,830	5,183,270
Less: Amounts with an original maturity of beyond three months	(3,454,725)	(4,506,543)
Cash and cash equivalents in the consolidated cash flow statement	292,105	676,727

13. Investments in subsidiaries

The SFC formed Investor Compensation Company Limited (ICC) on 11 September 2002 with an issued share capital of $0.2. On 20 November 2012, the SFC launched the Investor Education Centre (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 established under the 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 March 2018, the investments in subsidiaries, which are stated at cost less any impairment losses, amounted to $0.2 (2017: $0.2). The balance is too small to appear on the statement of financial position which is expressed in thousands of dollars.

14. Creditors and accrued charges

Creditors and accrued charges mainly include accruals and payables to creditors relating to operating expenses. Payables are usually due within one year.

15. Non-current liabilities

Non-current liabilities represent provision for premises reinstatement cost to restore the premises to its original condition when the lease has expired.

16. Debtors, deposits and prepayments

Debtors, deposits and prepayments include $201,619,000 receivables classified as loans and receivables in accordance with the determination of HKAS 39, *Financial instruments: Recognition and measurement* (2017: $141,623,000). Receivables are usually due within 30 days. Receivables mainly comprise levies receivables.

We do not provide an ageing analysis of debtors as there was no material overdue debtor balance included in "debtors, deposits and prepayments" as at 31 March 2018 and 2017.

17. Initial funding by Government

The Government provided funds to pay for the SFC's initial non-recurrent and capital expenditure. These funds are not repayable to the Government.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

18. Capital commitments

Capital commitments for fixed assets contracted for at the end of the year but not yet incurred amounted to $37,286,000 (2017: $19,969,000).

19. Commitment to pay rents for offices

At 31 March 2018 the minimum amount we are committed to pay in rent for our offices up to 31 August 2020 are as follows:

	The Group and the SFC	
	2018 $'000	2017 $'000
Payable next year	200,457	205,077
Payable in one to five years	284,069	477,534
Payable in more than five years	–	–
	484,526	682,611

During the year ended 31 March 2018, $204,381,000 net of lease incentives, was recognised as an expense in the statement of profit or loss and other comprehensive income in respect of operating leases (2017: $208,744,000).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

20. Related party transactions

We have related party relationships with the Unified Exchange Compensation Fund (UECF), the Investor Compensation Fund (ICF), Securities Ordinance (Chapter 333) – Dealers' Deposits Fund (SDD), Commodities Trading Ordinance (Chapter 250) – Dealers' Deposits Fund (CDD) and Securities Ordinance (Chapter 333) – Securities Margin Financiers' Security Fund (SMF). In addition to the related parties relationship disclosed in note 22 in these financial statements, we have the following significant related party transactions and balances.

(a) Reimbursement from the ICF for all the ICC's expenses, in accordance with Section 242(1) of the SFO

During the year, $5,729,000 was recovered from the ICF for the ICC's expenses (2017: $5,574,000). As at 31 March 2018, the amount due to the ICF from the ICC was $203,000 (as at 31 March 2017: $75,000).

(b) Remuneration of key management personnel

We consider that the directors' emoluments as disclosed in note 7 are the only remuneration for key management personnel of the Group.

21. Financial risk management and fair values

Financial instruments of the Group mainly comprise debt securities and units in equity funds. The underlying investments of the equity funds mainly comprised equity securities.

The main financial risks of the Group arise from its investments in debt securities and units in equity funds. The Group appoints external investment managers to manage the Group's investments and to ensure that the portfolio's investments comply with the investment policy approved by the Financial Secretary which sets control limits on credit risk, market risk, interest rate risk, liquidity risk and foreign exchange risk. The external investment managers report thereon to the Group on a regular basis.

The Group's exposure to these risks and the financial risk management policies and practices used by the Group to manage these risks are described below.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

21. Financial risk management and fair values (Cont'd)

(a) Credit risk

The Financial Secretary has approved our investment policy which, subject to other control limits, allows the Group to invest in dated securities rated A or above and bank deposits with licensed banks rated P-1 or A-1 by Moody's or S&P respectively. Investment in unit trusts and mutual funds authorised as collective investment schemes under Section 104 of the SFO up to 15% of the total value of funds under management is permitted. The policy also limits the exposure to 10% for each organisation and 20% for each country, except for the holdings of US Treasuries. During the year, the Group complied with the above investment policy in order to manage its credit risk, and as a result, was not exposed to significant credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the statement of financial position after deducting any impairment allowance.

(b) Interest rate risk

The Group's interest bearing assets mainly comprise fixed interest rate bearing debt securities and bank balances. The Group is subject to the risk that future cash flows from re-investments will fluctuate because of changes in market interest rates (re-pricing risk). The Group manages re-pricing risk of its fixed rate debt securities by imposing different levels of concentration and maturity limits to the investments. The effective interest rates and maturity profile of the Group's interest bearing assets are disclosed in the respective notes to the financial statements. As at 31 March 2018, it is estimated that a general increase/decrease of 100 basis points, with all other variables held constant, would increase/decrease the Group's interest income and accumulated surplus by approximately $37,610,000 (2017: $52,501,000). As at 31 March 2018 the average duration of the Group's investment portfolio was 1.84 years (31 March 2017: 1.64 years). At 31 March 2018, it is estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would decrease/increase the Group's gains on revaluation of mark to market debt securities and the accumulated surplus by approximately $14,543,000 (2017: $12,110,000).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

21. Financial risk management and fair values (Cont'd)

(b) Interest rate risk (Cont'd)

The sensitivity analysis above is estimated as an annualised impact on interest income assuming the change in interest rates had occurred at the end of the reporting period. The analysis is performed on the same basis for 2017.

(c) Exchange rate risk

The Group'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, the Group was not exposed to significant foreign exchange risk at the end of the reporting period.

(d) Market risk

The investment activities of the Group expose it to various types of market risks which are associated with the markets in which it invests, to the extent of the amount invested in debt securities and equity funds. Such risk will be reflected in the price and the carrying value of the financial assets concerned.

The Group invests in units of equity funds, which mainly comprised listed equity securities, the performance of which is measured against the results of benchmark indices, MSCI AC Asia Free ex Japan and MSCI World (Net Dividends), including their returns and volatilities. Based on the weighted average movement of these benchmark indices (12.4%) in the corresponding period, it is estimated that a general increase/decrease of such benchmark indices of 12.4% (2017: 9.8%) would increase/decrease the Group's investment income and the accumulated surplus by approximately $122,813,000 (2017: $102,912,000).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

21. Financial risk management and fair values (Cont'd)

(d) Market risk (Cont'd)

The sensitivity analysis above indicates the instantaneous change in the Group's accumulated surplus that would arise assuming that the changes in the benchmark indices had occurred at the end of the reporting period and had been applied to re-measure those financial instruments held by the Group which expose the Group to equity price risk at the end of the reporting period. It is also assumed that the fair values of the Group's investment in equity funds would change in accordance with the historical correlation with the relevant benchmark indices since the portfolio is diversified in terms of industry distribution and that all other variables remain constant.

