

Securities and Futures Commission

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 131, which comprise:

- the consolidated statement of financial position as at 31 March 2020;
- 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 statement of cash flows 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 2020, 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 (HKSA) 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.

The key audit matter identified in our audit is the valuation of investments.

Valuation of investments

The aggregate carrying value of the Group's investment portfolio was HK\$3,652 million, which represented 50% of consolidated total assets as at 31 March 2020.

The investment portfolio comprise of i) debt securities and pooled funds (equity instruments) with a total value of HK\$1,068 million which is carried at fair value through profit or loss and ii) debt investments with a total value of HK\$2,584 million which were accounted for at amortised cost.

The Group's debt and equity instruments at fair value through profit or loss are categorised under the Level 1 and 2 in the fair value hierarchy and valued based on market prices or valuation models using market observable inputs.

We identified valuation of investments as a key audit matter because of the size of these items in the financial statements, the impact of changes in valuation on the profit and loss and the management judgments and assumptions used in assessing expected credit losses (ECL) associated with the financial instruments carried at amortised cost.

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

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

Key audit matters (continued)

How our audit addressed the Key audit matter

The audit procedures we performed in connection with the valuation of investments included:

- For Level 1 and Level 2 financial instruments, we compared the fair values applied by the Group with publicly available market data on a sample basis. For investments in the pooled funds, we performed a look-through analysis to understand the underlying investments and the basis of valuation for a sample of these investments.
- For Level 2 financial instruments, we involved our internal valuation specialists to carry out independent valuations by developing valuation models, identifying and obtaining relevant inputs from publicly available market data and comparing the results against fair values recorded by the Group on a sample basis.
- We assessed the appropriateness of the ECL methodologies and assumptions associated with the financial instruments carried at amortised cost. The methodologies and assumptions include economic indicators selected by management, economic scenarios and probability weightings applied by management. We assessed the reasonableness of the economic indicators and performed sensitivity analysis to understand the impact of changes in economic indicators, scenarios and weightings on the ECL result. We examined data inputs to the ECL calculation on a selected sample, including historical data and data at the measurement date, to assess their accuracy and completeness.

Based on the procedures we performed, we found that the valuation of investments are supported by available evidence and the models, key parameters, significant judgements and assumptions adopted by management were considered acceptable. We found that management's estimates and judgements made in determining the ECL for financial instruments carried at amortised cost to be acceptable.

Notes 3(h), 9, 10 and 22(f)(i) to the consolidated financial statements sets out the Group's accounting policies relating to this matter, detailed breakdown of these investments and the respective fair value hierarchy disclosures.

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 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.

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

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

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

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 HKSA's 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 HKSA's, 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.
- 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.

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

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

Auditor's responsibilities for the audit of the consolidated financial statements (continued)

- 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, 28 May 2020

Consolidated statement of profit or loss and other comprehensive income

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Income			
Levies	2(a)	1,430,678	1,483,846
Fees and charges		162,847	127,343
Investment income net of third party expenses			
Investment income	5	48,233	138,565
Less: custody and advisory expenses		(7,857)	(7,717)
Recoveries from the Investor Compensation Fund		5,989	5,859
Exchange loss		(49,510)	(190)
Other income	6	528	11,600
		1,590,908	1,759,306
Expense			
Staff costs and directors' emoluments	7	1,419,420	1,354,504
Premises expenses			
Rent	3(q)	-	200,710
Rates, management fees and others		45,456	46,700
Depreciation			
Fixed assets	11(a)	44,015	35,798
Right-of-use assets	12	218,796	-
Finance costs	12	3,487	-
Other expenses	8	235,036	216,136
		1,966,210	1,853,848
Loss and total comprehensive income for the year		(375,302)	(94,542)

The notes on pages 108 to 131 form part of these financial statements.

Consolidated statement of financial position

As at 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Non-current assets			
Fixed assets	11(a)	135,712	94,835
Right-of-use assets	12	324,040	–
Deposits for leases		33,767	–
Financial assets at amortised costs – debt securities	9	1,600,123	981,502
		2,093,642	1,076,337
Current assets			
Financial assets at amortised costs – debt securities	9	984,239	563,877
Financial assets at fair value through profit or loss			
Debt securities	10	419,469	795,946
Pooled funds	10	648,510	925,476
Debtors, deposits and prepayments	17	265,200	227,018
Fixed deposits with banks	13	2,832,302	3,653,456
Cash at bank and in hand	13	51,871	71,908
		5,201,591	6,237,681
Current liabilities			
Fees received in advance		47,097	8,850
Creditors and accrued charges	15	167,043	189,855
Lease liabilities	12	96,115	–
Provisions	16	66,532	–
		376,787	198,705
Net current assets		4,824,804	6,038,976
Total assets less current liabilities		6,918,446	7,115,313

Consolidated statement of financial position (continued)

As at 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$' 000	2019 \$' 000
Non-current liabilities			
Lease liabilities	12	203,558	–
Provisions	16	19,968	45,091
		223,526	45,091
Net assets			
		6,694,920	7,070,222
Funding and reserves			
Initial funding by Government	18	42,840	42,840
Reserve for property acquisition	24	3,000,000	3,000,000
Accumulated surplus		3,652,080	4,027,382
		6,694,920	7,070,222

Approved and authorised for issue by the SFC on 28 May 2020 and signed on its behalf by

Tim Lui
Chairman

Ashley Alder
Chief Executive Officer

The notes on pages 108 to 131 form part of these financial statements.