(e) Fair value measurement

(i) Financial assets measured at fair value

The following table presents the fair value of the Group's financial instruments measured at the end of the reporting period on a recurring basis, categorised into the three-level fair value hierarchy as defined in HKFRS 13, *Fair value measurement*. The level into which a fair value measurement is classified is determined with reference to the observability and significance of the inputs used in the valuation technique as follows:

- Level 1 valuations: Fair value measured using only Level 1 inputs ie, unadjusted quoted prices in active markets for identical assets or liabilities at the measurement date.
- Level 2 valuations: Fair value measured using only Level 2 inputs ie, observable inputs which fail to meet Level 1, and not using significant unobservable inputs. Unobservable inputs are inputs for which market data are not available.
- Level 3 valuations: Fair value measured using significant unobservable inputs.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

21. Financial risk management and fair values (Cont'd)

(e) Fair value measurement (Cont'd)

(i) Financial assets measured at fair value (Cont'd)

	2018			
	Level 1 $'000	Level 2 $'000	Level 3 $'000	Total $'000
Assets				
Debt securities				
– Listed	–	384,749	–	384,749
– Unlisted	–	387,551	–	387,551
Pooled funds				
– Unlisted	934,768	–	–	934,768
	934,768	772,300	–	1,707,068

	2017			
	Level 1 $'000	Level 2 $'000	Level 3 $'000	Total $'000
Assets				
Debt securities				
– Listed	–	428,068	–	428,068
– Unlisted	–	288,335	–	288,335
Pooled funds				
– Unlisted	941,911	–	–	941,911
	941,911	716,403	–	1,658,314

The fair value of the investment in the unlisted pooled funds is determined based on the Group's share in the net assets of the pooled funds as determined by the custodian which is publicly available in the market. The majority of the underlying assets of the pooled funds are listed securities.

Changes in the market conditions could materially affect fair value estimates. Any increase or decrease in the fair values of financial instruments would affect profit or loss in future years.

During the year there were no significant transfers between financial instruments in Level 1 and 2, or transfers into or out of Level 3. The Group's policy is to recognise transfers between levels of fair value hierarchy as at the end of the reporting period in which they occur.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

21. Financial risk management and fair values (Cont'd)

(e) Fair value measurement (Cont'd)

(ii) Fair value of financial assets carried at other than fair value

The carrying amounts of the Group's financial instruments carried at cost or amortised cost are not materially different from their fair values as at 31 March 2018 and 2017 except for the following financial instruments, for which their carrying amounts and fair value and the level of fair value hierarchy are disclosed below:

	Carrying amount at 31 March 2018 $'000	Fair value at 31 March 2018 $'000	2018 Level 1 $'000	2018 Level 2 $'000	2018 Level 3 $'000
Held-to-maturity debt securities	**1,582,116**	**1,559,439**	**1,559,439**	**–**	**–**

	Carrying amount at 31 March 2017 $'000	Fair value at 31 March 2017 $'000	2017 Level 1 $'000	2017 Level 2 $'000	2017 Level 3 $'000
Held-to-maturity debt securities	30,003	30,006	30,006	–	–

The following summarises the major methods and assumptions used in estimating the fair values of these financial instruments.

- The fair value of listed held-to-maturity debt securities is based on quoted market prices at the end of the reporting period using current bid prices without any deduction for transaction costs. Fair value for unlisted debt investments are based on third-party quotes.

22. Sponsored unconsolidated structured entities

The SFC considers the ICF, UECF, SDD, CDD and SMF as unconsolidated structured entities sponsored by the SFC where no interests are held by the SFC.

Pursuant to Section 236 of the SFO, the SFC has established and maintained the ICF to compensate investors who suffer a loss due to the default of an intermediary in relation to trading of products on Hong Kong Exchanges and Clearing Limited. The SFC is primarily responsible for the administration and management of the ICF in accordance with Section 238 of the SFO, but has transferred some functions to the ICC under Section 80 of the SFO. According to Section 237(2)(b) of the SFO, the SFC may, with the consent in writing of the Financial Secretary, pay into the ICF from its reserves such amount of money as it considers appropriate. As at 31 March 2018, the ICF's maximum liability in respect of claims received was $2,375,000 (2017: $3,034,000) and the net asset value was $2.4 billion (2017: $2.3 billion).

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

22. Sponsored unconsolidated structured entities (Cont'd)

The SFC is also responsible for the administration and management of the UECF, SDD, CDD and SMF under respective provisions in the repealed Securities Ordinance and Commodities Trading Ordinance. These funds provide compensation to investors who suffer a loss due to the default of an intermediary occurring before 1 April 2003 when the SFO came into effect. As at 31 March 2018, the UECF's maximum liability in respect of claims received was $10,245,000 (2017: $10,607,000) and the net asset value was $75,804,000 (2017: $72,891,000). There were no outstanding claims against the SDD, CDD and SMF as at 31 March 2018. Claims for any defaults occurring after 31 March 2003 should be made against the ICF.

During the year, the SFC has not provided financial or other support to these unconsolidated structured entities that it was not contractually required to provide (2017: nil). The related party relationships with these entities are disclosed in note 20 of these financial statements.

23. Funding and reserve management

The SFC manages its funding requirements from its income and accumulated surplus. Apart from the initial funding by the Government as disclosed in note 17, the SFC is eligible to receive an appropriation from the Government in each financial year. Since the financial year ended 31 March 1994, the SFC has requested the Government not to make an appropriation to it. There were no externally imposed capital requirements to which the SFC is subject to.

The SFC has earmarked $3 billion from its accumulated surplus to set up a reserve for the possible future acquisition of office premises. The SFC's investment holdings and available cash balances will be used to support this reserve.

24. Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 March 2018

Up to the date of issue of these financial statements, the HKICPA has issued a number of amendments and new standards which are not yet effective for the year ended 31 March 2018 and which have not been adopted in these financial statements. These include the following which may be relevant to the Group.

	Effective for accounting periods beginning on or after
HKFRS 9, *Financial instruments*	1 January 2018
HKFRS 15, *Revenue from contracts with customers*	1 January 2018
HKFRS 16, *Leases*	1 January 2019

The Group is in the process of making an assessment of what the impact of these amendments and new standards is expected to be in the period of initial application. So far the Group has identified some aspects of the new standards which may have a significant impact on the consolidated financial statements.

HKFRS 9 introduces new requirements for classification and measurement of financial assets, calculation of impairment of financial assets and hedge accounting. Based on the preliminary assessment, the Group expects that its financial assets currently measured at amortised cost and fair value through profit or loss will continue with their respective classification and measurements upon the adoption of HKFRS 9.

Notes to the Consolidated Financial Statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

24. Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 March 2018 (Cont'd)

The new impairment model requires the recognition of impairment provisions on the Group's financial assets classified as amortised cost based on expected credit losses rather than only incurred credit losses as is the case under HKAS 39. Based on the assessments undertaken to date, the Group expects that the adoption of the new standard would not have a significant effect on the loss allowance in relation to debt investments held at amortised cost.

HKFRS 15 establishes a comprehensive framework for determining when to recognise revenue and how much revenue to recognise. The core principle is that a company should recognise revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The Group has assessed the impact of this new standard and expects that it will not have a significant effect on the consolidated statements.

HKFRS 16 primarily affects the Group's accounting as a lessee of leases for properties which are currently classified as operating leases. The application of the new accounting model is expected to lead to an increase in both assets and liabilities and to impact on the timing of the expense recognition in the statement of profit or loss over the period of the lease. However, a more detailed analysis of what the impact of the new standard is required to determine the exact extent of this impact.