Statement of financial position

As at 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Non-current assets			
Fixed assets	11(b)	135,658	94,738
Right-of-use assets	12	324,040	–
Deposits for leases		33,767	–
Financial assets at amortised costs – debt securities	9	1,600,123	981,502
		2,093,588	1,076,240
Current assets			
Financial assets at amortised costs – debt securities	9	984,239	563,877
Financial assets at fair value through profit or loss			
Debt securities	10	419,469	795,946
Pooled funds	10	648,510	925,476
Debtors, deposits and prepayments	17	274,141	233,187
Fixed deposits with banks		2,832,302	3,653,456
Cash at bank and in hand		29,836	49,747
		5,188,497	6,221,689
Current liabilities			
Fees received in advance		47,097	8,850
Creditors and accrued charges	15	153,895	173,766
Lease liabilities	12	96,115	–
Provisions	16	66,532	–
		363,639	182,616
Net current assets		4,824,858	6,039,073
Total assets less current liabilities		6,918,446	7,115,313

Statement of financial position (continued)

As at 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Non-current liabilities			
Lease liabilities	12	203,558	–
Provisions	16	19,968	45,091
		223,526	45,091
Net assets		6,694,920	7,070,222
Funding and reserves			
Initial funding by Government	18	42,840	42,840
Reserve for property acquisition	24	3,000,000	3,000,000
Accumulated surplus		3,652,080	4,027,382
		6,694,920	7,070,222

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Tim Lui
Chairman

Ashley Alder
Chief Executive Officer

The notes on pages 108 to 131 form part of these financial statements.

Consolidated statement of changes in equity

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Initial funding by Government \$' 000	Reserve for property acquisition \$' 000	Accumulated surplus \$' 000	Total \$' 000
Balance at 1 April 2018	42,840	3,000,000	4,121,924	7,164,764
Loss and total comprehensive income for the year	–	–	(94,542)	(94,542)
Balance at 31 March 2019 and 1 April 2019	42,840	3,000,000	4,027,382	7,070,222
Loss and total comprehensive income for the year	–	–	(375,302)	(375,302)
Balance at 31 March 2020	42,840	3,000,000	3,652,080	6,694,920

The notes on pages 108 to 131 form part of these financial statements.

Consolidated statement of cash flows

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Cash flows from operating activities			
Loss for the year		(375,302)	(94,542)
Adjustments for:			
Depreciation – Fixed assets		44,015	35,798
Depreciation – Right-of-use assets		218,796	–
Finance costs		3,487	–
Interest income on deposits for leases		(16)	–
Investment income		(48,233)	(138,565)
Exchange difference		49,680	218
Loss on disposal of fixed assets		3	–
		(107,570)	(197,091)
Decrease in right-of-use assets		303	–
(Increase)/decrease in debtors, deposits and prepayments		(89,464)	8,003
Increase in fees received in advance		38,247	40
(Decrease)/increase in creditors and accrued charges		(22,135)	76,538
Increase in provisions		–	4,267
Net cash used in operating activities		(180,619)	(108,243)
Cash flows from investing activities			
Decrease in fixed deposits other than cash and cash equivalents		1,298,674	19,061
Interest received		161,139	121,268
Debt securities at fair value through profit or loss purchased		(544,263)	(381,883)
Debt securities at fair value through profit or loss sold or redeemed		934,628	366,534
Pooled funds sold		154,595	4,201
Debt securities at amortised cost purchased		(1,642,784)	–
Debt securities at amortised cost redeemed at maturity		573,495	35,324
Fixed assets purchased		(84,895)	(58,710)
Net cash generated from investing activities		850,589	105,795
Cash flows from financing activities			
Principal element of lease payments		(202,734)	–
Interest element of lease payment		(3,487)	–
Net cash used in financing activities		(206,221)	–
Net increase/(decrease) in cash and cash equivalents		463,749	(2,448)
Cash and cash equivalents at the beginning of the year		289,657	292,105
Cash and cash equivalents at the end of the year	13	753,406	289,657

Analysis of the balance of cash and cash equivalents

	2020 \$'000	2019 \$'000
Fixed deposits with banks	701,535	217,749
Cash at bank and in hand	51,871	71,908
	753,406	289,657

The notes on pages 108 to 131 form part of these financial statements.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (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 SFC's funding 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 and investments in 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 SFC and its subsidiaries (together, the Group or We) 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.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (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 as the measurement basis except that financial assets 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 debt securities requires significant judgement. In making this judgement, we evaluate business model and the contractual cash flows characteristics of these securities. 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.

(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 those returns through its power to direct the activities of 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. We record other fees and charges received in advance as a liability.

(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 debt securities measured at amortised cost.

(iv) Net gain/loss on financial assets

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

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(e) Leases

We have applied HKFRS 16 *Leases* as issued by the HKICPA and effective for accounting periods beginning on or after 1 April 2019. The impact of the adoption of HKFRS 16 is disclosed in note 3(q).

From 1 April 2019, leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Group.

Lease liabilities included fixed lease payments less any lease incentives receivable, variable lease payment based on an index or a rate, amounts expected to be payable under residual value guarantees and payments of penalties for terminating the lease. The lease liabilities are initially measured at the present value of the remaining lease payments, discounted at the Group's incremental borrowing rate at the lease commencement date. The lease payments are allocated between principal and finance cost. The finance cost is charged to profit or loss using the incremental borrowing rate on the remaining balance of the lease liabilities for each period. The lease liabilities are reduced by an amount equal to the lease payments made less the finance costs charged for that period.

The right-of-use assets are measured at the amount equal to the initial measurement of the lease liability, adjusted for any prepaid lease payments, lease incentives received, any initial direct costs or reinstatement provisions relating to that lease. The right-of-use assets are depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

Payments associated with short-term leases and all leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less.

Until 31 March 2019, leases in which a significant portion of the risks and rewards of ownership are not transferred to the Group as a lessee are classified as 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 historical cost less accumulated depreciation and any impairment losses (see note 3(o)). Historical cost includes expenditure that is directly attributable to the acquisition of the items. We charge depreciation to the statement of profit or loss and other comprehensive income using the straight-line method over the estimated useful lives from the point at which the asset is ready for use as follows:

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

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

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

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.