Investor Compensation Fund

Report of the Investor Compensation Fund Committee

The members of the Investor Compensation Fund Committee (the Committee) present their annual report together with the audited financial statements for the year ended 31 March 2018.

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 financial year ended 31 March 2018 and the financial position of the Fund as at that date are set out in the financial statements on pages 133 to 148.

Members of the Committee

The members of the Committee during the year ended 31 March 2018 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 of the Fund had a material interest, subsisted at the end of the financial year or at any time during the financial year.

Auditor

PricewaterhouseCoopers (PwC) retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of PwC as auditor of the Fund is to be proposed at the forthcoming committee meeting.

By order of the Committee

Keith Lui
Chairman

1 June 2018

Independent auditor's report
To the Securities and Futures Commission

Opinion

What we have audited

The financial statements of Investor Compensation Fund (the Fund) established under Part XII of the Securities and Futures Ordinance set out on pages 133 to 148, which comprise:

- the statement of financial position as at 31 March 2018;
- the statement of profit or loss and other comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the cash flow statement for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Fund as at 31 March 2018, and of its financial performance and its cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards (HKFRSs) issued by the Hong Kong Institute of Certified Public Accountants (HKICPA).

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (HKSAs) issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Fund in accordance with the HKICPA's Code of Ethics for Professional Accountants (the Code), and we have fulfilled our other ethical responsibilities in accordance with the Code.

Other information

The directors of the Securities and Futures Commission (SFC) are responsible for the other information. The other information comprises all of the information included in the annual report, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of directors of the SFC for the financial statements

The directors of the SFC are responsible for the preparation of the financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA, and for such internal control as the directors of the SFC determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors of the SFC are responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors of the SFC either intend to liquidate the Fund or to cease operations, or have no realistic alternative but to do so.

Independent auditor's report (continued) To the Securities and Futures Commission

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with HKSAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors of the SFC.

- Conclude on the appropriateness of the directors of the SFC's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the directors of the SFC regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 1 June 2018

Statement of profit or loss and other comprehensive income

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Income			
Net investment income	5	73,603	77,141
Exchange difference		16,504	3,110
Recoveries		1,620	1
		91,727	80,252
Expenses			
Investor Compensation Company Limited expenses	7	5,729	5,574
Compensation expenses	8	–	182
Auditor's remuneration		166	160
Bank charges		968	967
Professional fees		4,120	3,842
		10,983	10,725
Surplus and total comprehensive income for the year		80,744	69,527

The notes on pages 137 to 148 form part of these financial statements.

Statement of financial position

At 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Current assets			
Financial assets designated at fair value through profit or loss			
– Debt securities	9	1,939,279	1,893,248
– Pooled fund	9	350,084	330,386
Interest receivable		17,015	13,651
Due from Investor Compensation Company Limited		203	75
Fixed deposits with banks	10	52,586	26,201
Cash at bank	10	3,347	18,770
		2,362,514	2,282,331
Current liabilities			
Provision for compensation	8	–	476
Creditors and accrued charges		1,364	1,449
		1,364	1,925
Net current assets		2,361,150	2,280,406
Net assets		2,361,150	2,280,406
Representing:			
Compensation fund			
Contributions from Unified Exchange Compensation Fund	11	994,718	994,718
Contributions from Commodity Exchange Compensation Fund	11	108,923	108,923
Accumulated surplus		1,257,509	1,176,765
		2,361,150	2,280,406

Approved and authorised for issue by the Securities and Futures Commission on 1 June 2018 and signed on its behalf by

Carlson Tong
Chairman of the SFC

Ashley Alder
Chief Executive Officer of the SFC

The notes on pages 137 to 148 form part of these financial statements.

Statement of changes in equity

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	Contributions from Unified Exchange Compensation Fund $'000	Contributions from Commodity Exchange Compensation Fund $'000	Accumulated surplus $'000	Total $'000
Balance at 1 April 2016	994,718	108,923	1,107,238	2,210,879
Surplus and total comprehensive income for the year	–	–	69,527	69,527
Balance at 31 March 2017 and 1 April 2017	994,718	108,923	1,176,765	2,280,406
Surplus and total comprehensive income for the year	–	–	80,744	80,744
Balance at 31 March 2018	994,718	108,923	1,257,509	2,361,150

The notes on pages 137 to 148 form part of these financial statements.

Cash flow statement

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	2018 $'000	2017 $'000
Cash flows from operating activities		
Surplus for the year	80,744	69,527
Adjustments for:		
Net investment income	(73,603)	(77,141)
Exchange difference	(16,504)	(3,110)
	(9,363)	(10,724)
Increase in amount due from Investor Compensation Company Limited	(128)	(2)
Decrease in provision for compensation	(476)	(936)
(Decrease)/increase in creditors and accrued charges	(85)	73
Net cash used in operating activities	(10,052)	(11,589)
Cash flows from investing activities		
Debt securities purchased	(1,100,731)	(536,658)
Debt securities sold or redeemed	1,037,862	494,332
Equity securities sold	36,789	1,455
Interest received	47,094	46,468
Net cash generated from investing activities	21,014	5,597
Net increase/(decrease) in cash and cash equivalents	10,962	(5,992)
Cash and cash equivalents at beginning of the year	44,971	50,963
Cash and cash equivalents at end of the year	55,933	44,971

Analysis of the balance of cash and cash equivalents

	2018 $'000	2017 $'000
Fixed deposits with banks	52,586	26,201
Cash at bank	3,347	18,770
	55,933	44,971

The notes on pages 137 to 148 form part of these financial statements.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

1. Purpose, limitation and principal activity

The Securities and Futures Ordinance (SFO) provides for the establishment of the Investor Compensation Fund (the Fund) to compensate investors who suffer a loss due to the default of an intermediary in relation to trading of products on Hong Kong Exchanges and Clearing Limited. The defaulting intermediary must be licensed by or registered with the Securities and Futures Commission (SFC) for dealing in securities, futures contracts or securities margin financing.

The SFC is primarily responsible for the administration and management of the Fund in accordance with Section 238 of the SFO, but has transferred some functions to the Investor Compensation Company Limited (ICC) under Section 80 of the SFO. The ICC is thus responsible for receipt, determination and payment of valid claims against the Fund in respect of defaults of intermediaries occurring on or after 1 April 2003. Upon making payment to a claimant, the SFC is subrogated to the claimant's right against the defaulter.

Pursuant to Section 244 of the SFO, the Chief Executive in Council has by order set the maximum amount of compensation at $150,000 per claimant for a single default in relation to securities traded at The Stock Exchange of Hong Kong Limited (SEHK) or futures contracts traded at Hong Kong Futures Exchange Limited (HKFE).

If amounts owed to claimants against the Fund exceed the Fund's net assets, the SFC would apportion compensation payments to claimants as provided in the Securities and Futures (Investor Compensation-Claims) Rules. The SFC would pay unpaid claim amounts when funds become available in the Fund.

2. Money constituting the Fund

The Fund mainly consists of the amounts paid from the two compensation funds, the Unified Exchange Compensation Fund (UECF) and the Commodity Exchange Compensation Fund (CECF) (wound up on 26 May 2006). The SFC will also pay into the Fund any remaining balance in the Securities Dealers' Deposits Fund, the Commodities Dealers' Deposits Fund and the Securities Margin Financiers' Security Fund after repaying the dealers' deposits and any money due to the registered dealers in accordance with Section 76(11) of Schedule 10 of the SFO though it is not likely that these payments will be made within the coming year.