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.

We review the assets' residual values and useful lives and adjust, if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

(h) Financial assets

(i) Classification

The Group classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value through profit or loss; and
- those to be measured at amortised cost.

The classification depends on the entity's business model for managing the financial assets and the contractual term of the cash flows.

For assets measured at fair value, gains and losses will be recorded in profit or loss.

The Group reclassifies debt investments when and only when its business model for managing those assets changes.

(ii) Recognition and derecognition

Regular way purchases and sales of financial assets are recognised on settlement-date, the date on which the assets are delivered to the Group. 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.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all the risks and rewards of ownership.

(iii) Measurement

At initial recognition, we measure a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

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:

Amortised cost:

Investments in debt securities that are held for the collection of contractual cash flows, where those cash flows represent solely payments of principal and interest, are measured at amortised cost. Interest income from these financial assets is included in investment income using the effective interest rate method. Any gain or loss arising from derecognition is recognised directly in the statement of profit or loss and other comprehensive income. Impairment losses are presented as a separate line item in the statement of profit or loss and other comprehensive income.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(h) Financial assets (cont'd)

(iii) Measurement (cont'd)

FVPL:

Changes on fair value of investments in debt securities and equity funds that are subsequently measured at FVPL are recognised in the statement of profit or loss and other comprehensive income and presented net within other gains/(losses) in the period in which they arise.

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. Unlisted equity investments are comprised of shares in equity funds. The fair value is determined based on the Group's share of the net assets of the equity funds as determined by the custodian.

(iv) Impairment

We assess on a forward looking basis the expected credit losses associated with our financial instruments carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

(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, 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.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(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, deposits and other receivables

We state debtors, deposits and other receivables initially at their fair value and thereafter at amortised cost less impairment losses. We hold the balance with the objective of collecting the contractual cash flows and therefore measure them subsequently at amortised cost using the effective interest method. See note 3(h)(iv) for further information about the Group's accounting for impairment.

(l) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand, fixed deposits with banks and other financial institutions with original maturities of three months or less that are readily convertible to known amounts of cash.

(m) 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 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 of non-financial assets

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.

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.

(p) Provisions and contingent liabilities

We recognise a provision in the statement of financial position when the Group has a legal or constructive obligation 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.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(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. Except as described below, these developments have had no material effect on how the Group's results and financial position for the current or prior periods have been prepared or presented.

HKFRS 16, *Leases*

The Group has applied HKFRS 16 from 1 April 2019. The Group applied the simplified transition approach and did not restate comparative amounts. In applying HKFRS 16 for the first time, the Group has adopted the following practical expedients as permitted by the standard:

- applying a single discount rate to a portfolio of leases with reasonably similar characteristics;
- relying on previous assessments on whether leases are onerous as an alternative to performing an impairment review – there were no onerous contracts as at 1 April 2019; and
- excluding initial direct costs for the measurement of the right-of-use assets at the date of initial application.

The Group has also elected not to reassess whether a contract is, or contains a lease at the date of initial application. Instead, for contracts entered into before the transition date the Group relied on its assessment made applying HKAS 17 and Interpretation 4 *Determining whether an Arrangement contains a Lease*.

Upon the adoption of HKFRS 16, leases that were previously been classified as "operating leases" under the HKAS 17 *Leases* are now recognised in the consolidated statement of financial position as lease liabilities with a corresponding right-of-use assets. The lease liabilities are measured at the present value of the remaining lease payments, discounted at the Group's incremental borrowing rate at the lease commencement date. The finance cost is charged to profit or loss using the incremental borrowing rate on the remaining balance of the lease liabilities for each period. The lease liabilities are reduced by an amount equal to the lease payments made less the finance costs charged for that period. The right-of-use assets are measured at the amount equal to the lease liability, adjusted for any prepaid or accrued lease payments or provisions for reinstatement relating to that lease as at 31 March 2019. The right-of-use assets are depreciated over the shorter of the assets' useful life and the lease term on a straight-line basis.

As at 31 March 2019, the Group has non-cancellable operating lease commitments for properties of \$285,809,000. As a result of initially applying HKFRS 16, the Group recognised right-of-use assets of \$303,807,000 and lease liabilities of \$282,469,000 discounted at 1.55% as at 1 April 2019.

For the year ended 31 March 2019, the Group recognised rent expense for the operating lease of \$200,710,000. Following the adoption of HKFRS 16, the Group recognised depreciation expense for right-of-use assets of \$218,796,000 and interest expense on lease liabilities of \$3,487,000 for the year ended 31 March 2020.

See note 12 for further information.

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 2020 (Expressed in Hong Kong dollars)

5. Investment income

	2020 \$'000	2019 \$'000
Interest income from bank deposits	86,295	80,445
Interest income from financial assets at FVPL – debt securities	15,468	18,438
Interest income from debt securities at amortised cost	42,157	37,628
Net loss on financial assets at FVPL – pooled funds	(112,043)	(4,806)
Net gain on financial assets at FVPL – debt securities	19,940	8,604
Net loss on debt securities at amortised cost	(3,584)	(1,744)
	48,233	138,565

Certain comparative information have been reclassified to conform with the current year's presentation.

6. Other income

	2020 \$'000	2019 \$'000
Investigation costs awarded	163	11,272
Sale of SFC publications	138	277
Others	227	51
	528	11,600

7. Staff costs and directors' emoluments

	2020 \$'000	2019 \$'000
Salaries and allowances	1,289,531	1,223,668
Retirement benefits	85,187	84,736
Medical and life insurance	39,343	38,487
Staff functions	1,924	2,216
Recruitment	1,833	3,912
Registration and membership fees	1,602	1,485
	1,419,420	1,354,504

The total number of staff as at 31 March 2020 was 947 (921 for the SFC, 23 for the Investor and Financial Education Council and 3 for the Investor Compensation Company Limited) (as at 31 March 2019: the total number of staff was 935 comprising 910 for the SFC, 22 for the Investor and Financial Education Council and 3 for the Investor Compensation Company Limited).

Notes to the consolidated financial statements

For the year ended 31 March 2020 (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	2020 Total \$'000	2019 Total \$'000
Chief Executive Officer						
Ashley Alder, JP	–	7,146	2,382	715	10,243	10,243
Executive Directors						
Julia Leung Fung-yee, SBS	–	5,150	1,545	515	7,210	7,335
Thomas Atkinson	–	4,623	1,110	462	6,195	5,895
Christina Choi Fung-yee	–	4,382	1,139	438	5,959	5,754
Brian Ho Yin-tung	–	4,962	1,241	496	6,699	6,568
Rico Leung Chung-yin (appointed 28 August 2019 ³)	–	2,612	653	261	3,526	–
Keith Lui Kei-kwong (retired 27 August 2019 ²)	–	2,701	504	201	3,406	6,568
	–	31,576	8,574	3,088	43,238	42,363
Non-executive Chairman						
Tim Lui Tim-leung, SBS, JP (appointed 20 October 2018)	1,255	–	–	–	1,255	564
Carlson Tong Ka-shing, GBS, JP (retired 19 October 2018 ⁴)	–	–	–	–	–	558
Non-executive Directors						
Albert Au Siu-cheung, BBS (retired 25 May 2019 ⁵)	48	–	–	–	48	280
Agnes Chan Sui-kuen (appointed 20 October 2018)	314	–	–	–	314	141
Clement Chan Kam-wing, MH (appointed 26 May 2019)	267	–	–	–	267	–
Edward Cheng Wai-sun, GBS, JP	314	–	–	–	314	280
Lester Garson Huang, SBS, JP	314	–	–	–	314	280
Teresa Ko, JP (retired 31 July 2018 ⁴)	–	–	–	–	–	84
Dr James C Lin (appointed 1 August 2018)	314	–	–	–	314	196
Nicky Lo Kar-chun, SBS, JP (appointed 24 April 2019)	294	–	–	–	294	–
Mary Ma Xuezheng (retired 23 April 2019 ⁶)	18	–	–	–	18	280
Dr William Wong Ming-fung, SC, JP	314	–	–	–	314	280
Dr Kelvin Wong Tin-yau, JP (retired 19 October 2018 ⁴)	–	–	–	–	–	140
	3,452	–	–	–	3,452	3,083
Total directors' emoluments	3,452	31,576	8,574	3,088	46,690	45,446

¹ This represents net contribution expenses accrued during the year ended 31 March 2020 in accordance with the accounting policy set out in note 3(f) on page 110. 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 2020 was \$2,365,000 (as at 31 March 2019: \$2,099,000).

² Retired having completed appointment period.

³ Mr Rico Leung's emoluments covered the period from 28 August 2019, when his appointment took effect, to 31 March 2020.

⁴ Retired having completed appointment period of six years.

⁵ Retired having completed appointment period of four years.

⁶ Retired having completed appointment period of five and a half years.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

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

The aggregate of the emoluments of the five highest paid individuals, representing the emoluments of the Chief Executive Officer and four senior management, was \$36,433,000 (2019: \$36,609,000) with the breakdown as follows:

	2020 \$'000	2019 \$'000
Salaries and allowances	26,244	26,527
Discretionary pay	7,565	7,429
Retirement scheme contributions	2,624	2,653
	36,433	36,609

Their emoluments are within the following bands:

	2020 No. of individuals	2019 No. of individuals
\$5,500,001 to \$6,000,000	0	1
\$6,000,001 to \$6,500,000	2	0
\$6,500,001 to \$7,000,000	1	2
\$7,000,001 to \$7,500,000	1	1
\$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	0	0
\$10,000,001 to \$10,500,000	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 2020 (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 which are a percentage 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 (2019: nil).

(ii) Executive staff

For executive staff, we make monthly contributions which are a percentage 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 \$4,410,000 (2019: \$3,372,000) and the amount so forfeited available at the end of the reporting period was \$20,000 (2019: \$684,000).

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

	2020 \$'000	2019 \$'000
Learning and development	3,480	7,700
Legal and professional services	99,025	72,047
Information and systems services	78,266	64,854
Auditor's remuneration	946	894
Funding for the Financial Reporting Council	–	8,496
Funding for the International Financial Reporting Standards Foundation	394	393
General office and insurance	9,440	10,302
Investor and other education programme costs to the Investor and Financial Education Council	33,491	38,721
Overseas travelling, regulatory meeting expenses and others	9,991	12,729
Loss on disposal of fixed assets	3	–
	235,036	216,136

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

9. Financial assets at amortised cost – debt securities

The Group and the SFC

		2020 \$' 000	2019 \$' 000
Maturing after one year in the second to sixth years	– unlisted	–	78,696
	– listed in Hong Kong	631,979	157,269
	– listed outside Hong Kong	968,144	745,537
		1,600,123	981,502
Maturing within one year	– unlisted	77,540	–
	– listed in Hong Kong	170,610	261,173
	– listed outside Hong Kong	736,089	302,704
		984,239	563,877
		2,584,362	1,545,379
Amortised cost at 31 March	– unlisted	77,540	78,696
	– listed in Hong Kong	802,589	418,442
	– listed outside Hong Kong	1,704,233	1,048,241
		2,584,362	1,545,379
Market value at 31 March	– unlisted	77,285	77,975
	– listed in Hong Kong	804,711	416,182
	– listed outside Hong Kong	1,699,709	1,042,376
		2,581,705	1,536,533

The weighted average yield to maturity of the debt securities was 2.4% p.a. as at 31 March 2020 (2019: 2.8% p.a.).