Other sources of money for the Fund include the levies chargeable on securities traded on SEHK and futures contracts traded on HKFE (see also note 6), and returns earned on the investment of the Fund (see also note 5).

3. Significant accounting policies

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards (HKFRSs), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (HKASs) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (HKICPA) and accounting principles generally accepted in Hong Kong. A summary of the significant accounting policies adopted by the Fund is set out below.

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for the current accounting period of the Fund. Note 3(m) provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Fund for the current and prior accounting periods reflected in these financial statements.

The Fund has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 15).

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(b) Basis of preparation

We have prepared these financial statements using the historical cost basis as the measurement basis, except that we state financial instruments classified as designated at fair value through profit or loss at their fair value (see note 3(e)).

We prepare the financial statements in conformity with HKFRSs which require management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. We make estimates and associated assumptions based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

We review estimates and underlying assumptions on an ongoing basis. We recognise revisions to accounting estimates in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

(c) Recognition of income

We recognise income in the statement of profit or loss and other comprehensive income provided it is probable that the economic benefits will flow to the Fund and we can measure reliably the revenue and costs. We record interest income as it accrues using the effective interest method.

(d) Translation of foreign currencies

We translate foreign currency transactions during the year into Hong Kong dollars at the foreign exchange rates ruling at the transaction dates. We translate monetary assets and liabilities denominated in foreign currencies that are stated at fair value into Hong Kong dollars at the foreign exchange rates ruling at the end of the reporting period. We record exchange gains and losses on translation in the statement of profit or loss and other comprehensive income.

(e) Financial instruments

(i) Initial recognition

We classify the financial instruments into different categories at inception, depending on the purpose for which the assets were acquired or the liabilities were incurred. The categories are: fair value through profit or loss, loans and receivables and other financial liabilities.

We initially measure financial instruments at fair value, which normally will be equal to the transaction price, plus, in case of a financial asset or financial liability not held at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. We charge transaction costs on financial assets and financial liabilities at fair value through profit or loss immediately.

We account for financial assets and financial liabilities on the date the Fund becomes a party to the contractual provisions of the instrument. We use settlement date accounting to record regular purchase or sale of financial assets. From this date, we record in our books any gains and losses arising from changes in fair value of the financial assets or financial liabilities at fair value through profit or loss.

The Fund's financial instruments mainly consist of debt and equity securities designated at fair value through profit or loss. We state financial assets and liabilities under this category at fair value and recognise changes in the fair value in the statement of profit or loss and other comprehensive income in the period in which they arise. Upon disposal or repurchase, the difference between the net sale proceeds or the net payment and the carrying value is included in the statement of profit or loss and other comprehensive income.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(e) Financial instruments (cont'd)

(ii) Fair value measurement principles

We determine the fair value of financial instruments based on their quoted market prices on a recognised stock exchange or a price from a broker/dealer for non-exchange-traded financial instruments at the end of the reporting period without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices. Unlisted equity investments are shares in pooled funds. The fair value is determined based on the Fund's share in the net assets of the pooled funds as determined by the custodian.

(iii) Derecognition

We derecognise a financial asset when the contractual rights to receive the cash flows from the financial asset expire, or where the financial asset together with substantially all the risks and rewards of ownership have been transferred.

We derecognise a financial liability when the obligation specified in the contract is discharged, cancelled or expired.

(iv) Offsetting

We offset the financial assets and financial liabilities and report the net amount in the statement of financial position where there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(f) Impairment

The carrying amount of the Fund's assets are reviewed at each reporting period to determine whether there is objective evidence of impairment. Objective evidence that financial assets are impaired includes observable data that comes to the attention of the Fund about one or more of the following loss events which have an impact on the future cash flows of the assets that can be estimated reliably:

- significant financial difficulty of the issuer or borrower;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- significant changes in the technological, market, economic or legal environment that have an adverse effect on the borrower;
- disappearance of an active market for financial assets because of financial difficulties; and
- a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost.

If any such evidence exists, the carrying amount of financial assets held at amortised cost is reduced to the estimated recoverable amount by means of a charge to the statement of profit or loss and other comprehensive income.

(g) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and demand deposits with banks and other financial institutions.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(h) Other receivables

We state other receivables initially at fair value and thereafter at amortised cost less impairment losses (see note 3(f)), unless the effect of discounting would be immaterial, in which case we state them at cost less impairment losses.

(i) Provision for compensation

We make provision for liabilities arising from claims resulting from defaults for which it is probable that the Fund will require an outflow of economic benefits to settle the obligation and the amount can be estimated reliably, independent of whether a notice calling for claims pursuant to Section 3 of the Securities and Futures (Investor Compensation-Claims) Rules has been published. The provision covers all such claims received up to the date on which the financial statements are approved by the SFC. If the effect is material, we determine provisions by discounting the expected future cash flows that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

The maximum liability of the Fund to claims for each default case is set at $150,000 per claimant.

As the Fund is continually updating information in respect of claims received, it is possible that the recent claim experience is not indicative of future payments that will be required for claims received as at the end of the reporting period. Any increase or decrease in the provision would affect profit and loss in future years.

(j) Creditors and accrued charges

We state creditors and accrued charges initially at fair value and thereafter at amortised cost unless the effect of discounting would be immaterial, in which case we state them at cost.

(k) Provisions and contingent liabilities

We recognise a provision in the statement of financial position when the Fund has a legal or constructive obligation of uncertain timing or amount as a result of a past event, and it is probable that the Fund will require an outflow of economic benefits to settle the obligation and the amount can be estimated reliably.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, we disclose the obligation as a contingent liability, unless the probability of outflow of economic benefits is remote. We also disclose possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events as contingent liabilities unless the probability of outflow of economic benefits is remote.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(l) Related parties

For the purpose of these financial statements, a party is considered to be related to the Fund if:

(a) A person, or a close member of that person's family, is related to the Fund if that person:

(i) has control or joint control over the Fund;

(ii) has significant influence over the Fund; or

(iii) is a member of the key management personnel of the Fund.

(b) An entity is related to the Fund if any of the following conditions applies:

(i) The entity and the Fund are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

(iii) Both entities are joint ventures of the same third party.

(iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(v) The entity is a post-employment benefit plan for the benefit of employees of either the group or an entity related to the group.

(vi) The entity is controlled or jointly controlled by a person identified in (a).

(vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the Fund.

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity.

(m) Changes in accounting policies

The HKICPA has issued a number of amendments to HKFRSs that are first effective for the current accounting period of the Fund. None of these developments have had a material effect on how the Fund's results and financial position for the current or prior periods have been prepared or presented.

The Fund has not applied any new standard or interpretation that is not yet effective for the current accounting period.

4. Taxation

The interest and profits on investments earned by the Fund are not subject to Hong Kong Profits Tax under Section 14 of the Inland Revenue Ordinance.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

5. Net investment income

	2018 $'000	2017 $'000
Interest income from bank deposits	828	84
Interest income on financial assets designated at fair value through profit or loss	44,455	41,923
Realised gain on disposal of equity securities	989	4
Realised gain/(loss) on redemption/disposal of debt securities	2,422	(1,615)
Gain on revaluation of equity securities	52,138	48,362
Loss on revaluation of debt securities	(27,229)	(11,617)
Net investment income	73,603	77,141

6. Levy from SEHK and HKFE

From 1 April 2003, the Fund received a levy chargeable on leviable SEHK transactions and leviable HKFE contracts pursuant to Part 2 and Part 3 of the Securities and Futures (Investor Compensation – Levy) Rules.

After the Securities and Futures (Investor Compensation – Levy) (Amendment) Rules 2005 came into effect on 28 October 2005, a levy suspension and re-instatement mechanism was established whereby the investor compensation levies can be suspended when the net asset value of the Fund exceeds $1.4 billion, and subsequently reinstated when the net asset value of the Fund falls below $1 billion. Pursuant to the Securities and Futures (Investor Compensation – Levy) (Amendment) Rules 2005 and the Gazette on 11 November 2005, no person is required to pay any levy to the Fund in respect of a sale and purchase transaction of securities and futures contract with effect from 19 December 2005.

7. ICC expenses

The SFC formed the 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 SFO. The Fund is responsible for funding the establishment and operation of the ICC. For the year ended 31 March 2018, the ICC incurred costs of $5,729,000 for its operations (2017: $5,574,000) which were reimbursed by the Fund.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

8. 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 year ended 31 March 2018	(476)
Balance as at 31 March 2018	–

9. Financial assets designated at fair value through profit or loss

	2018 $'000	2017 $'000
(a) Debt securities		
(i) Listing status		
Listed – outside Hong Kong	1,103,850	977,432
Listed – in Hong Kong	443,133	490,715
Unlisted	392,296	425,101
	1,939,279	1,893,248
(ii) Maturity profile		
Within one year	404,749	856,310
After one year but within two years	454,873	361,785
After two years but within five years	1,001,791	635,207
After five years	77,866	39,946
	1,939,279	1,893,248
(iii) The weighted average effective interest rate of debt securities on 31 March 2018 was 2.9% (2017: 2.1%).		
(b) Pooled fund – Unlisted	350,084	330,386

The pooled fund comprises mainly listed equity securities.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

10. Deposits with banks and cash at bank

The effective interest rate on deposits with banks and cash at bank at 31 March 2018 ranged from 0.80% to 1.53% (2017: 0.50% to 1.26%). The balances of deposits at both 31 March 2018 and 31 March 2017 mature within one year.

11. Contributions from UECF and CECF

Under Sections 74(2) and 75(2) of Schedule 10 of the SFO, the SFC may pay into the Fund such sum of money from the UECF and the CECF as it considers appropriate after 1 April 2003. Up to 31 March 2018, the SFC had $994,718,000 (2017: $994,718,000) and $108,923,000 (2017: $108,923,000) paid into the Fund from the UECF and the CECF respectively.

The Fund defines "capital" as including contributions from the UECF and the CECF and the accumulated surplus.

12. Material related party transactions

We have related party relationships with the SFC, ICC and the UECF. There were no significant related party transactions other than those disclosed in the financial statements of the Fund for the years ended 31 March 2017 and 2018 (refer to notes 7 and 11).

13. Financial risk management and fair values

The financial assets of the Fund mainly comprise debt securities and units in a pooled fund. The underlying investments of the pooled fund mainly comprise equity securities.

The main financial risks of the Fund arise from its investments in debt securities and units in the pooled fund. The SFC appoints external investment managers to manage the Fund's investments and to ensure that the portfolio's investments comply with the Fund's investment policy approved by the SFC which sets control limits on credit risk, market risk, interest rate risk, liquidity risk and foreign currency risk. The external investment managers report thereon to the SFC on a regular basis.

The Fund's exposure to these risks and the financial risk management policies and practices used by the Fund to manage these risks are described below.

(a) Credit risk

The Fund's Investment Policy and Administrative Guidelines (the Policy) only allows the Fund to invest in pooled funds, fixed rate dated securities rated A or above or in bank deposits with licensed banks rated P-1 or A-1 by Moody's or S&P respectively. Investment in unit trusts and mutual funds authorised as collective investment schemes under Section 104 of the SFO up to 15% of the total value of funds under management is also permitted. The Policy also limits the Fund's exposure to 10% for each organisation and 20% for each country, except for holdings of US Treasuries, any issuances by the Hong Kong Government and the Government of the People's Republic of China. The Fund's investment managers are responsible for managing the portfolio and ensuring the portfolio's investments meet the Policy and reports thereon on a monthly basis. During the year, the Fund complied with the above Policy. The maximum exposure to credit risk is the carrying value of the assets in the statement of financial position.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

13. Financial risk management and fair values (cont'd)

(b) Liquidity risk

The Fund's policy is to regularly monitor its liquidity requirement to ensure that it maintains sufficient reserves of cash and readily realisable marketable securities to meet its liquidity requirements in the short and longer term.

All financial liabilities are due within one year or payable on demand.

(c) Interest rate risk

The Fund's interest bearing assets mainly comprise fixed interest rate bearing debt securities and bank deposits. The Fund's bank deposits are exposed to short-term bank deposit interest re-pricing risk.

The Fund is subject to the risk that future cash flows of a debt security will fluctuate because of changes in market interest rates. In order to manage the re-pricing risk, the Fund adopts a policy of maintaining duration at no more than five years within its debt securities portfolio. As at 31 March 2018 the duration was 2.26 years (31 March 2017: 1.55 years).

At 31 March 2018, it is estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would decrease/increase the Fund's gains on revaluation of debt securities and the accumulated surplus by approximately $44,803,000 (2017: $29,659,000). Further, at 31 March 2018, it is estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would increase/decrease the Fund's interest income and the accumulated surplus by approximately $2,990,000 (2017: $5,031,000). Other components of the accumulated surplus would not be affected (2017: Nil) by the changes in interest rates.

The sensitivity analysis above indicates the instantaneous change in the Fund's accumulated surplus that would arise assuming that the change in interest rates had occurred at the end of the reporting period and had been applied to re-measure those financial instruments held by the Fund which expose the Fund to fair value interest rate risk at the end of the reporting period. The analysis is performed on the same basis for the year ended 31 March 2017.

(d) Foreign currency risk

The Fund's investment policy allows the Fund to have US dollars and renminbi foreign exchange exposure. As at 31 March 2018, the Fund has exposure to US dollars, as Hong Kong dollars are pegged with US dollars, the Fund was not exposed to significant foreign exchange risk.

(e) Market risk

The investment activities of the Fund expose it to various types of market risks which are associated with the markets in which it invests, to the extent of the amount invested in debt and equity securities. Such risk will be reflected in the price and the carrying value of the financial assets concerned.

The Fund invests in units of a pooled fund, which mainly comprises listed equity securities, the performance of which is measured against the benchmark index MSCI AC Pacific ex Japan. It is estimated that a general increase/decrease of 14.5% in the benchmark index would increase/decrease the Fund's surplus and the accumulated surplus by approximately $50,062,000 (2017: a general increase/decrease of 14.3% in the benchmark index would increase/decrease the Fund's surplus and the accumulated surplus by approximately $47,245,000).

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

13. Financial risk management and fair values (cont'd)

(e) Market risk (cont'd)

The sensitivity analysis above indicates the instantaneous change in the Fund's accumulated surplus that would arise assuming that the changes in the benchmark index had occurred at the end of the reporting period and had been applied to re-measure those financial instruments held by the Fund which expose the Fund to equity price risk at the end of the reporting period. It is also assumed that the fair values of the Fund's investment in pooled fund would change in accordance with the historical correlation with the relevant benchmark index since the portfolio is diversified in terms of industry distribution and that all other variables remain constant. The analysis is performed on the same basis for 2017.