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

10. Financial assets at fair value through profit or loss

The Group and the SFC

	2020 \$' 000	2019 \$' 000
(a) Debt securities		
(i) Listing status		
Listed – outside Hong Kong	413,300	597,932
Listed – in Hong Kong	–	49,053
Unlisted	6,169	148,961
	419,469	795,946
(ii) Maturity profile		
Within one year	21,739	259,207
After one year but within two years	58,909	184,416
After two years but within five years	226,748	352,323
After five years	112,073	–
	419,469	795,946
(iii) The weighted average effective interest rate of debt securities on 31 March 2020 was 2.1% p.a. (2019: 2.4% p.a.).		
(b) Pooled funds – unlisted	648,510	925,476
The pooled funds comprise mainly listed equity securities.		

Notes to the consolidated financial statements

For the year ended 31 March 2020 (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 computer and software \$'000	Motor vehicles \$'000	Total \$'000
Cost						
At 1 April 2019	127,970	10,998	270,272	144,716	2,735	556,691
Additions	27,212	59	38,588	19,036	–	84,895
Disposal	(16)	(33)	(290)	(4,499)	–	(4,838)
At 31 March 2020	155,166	11,024	308,570	159,253	2,735	636,748
Accumulated depreciation						
At 1 April 2019	118,720	9,731	209,194	121,651	2,560	461,856
Charge for the year	2,892	485	25,602	14,955	81	44,015
Written back on disposals	(16)	(33)	(290)	(4,496)	–	(4,835)
At 31 March 2020	121,596	10,183	234,506	132,110	2,641	501,036
Net book value						
At 31 March 2020	33,570	841	74,064	27,143	94	135,712
Cost						
At 1 April 2018	126,190	10,760	235,112	125,974	2,735	500,771
Additions	1,941	350	35,160	21,259	–	58,710
Disposal	(161)	(112)	–	(2,517)	–	(2,790)
At 31 March 2019	127,970	10,998	270,272	144,716	2,735	556,691
Accumulated depreciation						
At 1 April 2018	113,198	9,291	192,427	111,453	2,479	428,848
Charge for the year	5,683	552	16,767	12,715	81	35,798
Written back on disposals	(161)	(112)	–	(2,517)	–	(2,790)
At 31 March 2019	118,720	9,731	209,194	121,651	2,560	461,856
Net book value						
At 31 March 2019	9,250	1,267	61,078	23,065	175	94,835

Notes to the consolidated financial statements

For the year ended 31 March 2020 (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 computer and software \$'000	Motor vehicles \$'000	Total \$'000
Cost						
At 1 April 2019	127,953	10,931	270,272	143,387	2,735	555,278
Additions	27,212	59	38,588	19,036	–	84,895
Disposal	(16)	(33)	(290)	(4,499)	–	(4,838)
At 31 March 2020	155,149	10,957	308,570	157,924	2,735	635,335
Accumulated depreciation						
At 1 April 2019	118,704	9,664	209,194	120,418	2,560	460,540
Charge for the year	2,893	484	25,600	14,914	81	43,972
Written back on disposals	(16)	(33)	(290)	(4,496)	–	(4,835)
At 31 March 2020	121,581	10,115	234,504	130,836	2,641	499,677
Net book value						
At 31 March 2020	33,568	842	74,066	27,088	94	135,658
Cost						
At 1 April 2018	126,174	10,691	235,112	124,729	2,735	499,441
Additions	1,940	349	35,160	21,175	–	58,624
Disposal	(161)	(109)	–	(2,517)	–	(2,787)
At 31 March 2019	127,953	10,931	270,272	143,387	2,735	555,278
Accumulated depreciation						
At 1 April 2018	113,182	9,222	192,427	110,272	2,479	427,582
Charge for the year	5,683	551	16,767	12,663	81	35,745
Written back on disposals	(161)	(109)	–	(2,517)	–	(2,787)
At 31 March 2019	118,704	9,664	209,194	120,418	2,560	460,540
Net book value						
At 31 March 2019	9,249	1,267	61,078	22,969	175	94,738

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

12. Leases

The Group has applied HKFRS 16 from 1 April 2019. Please see Note 3(q) for further information.

As of 31 March 2020, the Group has right-of-use assets and lease liabilities as follows:

The Group and the SFC

	2020 \$' 000	At 1 April 2019 \$' 000
Right-of-use assets – Premises	324,040	303,807
Lease liabilities		
Current	96,115	198,160
Non-current	203,558	84,309
	299,673	282,469

- (i) The Group has entered a new lease for premises during the year and recognised right-of-use assets of \$239,030,000 and lease liabilities of \$219,938,000.
- (ii) The Group recognised depreciation expense for right-of-use assets for premises of \$218,796,000 and interest expense on lease liabilities of \$3,487,000 for the year ended 31 March 2020. The total cash outflow for leases during the year was \$206,221,000.
- (iii) During the year, the Group entered into new operating leases for premises and equipment with commencement date after the reporting period. Minimum lease payment throughout the lease term is \$837,057,000.

13. Bank deposits and cash at bank

The effective interest rate on bank deposits as at 31 March 2020 ranged from 1.1% p.a. to 3.0% p.a. (2019: 1.2% p.a. to 3.2% p.a.). These balances matured within one year as at both 31 March 2020 and 31 March 2019.

Reconciliation to cash and cash equivalents:

	2020 \$' 000	2019 \$' 000
Cash at bank and in hand	51,871	71,908
Fixed deposits with banks	2,832,302	3,653,456
Amounts shown in the consolidated statement of financial position	2,884,173	3,725,364
Less: Amounts with an original maturity beyond three months	(2,130,767)	(3,435,707)
Cash and cash equivalents in the consolidated statement of cash flows	753,406	289,657

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

14. 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 and Financial Education Council (IFEC) 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 IFEC 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 2020, the investments in subsidiaries, which are stated at cost less any impairment losses, amounted to \$0.2 (2019: \$0.2). The balance is too small to appear on the statement of financial position which is expressed in thousands of dollars.