(f) Fair values of financial instruments

The following table presents the carrying value of financial instruments measured at fair value at the end of the reporting period across the three levels of the fair value hierarchy defined in HKFRS 13, *Fair value measurement*, with the fair value of each financial instrument categorised in its entirety based on the lowest level of input that is significant to that fair value measurement. The levels are defined as follows:

- Level 1 (highest level): fair values measured using quoted prices (unadjusted) in active markets for identical financial instruments.
- Level 2: fair values measured using quoted prices in active markets for similar financial instruments, or using valuation techniques in which all significant inputs are directly or indirectly based on observable market data.
- Level 3 (lowest level): fair values measured using valuation techniques in which any significant input is not based on observable market data.

All financial instruments are carried at amounts not materially different from their fair values as at 31 March 2018 and 2017.

The fair value of the debt securities is the quoted market price or based on quotes from bond market-makers.

The fair value of the investment in the unlisted pooled fund is determined based on the Fund's share in the net assets of the pooled fund as determined by the custodian. The majority of the underlying assets of the pooled fund are listed securities.

Changes in the market conditions could materially affect fair value estimates. Any increase or decrease in the fair values of financial instruments would affect profit or loss in future years.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

13. Financial risk management and fair values (cont'd)

(f) Fair values of financial instruments (cont'd)

	2018			
	Level 1 $'000	Level 2 $'000	Level 3 $'000	Total $'000
Assets				
Debt securities				
– Listed	1,271,926	275,057	–	1,546,983
– Unlisted	11,169	381,127	–	392,296
Pooled fund				
– Unlisted	350,084	–	–	350,084
	1,633,179	656,184	–	2,289,363

	2017			
	Level 1 $'000	Level 2 $'000	Level 3 $'000	Total $'000
Assets				
Debt securities				
– Listed	1,229,343	238,804	–	1,468,147
– Unlisted	61,693	363,408	–	425,101
Pooled fund				
– Unlisted	330,386	–	–	330,386
	1,621,422	602,212	–	2,223,634

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

14. Contingent liabilities

As at the date of this report, in addition to the provision made as described in note 8, there are 15 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 $2,375,000 (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.

15. Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 March 2018

Up to the date of issue of these financial statements, the HKICPA has issued a number of amendments and new standards which are not yet effective for the year ended 31 March 2018 and which have not been adopted in these financial statements. These include the following which may be relevant to the Fund.

	Effective for accounting periods beginning on or after
HKFRS 9, *Financial instruments*	1 January 2018

HKFRS 9 introduces new requirements for classification and measurement of financial assets, calculation of impairment of financial assets and hedge accounting. Based on the preliminary assessment, the Fund expects that its financial assets currently measured at amortised cost and fair value through profit or loss will continue with their respective classification and measurements upon the adoption of HKFRS 9.

The new impairment model requires the recognition of impairment provisions on the Fund's financial assets classified as amortised cost based on expected credit losses rather than only incurred credit losses as is the case under HKAS 39. Based on the assessments undertaken to date, the Fund expects that the adoption of the new standard would not have a significant effect on the loss allowance in relation to financial assets held at amortised cost.

Unified Exchange Compensation Fund

Report of the Securities Compensation Fund Committee

The members of the Securities Compensation Fund Committee (the Committee) present their annual report together with the audited financial statements for the year ended 31 March 2018.

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 from 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 March 2018, 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 financial year ended 31 March 2018 and the financial position of the Fund as at that date are set out in the financial statements on pages 152 to 162.

Members of the Committee

The members of the Committee during the year ended 31 March 2018 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 financial year or at any time during the financial year.

Auditor

PricewaterhouseCoopers (PwC) retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of PwC as auditor of the Fund is to be proposed at the forthcoming committee meeting.

By order of the Committee

Keith Lui
Chairman

28 May 2018

Independent Auditor's Report
To the Securities and Futures Commission

Opinion

What we have audited

The financial statements of Unified Exchange Compensation Fund (the Fund) established under Section 99 of the repealed Hong Kong Securities Ordinance set out on pages 152 to 162, which comprise:

- the statement of financial position as at 31 March 2018;
- the statement of profit or loss and other comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the cash flow statement for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Fund as at 31 March 2018, and of its financial performance and its cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards (HKFRSs) issued by the Hong Kong Institute of Certified Public Accountants (HKICPA).

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (HKSAs) issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Fund in accordance with the HKICPA's Code of Ethics for Professional Accountants (the Code), and we have fulfilled our other ethical responsibilities in accordance with the Code.

Emphasis of matter

We draw attention to the fact that the Fund is in the process of terminating its business and operations and is no longer considered to be a going concern. Details about the basis of preparation of the financial statements are set out in the significant accounting policies note 3(b) to the financial statements. Our opinion is not modified in respect of this matter.

Other information

The directors of the Securities and Futures Commission (SFC) are responsible for the other information. The other information comprises all of the information included in the annual report, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of directors of the SFC for the financial statements

The directors of the SFC are responsible for the preparation of the financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA, and for such internal control as the directors of the SFC determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Independent Auditor's Report (continued)
To the Securities and Futures Commission

In preparing the financial statements, the directors of the SFC are responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern. The directors of the SFC consider that the Fund is no longer operating on a going concern basis and have prepared the financial statements on the basis as set out in note 3 thereto.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with HKSAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors of the SFC.

- Conclude on the appropriateness of the directors of the SFC's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the directors of the SFC regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 28 May 2018

Statement of profit or loss and other comprehensive income

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	2018 $'000	2017 $'000
Income		
Interest income	691	560
	691	560
Expenses		
Recoveries re-distributed	–	1,152
Auditor's remuneration	77	74
Bank charge	–	3
Sundry expenses	1	1
	78	1,230
Surplus/(loss) and total comprehensive income for the year	613	(670)

The notes on pages 156 to 162 form part of these financial statements.

Statement of financial position

At 31 March 2018 (Expressed in Hong Kong dollars)

	Note	2018 $'000	2017 $'000
Current assets			
Equity securities received under subrogation		1	1
Interest receivable		98	77
Accounts receivable		9	–
Fixed deposits with banks		86,525	83,744
Cash at bank		224	332
		86,857	84,154
Current liabilities			
Creditors and accrued charges	5	10,303	10,663
Relinquished trading rights payable to SEHK	6	750	600
		11,053	11,263
Net current assets		75,804	72,891
Net assets		75,804	72,891
Representing:			
Compensation fund		75,804	72,891

Approved and authorised for issue by the Securities Compensation Fund Committee on behalf of the Securities and Futures Commission on 28 May 2018 and signed on its behalf by

Keith Lui
Chairman

Lee Kwok Keung
Committee Member

The notes on pages 156 to 162 form part of these financial statements.

Statement of changes in equity

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	Trading rights deposits from SEHK $'000 (see note 6)	Excess transaction levy from SEHK $'000 (see note 8)	Additional contributions from SEHK and the SFC $'000 (see note 9)	Other contributions $'000 (see note 10)	Accumulated surplus $'000	Contributions to Investor Compensation Fund $'000 (see note 11)	Total $'000
Balance at 1 April 2016	49,050	353,787	630,000	6,502	26,790	(994,718)	71,411
Net contributions from SEHK	2,150	–	–	–	–	–	2,150
Loss and total comprehensive income for the year	–	–	–	–	(670)	–	(670)
Balance at 31 March 2017	51,200	353,787	630,000	6,502	26,120	(994,718)	72,891
Balance at 1 April 2017	51,200	353,787	630,000	6,502	26,120	(994,718)	72,891
Net contributions from SEHK	2,300	–	–	–	–	–	2,300
Surplus and total comprehensive income for the year	–	–	–	–	613	–	613
Balance at 31 March 2018	53,500	353,787	630,000	6,502	26,733	(994,718)	75,804

The notes on pages 156 to 162 form part of these financial statements.

Cash flow statement

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

	2018 $'000	2017 $'000
Cash flows from operating activities		
Surplus/(loss) for the year	613	(670)
Adjustment for:		
Interest income	(691)	(560)
	(78)	(1,230)
Increase in accounts receivable	(9)	–
(Decrease)/increase in creditors and accrued charges	(360)	357
Increase/(decrease) in relinquished trading rights payable to SEHK	150	(200)
Net cash used in operating activities	(297)	(1,073)
Cash flows from investing activities		
Interest received	670	542
Net cash generated from investing activities	670	542
Cash flows from financing activities		
Net trading rights deposits from SEHK	2,300	2,150
Net cash generated from financing activities	2,300	2,150
Net increase in cash and cash equivalents	2,673	1,619
Cash and cash equivalents at beginning of the year	84,076	82,457
Cash and cash equivalents at end of the year	86,749	84,076

Analysis of the balance of cash and cash equivalents

	2018 $'000	2017 $'000
Fixed deposits with banks	86,525	83,744
Cash at bank	224	332
	86,749	84,076

The notes on pages 156 to 162 form part of these financial statements.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

1. Purpose, limitation and principal activity

The Fund provides compensation to investors who suffer a loss due to the default of an exchange participant of The Stock Exchange of Hong Kong Limited (SEHK). Part X of the repealed Securities Ordinance governs its operation.

SEHK receives and determines claims against the Fund. The Securities and Futures Commission (SFC) maintains and invests the money of the Fund and makes payments to claimants. Upon making payment to a claimant, the SFC is subrogated to the claimant's rights against the defaulter.

The repealed Securities Ordinance limits the total compensation amount that may be paid per exchange participant default to $8 million. If allowed claims exceed the limit, payments are made proportionally to claimants. SEHK, with the approval of the SFC, can decide to exceed the limit if it considers, among other things, that the assets of the Fund so permit. For eight defaults since 1998, SEHK proposed and the SFC approved exceeding the limit via payment of up to $150,000 per claimant or, if higher, the claimant's proportional share of the $8 million limit.

If amounts owed to claimants against the Fund exceed the Fund's net assets, the SFC would apportion compensation payments to claimants as provided in the repealed Securities Ordinance. Unpaid claim amounts would be charged against future receipts by the Fund and paid when funds are available.

After the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single Investor Compensation Fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. After settlement of all claims against the Fund and its other liabilities, the SFC will eventually transfer the remaining balance of the Fund into the ICF. Claims for any defaults occurring after 31 March 2003 should be made against the ICF. If the sum of money in the Fund is not sufficient to meet its liabilities, the SFC shall pay into the Fund from the ICF the appropriate sum of money according to Section 242 of the SFO.

Apart from the above change and Section 112 of the repealed Securities Ordinance, under Section 74 of Schedule 10 of the SFO, Part X of the repealed Securities Ordinance remains effective in respect of the operation of the Fund.

2. Money constituting the Fund

Before 1 April 2003, SEHK was required to keep deposited with the SFC $50,000 for each SEHK trading right under the repealed Securities Ordinance. When the SFC makes compensation payments out of the deposits, the SFC may require SEHK to replenish the net amount paid after the SFC has exhausted its subrogated rights against the defaulter. The SFC pays to SEHK the investment return earned on any remaining deposits net of the Fund expenses. During the year, the SFC did not make such payment as the total of the compensation payments exceeded the deposits received from SEHK (2017: Nil).

SEHK and the SFC have made contributions of their own money to the Fund. The SFC determined it would retain investment returns earned on these contributions in the Fund.

Other sources of money for the Fund include: recoveries; SEHK replenishments detailed in note 14; Contributions to Investor Compensation Fund detailed in note 11; and excess transaction levy received before the SFO became effective from 1 April 2003 detailed in note 8.

The Fund defines "capital" as including all elements of the Fund less contributions to the ICF and less contributions from SEHK (trading rights deposits from SEHK) as disclosed on the face of the statement of financial position.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards (HKFRSs), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (HKASs) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (HKICPA) and accounting principles generally accepted in Hong Kong. Significant accounting policies adopted by the Fund are set out below.

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for the current accounting period of the Fund. Note 3(i) provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Fund for the current and prior accounting periods reflected in these financial statements.

The Fund has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 15).

(b) Basis of preparation

Under the SFO, the Fund will continue in operation until all claims against it and all its liabilities have been settled. As the Fund will eventually cease operation, we have prepared these financial statements 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. We have not provided for potential future claims and recoveries as these cannot be reliably estimated. We have also not provided in the financial statements for all expenses expected to be incurred subsequent to the end of the reporting period and up to the date operations will cease and these are estimated to be immaterial.

We prepare the financial statements in conformity with HKFRSs which require management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. We make estimates and associated assumptions based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

We review estimates and underlying assumptions on an ongoing basis. We recognise revisions to accounting estimates in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

(c) Recognition of income

(i) Interest income

We record interest income as it accrues using the effective interest method.

(ii) Recoveries

We recognise recoveries pursuant to Section 118 of the repealed Securities Ordinance as income to the Fund and recoveries re-distributed to claimants as expenses. We record recoveries received and re-distributed when and only when we can be virtually certain that the recoveries will be received and paid.

(iii) Replenishments from SEHK

We record replenishments from SEHK pursuant to Section 107 of the repealed Securities Ordinance as income of the Fund on a receipt basis. For the purpose of calculating the amount to be replenished by SEHK, we deem compensation payments up to the amount of $8 million for each default to be charged to the contribution from SEHK.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(d) Impairment

The carrying amount of the Fund's assets are reviewed at each reporting period to determine whether there is objective evidence of impairment. Objective evidence that financial assets are impaired includes observable data that comes to the attention of the Fund about one or more of the following loss events which have an impact on the future cash flows of the assets that can be estimated reliably:

- significant financial difficulty of the issuer or borrower;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- significant changes in the technological, market, economic or legal environment that have an adverse effect on the borrower;
- disappearance of an active market for financial assets because of financial difficulties; and
- a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost.

If any such evidence exists, the carrying amount of financial assets held at amortised cost is reduced to the estimated recoverable amount by means of a charge to the statement of profit or loss and other comprehensive income.

(e) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and demand deposits with banks and other financial institutions.