15. 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. Due to the short-term nature of the balance, the carrying amount is considered to be the same as their fair value.

We do not provide an ageing analysis of creditors as there was no material overdue creditor balance as at 31 March 2020 and 2019.

16. Provisions

Provisions represent reinstatement cost to restore the premises to its original condition when the lease expires.

17. Debtors, deposits and prepayments

Debtors, deposits and prepayments include \$230,320,000 in receivables (2019: \$194,404,000) which are usually due within 30 days. Due to the short-term nature of the balance, the carrying amount is considered to be the same as their fair value.

We do not provide an ageing analysis of debtors as there was no material overdue debtor balance as at 31 March 2020 and 2019.

18. 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.

19. Capital commitment

Capital commitments for fixed assets contracted for at the end of the year but not yet incurred amounted to \$142,962,000 (2019: \$30,044,000).

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

20. Operating lease commitment

From 1 April 2019, the Group has recognised right-of-use assets for operating leases (see note 3(q) and note 12).

At 31 March 2019, the minimum amount of rent committed to pay for our offices up to 16 December 2021 are as follows:

The Group and the SFC

	2020 \$' 000	2019 \$' 000
Payable in next year	-	201,162
Payable in one to five years	-	84,647
	-	285,809

During the year ended 31 March 2019, \$200,710,000 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.

21. 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 23 in these 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, \$5,989,000 was recovered from the ICF for the ICC's expenses (2019: \$5,859,000). As at 31 March 2020, the amount due to the ICF from the ICC was \$138,000 (as at 31 March 2019: \$54,000).

(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.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

22. 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, interest rate risk, liquidity risk, foreign exchange risk and market 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.

(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 pooled 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 2020, 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 \$34,369,000 (2019: \$39,921,000). As at 31 March 2020, the average duration of the Group's investment portfolio was 1.39 years (31 March 2019: 1.32 years). At 31 March 2020, 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 \$15,806,000 (2019: \$14,430,000).

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 2019.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

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

(c) Liquidity risk

The Group'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. See note 24 for funding requirements.

Balances due within one year equal their carrying balances, as the impact of discounting is not significant, except for lease liabilities. As of 31 March 2020, the contractual undiscounted cash flows for financial liabilities are as follows:

The Group

	Carrying amount \$'000	Contractual undiscounted cash flows				
		Total \$'000	Within one year \$'000	After one year but within two years \$'000	After two years but within five years \$'000	After five years \$'000
<u>2020</u>						
Creditors and accrued charges	167,043	167,043	167,043	–	–	–
Lease liabilities	299,673	313,591	99,449	30,968	118,695	64,479
	466,716	480,634	266,492	30,968	118,695	64,479
<u>2019</u>						
Creditors and accrued charges	189,855	189,855	189,855	–	–	–

(d) Foreign exchange risk

The Group's investment guidelines for our investment portfolio only allow investments in assets denominated in Hong Kong dollars (HKD), US dollars (USD) and renminbi. Exposure to renminbi should not exceed 5% of the investment portfolio. The majority of the financial assets are denominated either in USD or HKD which are pegged within the Convertibility Zone. For the years ended 31 March 2020 and 2019, the exchange loss was mainly driven by the USD revaluation on financial assets.

As at 31 March 2020, the Group had financial assets denominated in USD of \$3,785,308,000 (2019: \$3,858,653,000). The USD/HKD exchange rate was 7.75 (2019: 7.85), it was estimated that a general change of 100 basis points in the USD/HKD exchange rate, with all other variables held constant, would increase the Group's surplus and accumulated surplus by approximately \$37,853,000 (2019: decrease by \$38,586,000).

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

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

(e) Market risk

The investment activities of the Group also 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 risks will be reflected in the price and the carrying value of the financial assets concerned.

The Group's investment guidelines allow the Group to invest in non-fixed income investment instruments up to 15% of the total value of funds under management. During the year, the Group complied with the above investment policy in order to manage its market risk. 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 ex Japan and MSCI World (Net Dividends), including their returns and volatilities. Based on the weighted average movement of these benchmark indices (21.6%) in the corresponding period, it is estimated that a general increase/decrease of such benchmark indices of 21.6% (2019: 15.2%) would increase/decrease the Group's investment income and the accumulated surplus by approximately \$139,938,000 (2019: \$145,149,000).

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.

(f) 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 2020 (Expressed in Hong Kong dollars)

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

(f) Fair value measurement (cont'd)

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

The Group

	2020			
	Level 1 \$' 000	Level 2 \$' 000	Level 3 \$' 000	Total \$' 000
Assets				
Debt securities				
– Listed	–	413,300	–	413,300
– Unlisted	–	6,169	–	6,169
Pooled funds				
– Unlisted	648,510	–	–	648,510
	648,510	419,469	–	1,067,979
	2019			
	Level 1 \$' 000	Level 2 \$' 000	Level 3 \$' 000	Total \$' 000
Assets				
Debt securities				
– Listed	3,933	643,051	–	646,984
– Unlisted	–	148,962	–	148,962
Pooled funds				
– Unlisted	925,476	–	–	925,476
	929,409	792,013	–	1,721,422

The fair value of the investment in the unlisted pooled funds is determined based on the net asset values of the pooled funds which is publicly available in the active 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, and no 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 2020 (Expressed in Hong Kong dollars)

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

(f) 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 2020 and 2019 except for the following financial instruments, for which their carrying amounts and fair value and the level of fair value hierarchy are disclosed below:

The Group

	2020				
	Carrying amount \$'000	Fair value \$'000	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000
Financial assets at amortised costs – debt securities	2,584,362	2,581,705	970,893	1,610,812	–

	2019				
	Carrying amount \$'000	Fair value \$'000	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000
Financial assets at amortised costs – debt securities	1,545,379	1,536,533	1,536,533	–	–

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

- The fair value of listed 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.

Notes to the consolidated financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

23. 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 the 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 2020, the ICF's maximum liability in respect of claims received was \$2,204,000 (2019: \$2,121,000) and the net asset value was \$2.4 billion (2019: \$2.4 billion).

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 2020, the UECF's maximum liability in respect of claims received was \$10,245,000 (2019: \$10,245,000) and the net asset value was \$82,045,000 (2019: \$79,332,000). There were no outstanding claims against the SDD, CDD and SMF as at 31 March 2020. Claims for any defaults occurring after 31 March 2003 should be made against the ICF.

During the year, the SFC did not provide financial or other support to these unconsolidated structured entities that it was not contractually required to provide (2019: nil). The related party relationships with these entities are disclosed in note 21 of these financial statements.

24. 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 18, 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.

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 2020.

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 2020 and the financial position of the Fund as at that date are set out in the financial statements on pages 135 to 145.

Members of the Committee

The members of the Committee during the year ended 31 March 2020 and up to the date of this report were:

Mr Leung Chung Yin, Rico (Chairman)	(appointed on 30 August 2019)
Mr Lui Kei Kwong, Keith (ex-Chairman)	(retired on 27 August 2019)
Mr Thomas Allan Atkinson	
Dr William Wong Ming Fung, SC, JP	
Mr Kok Ka Keung	(appointed on 1 April 2020)
Mr Tai Chi Kin Calvin	(retired on 31 March 2020)

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

Rico Leung
Chairman

22 May 2020

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 135 to 145, which comprise:

- the statement of financial position as at 31 March 2020;
- 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 statement of cash flows 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 2020, 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 (HKSA) 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 HKSA's 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 HKSA's, 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, 22 May 2020

Statement of profit or loss and other comprehensive income

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Income			
Net investment income	5	59,928	38,557
Exchange loss		(17,001)	(490)
Recoveries		–	50
Compensation payment given up		–	150
		42,927	38,267
Expenses			
Investor Compensation Company Limited expenses	7	5,989	5,859
Auditor's remuneration		179	172
Bank charges		–	409
Professional fees		–	1,472
		6,168	7,912
Surplus and total comprehensive income for the year		36,759	30,355

The notes on pages 139 to 145 form part of these financial statements.

Investor Compensation Fund

Statement of financial position

As at 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Current assets			
Interest receivable		7,185	25,425
Due from Investor Compensation Company Limited		138	54
Fixed deposits with banks	8	2,420,558	2,365,483
Cash at bank	8	651	845
		2,428,532	2,391,807
Current liabilities			
Creditors and accrued charges		268	302
		268	302
Net current assets		2,428,264	2,391,505
Net assets		2,428,264	2,391,505
Representing:			
Compensation fund		2,428,264	2,391,505

Approved and authorised for issue by the Securities and Futures Commission on 22 May 2020 and signed on its behalf by

Tim Lui
Chairman of the SFC

Ashley Alder
Chief Executive Officer of the SFC

The notes on pages 139 to 145 form part of these financial statements.

Statement of changes in equity

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Contributions from Unified Exchange Compensation Fund (note 9) \$' 000	Contributions from Commodity Exchange Compensation Fund (note 9) \$' 000	Accumulated surplus \$' 000	Total \$' 000
Balance at 1 April 2018	994,718	108,923	1,257,509	2,361,150
Surplus and total comprehensive income for the year	–	–	30,355	30,355
Balance at 31 March 2019 and 1 April 2019	994,718	108,923	1,287,864	2,391,505
Surplus and total comprehensive income for the year	–	–	36,759	36,759
Balance at 31 March 2020	994,718	108,923	1,324,623	2,428,264

The notes on pages 139 to 145 form part of these financial statements.

Statement of cash flows

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$' 000	2019 \$' 000
Cash flows from operating activities			
Surplus for the year		36,759	30,355
Adjustments for:			
Net investment income		(59,928)	(38,557)
Exchange loss		17,001	490
		(6,168)	(7,712)
(Increase)/decrease in amount due from Investor Compensation Company Limited		(84)	149
Decrease in creditors and accrued charges		(34)	(1,062)
Net cash used in operating activities		(6,286)	(8,625)
Cash flows from investing activities			
Decrease/(increase) in fixed deposits other than cash and cash equivalents		981,929	(2,333,384)
Debt securities purchased		–	(165,306)
Debt securities sold or redeemed		–	2,092,869
Pooled fund sold		–	338,934
Interest received		78,075	52,523
Net cash generated from/(used in) from investing activities		1,060,004	(14,364)
Net increase/(decrease) in cash and cash equivalents		1,053,718	(22,989)
Cash and cash equivalents at beginning of the year		32,944	55,933
Cash and cash equivalents at end of the year	8	1,086,662	32,944

Analysis of the balance of cash and cash equivalents

	2020 \$' 000	2019 \$' 000
Fixed deposits with banks	1,086,011	32,099
Cash at bank	651	845
	1,086,662	32,944

The notes on pages 139 to 145 form part of these financial statements.

Notes to the financial statements

For the year ended 31 March 2020 (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. For defaults occurring on or after 1 January 2020, the Fund also covers investors' losses in relation to securities traded on a stock market operated by the Shanghai Stock Exchange or the Shenzhen Stock Exchange and in respect of which an order for sale or purchase is permitted to be routed through the northbound link of a Stock Connect arrangement (Stock Connect Securities).

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 may make rules for the maximum amount of compensation that may be paid to a person making claim for compensation. For defaults occurring on or after 1 January 2020, the maximum compensation limit is raised from \$150,000 to \$500,000 per claimant for a single default.

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 The Stock Exchange of Hong Kong Limited (SEHK) (excluding orders routed through the southbound link of a Stock Connect arrangement), futures contracts traded on Hong Kong Futures Exchange Limited (HKFE) and Stock Connect Securities (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.