(f) Creditors and accrued charges

We state creditors and accrued charges initially at fair value and thereafter at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(g) Provisions and contingent liabilities

We recognise a provision in the statement of financial position when the Fund has a legal or constructive obligation of uncertain timing or amount as a result of a past event, and it is probable that the Fund will require an outflow of economic benefits to settle the obligation and the amount can be estimated reliably.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, we disclose the obligation as a contingent liability, unless the probability of outflow of economic benefits is remote. We also disclose possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events as contingent liabilities unless the probability of outflow of economic benefits is remote.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(h) Related parties

For the purpose of these financial statements, a party is considered to be related to the Fund if:

(a) A person, or a close member of that person's family, is related to the Fund if that person:

(i) has control or joint control over the Fund;

(ii) has significant influence over the Fund; or

(iii) is a member of the key management personnel of the Fund.

(b) An entity is related to the Fund if any of the following conditions applies:

(i) The entity and the Fund are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

(iii) Both entities are joint ventures of the same third party.

(iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(v) The entity is a post-employment benefit plan for the benefit of employees of either the group or an entity related to the group.

(vi) The entity is controlled or jointly controlled by a person identified in (a).

(vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

(viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the Fund.

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity.

(i) Changes in accounting policies

The HKICPA has issued a number of amendments to HKFRSs that are first effective for the current accounting period of the Fund. None of these developments have had a material effect on how the Fund's results and financial position for the current or prior periods have been prepared or presented.

The Fund has not applied any new standard or interpretation that is not yet effective for the current accounting period.

4. Taxation

The interest and profits on investment earned by the Fund are not subject to Hong Kong Profits Tax under Section 14 of the Inland Revenue Ordinance.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

5. Creditors and accrued charges

Creditors and accrued charges comprised mainly compensation payments re-established for those cheque payments that were not cleared over six months from the cheque issuing date and accrued auditor's remuneration.

These liabilities are classified as financial liabilities measured at amortised cost in accordance with the determination in HKAS 39, *Financial instruments: Recognition and measurement* unless the effect of discounting would be immaterial, in which case they are stated at cost. They are due on demand or within one year and are unsecured.

6. Trading rights deposits from SEHK/ Relinquished trading rights payable to SEHK

According to Section 104 of the repealed Securities Ordinance, 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 year, deposits of $2,700,000 in respect of 54 new trading rights were received from SEHK and deposits of $250,000 in respect of 5 relinquished trading rights were refunded to SEHK. As at 31 March 2018, there were 15 trading rights in total of $750,000 that have been relinquished but not yet refunded.

The movement of trading rights deposits from SEHK during the year was as follows:

	2018 $'000	2017 $'000
Balance brought forward	51,200	49,050
Add: new trading rights issued	2,700	2,750
Less: relinquished trading rights refunded	(250)	(800)
Adjustment for: (increase)/decrease in relinquished trading rights payable to SEHK	(150)	200
Balance carried forward	53,500	51,200

7. 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, will be re-distributed to claimants. As the timing of any future re-distribution and amount of these potential excess amounts are uncertain at the date of this report, we disclose this as a contingent liability.

8. Excess transaction levy from SEHK

SEHK paid these amounts to the Fund from 1992 to 1994 under an agreement with the SFC and the Financial Secretary concerning SEHK's budget and its receipt of transaction levy.

9. Additional contributions from SEHK and the SFC

Following the relaxation of the compensation rules and compensation limit in 1998, the SFC and SEHK had injected $330 million and $300 million respectively to the Fund during the years 1998 to 2001.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

10. Other contributions

In October 1993, a member of SEHK made a special contribution to the Fund $3,500,000 in recognition of the SFC's concerns about its misconduct in handling its client trading activities. In November 2000, the former Financial Services Bureau of the HKSAR Government transferred to the Fund $3,002,000 under the provisions of the Exchanges (Special Levy) Ordinance.

11. Contributions to Investor Compensation Fund

When the SFO and its subsidiary legislation came into effect from 1 April 2003, a new single Investor Compensation Fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. Under Section 74(2) of Schedule 10 of the SFO, the SFC may after 1 April 2003 pay into the ICF, which came into operation after 1 April 2003, such sum of money from the Fund as it considers appropriate. Total contributions paid into the ICF up to 31 March 2018 amounted to $994,718,000 (2017: $994,718,000).

12. Material related party transactions

The Fund has related party relationships with the ICF and the SFC. There were no significant related party transactions other than those disclosed in the financial statements of the Fund for the years ended 31 March 2018 and 2017.

13. Financial risk management

The Fund's interest bearing assets mainly comprise deposits at banks which mature or re-price in the short term, as a result of which the Fund is subject to a limited exposure to interest rate risk due to fluctuations in the prevailing market rates. At 31 March 2018, it is estimated that a general increase/decrease of 100 basis points in the interest rates, with all other variables held constant, would increase/ decrease the Fund's surplus and accumulated surplus by approximately $865,000 (2017: $837,000). Other components of accumulated surplus would not be affected (2017: Nil) by the changes in interest rates. The exposure to credit and liquidity risks arises in the normal course of the Fund's operation. The Fund is not exposed to any foreign exchange risk as all transactions and balances are denominated in Hong Kong dollars.

The Fund's credit risk is primarily attributable to amounts at bank. Management's policy is that bank balances are placed only with licensed banks rated P-1 or A-1 by Moody's or S&P respectively. There are no amounts past due or impaired.

The Fund's policy is to regularly monitor its liquidity requirements to ensure that it maintains sufficient reserves of cash to meet its liquidity requirements in the short and longer term.

Notes to the financial statements

For the year ended 31 March 2018 (Expressed in Hong Kong dollars)

14. Replenishments from SEHK

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

Up to 31 March 2018, SEHK replenished $16,361,000 to the Fund. In compliance with Section 107 of the repealed Securities Ordinance, if no further recoveries were to be collected, the SFC may require SEHK to further replenish $70,816,000 to the Fund as follows:

	2018 $'000	2017 $'000
Compensation paid up to the $8 million limit as set out in Section 109(3) of the repealed Securities Ordinance	100,738	100,738
Less: recoveries received for compensation paid up to $8 million	(29,946)	(29,946)
Add: recoveries re-distributed to claimants	16,385	16,385
Less: replenishments from SEHK	(16,361)	(16,361)
Net amount the SFC may request SEHK for replenishment	70,816	70,816

Under Section 74(3) of Schedule 10 of the SFO, the SFC having allowed sufficient funds to meet claims, may reimburse SEHK for the deposits paid by SEHK into the Fund for each trading right. The reimbursement of these SEHK deposits may be set off against further replenishments required from SEHK.

Replenishments from SEHK are not recognised in the statement of financial position given that the Fund is not aware of any need for requesting SEHK for replenishment in the near future.

15. Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 March 2018

Up to the date of issue of these financial statements, the HKICPA has issued a number of amendments and new standards which are not yet effective for the year ended 31 March 2018 and which have not been adopted in these financial statements. These include the following which may be relevant to the Fund.

	Effective for accounting periods beginning on or after
HKFRS 9, *Financial instruments*	1 January 2018

HKFRS 9 introduces new requirements for classification and measurement of financial assets, calculation of impairment of financial assets and hedge accounting. Based on the preliminary assessment, the Fund expects that its financial assets currently measured at amortised cost and fair value through profit or loss will continue with their respective classification and measurements upon the adoption of HKFRS 9.

The new impairment model requires the recognition of impairment provisions on the Fund's financial assets classified as amortised cost based on expected credit losses rather than only incurred credit losses as is the case under HKAS 39. Based on the assessments undertaken to date, the Fund expects that the adoption of the new standard would not have a significant effect on the loss allowance in relation to financial assets held at amortised cost.