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(a) Statement of compliance (cont'd)

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. 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.

(b) Basis of preparation

We have prepared these financial statements using the historical cost basis as the measurement basis.

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 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 record exchange gains and losses on translation in the statement of profit or loss and other comprehensive income.

(e) Financial assets

(i) Classification

The Fund classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value through profit or loss, and
- those to be measured at amortised cost.

The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will be recorded in profit or loss.

The Fund reclassifies debt investments when and only when its business model for managing those assets changes.

(ii) Recognition and derecognition

Regular way purchases and sales of financial assets are recognised on settlement-date, the date on which the assets are delivered to the Fund. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Fund has transferred substantially all the risks and rewards of ownership.

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(e) Financial assets (cont'd)

(iii) Measurement

At initial recognition, the Fund measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Debt instruments

Subsequent measurement of debt instruments depends on the Fund's business model for managing the asset and the cash flow characteristics of the asset. The Fund classifies its debt instruments as financial assets measured at amortised cost.

Amortised cost: Assets that are held for the collection of contractual cash flows, where those cash flows represent solely payments of principal and interest, are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising from derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as a separate line item in the statement of profit or loss.

FVPL: A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within other gains/(losses) in the period in which it arises.

(iv) Impairment

The Fund assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

(f) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and fixed deposits with banks with original maturities of three months or less that are readily convertible to known amounts of cash.

(g) Other receivables

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

(h) Provisions 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 reflect 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 is set at \$150,000 per claimant for each default case occurring on or before 31 December 2019 and \$500,000 per claimant for each default case occurring on or after 1 January 2020.

As the Fund is continually updating information in respect of the 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.

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(i) 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.

(j) 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.

(k) 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 Fund or an entity related to the Fund.
 - (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.

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 2020 (Expressed in Hong Kong dollars)

5. Net investment income

	2020 \$' 000	2019 \$' 000
Interest income from bank deposits	59,928	34,947
Interest income on financial assets at fair value through profit or loss	–	22,629
Realised loss on disposal of pooled fund	–	(10,350)
Realised loss on redemption/disposal of debt securities	–	(8,669)
Net investment income	59,928	38,557

6. Levy from SEHK and HKFE

From 1 April 2003, the Fund received a levy chargeable on securities traded on SEHK and futures contracts traded on HKFE 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 2019 which came into effect on 1 January 2020, the Fund is entitled for levy chargeable on securities traded on SEHK (excluding orders routed through the southbound link of a Stock Connect

arrangement), futures contracts traded on HKFE and Stock Connect Securities and the trigger levels for levy suspension and re-instatement were raised to \$3 billion and \$2 billion respectively.

Pursuant to 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. The changes in trigger levels do not affect the levy suspension in effect.

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 2020, the ICC incurred costs of \$5,989,000 for its operations (2019: \$5,859,000) which were reimbursed by the Fund.

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

8. Fixed deposits with banks and cash at bank

The effective interest rates on bank deposits at 31 March 2020 ranged from 0.93% p.a. to 2.86% p.a. (2019: 1.40% p.a. to 3.44% p.a.). The balances of deposits at both 31 March 2020 and 31 March 2019 mature within one year.

Reconciliation to cash and cash equivalents

	2020 \$' 000	2019 \$' 000
Cash at bank	651	845
Fixed deposits with banks	2,420,558	2,365,483
Amounts shown in the statement of financial position	2,421,209	2,366,328
Less: Amounts with an original maturity of beyond three months	(1,334,547)	(2,333,384)
Cash and cash equivalents in the statement of cash flows	1,086,662	32,944

9. 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 2020, the SFC had \$994,718,000 (2019: \$994,718,000) and \$108,923,000 (2019: \$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.

10. Related party transactions

The Fund has related party relationships with the SFC, the 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 2019 and 2020 (refer to notes 7 and 9).

11. Financial risk management

The Fund's interest bearing assets mainly comprise fixed 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 2020, it was 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 \$24,206,000 (2019: \$23,655,000). The exposure to credit, liquidity and foreign currency risks arises in the normal course of the Fund's operation.

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.

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

11. Financial risk management (cont'd)

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

The Fund's policy allows the Fund to have US dollars (USD) and renminbi foreign exchange exposures. As at 31 March 2020, the Fund had exposure to USD only. As Hong Kong dollars (HKD) are pegged with USD, the Fund was exposed to limited foreign exchange risk at the end of the reporting period. For the years ended 31 March 2020 and 2019, the Fund's exchange loss was mainly driven by the USD revaluation on financial assets.

As at 31 March 2020, the Fund had financial assets denominated in USD of \$1,339,501,000 (2019: \$1,320,894,000). The USD/HKD exchange rate was 7.75 (2019: 7.85), it was estimated that a change of 100 basis points in the USD/HKD exchange rate, with all other variables held constant, would increase the Fund's surplus and accumulated surplus by approximately \$13,395,000 (2019: decrease by \$13,209,000).

12. Provision for compensation and contingent liabilities

The Fund assessed and concluded that there was no provision for compensation as at 31 March 2020 and 2019.

As at the date of this report, 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 in aggregate is \$2,204,000 (2019: \$2,121,000). This is determined based on the lower of the maximum compensation limit per claimant (detailed in note 3(h)) or the amount claimed.

Unified Exchange Compensation Fund

Report of the Securities Compensation Fund Committee

The members of the Securities Compensation Fund Committee (the Committee) present their annual report together with the audited financial statements for the year ended 31 March 2020.

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 2020, the Fund transferred \$994,718,000 to the ICF. After the 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 2020 and the financial position of the Fund as at that date are set out in the financial statements on pages 149 to 159.

Members of the Committee

The members of the Committee during the year ended 31 March 2020 and up to the date of this report were:

Mr Leung Chung Yin, Rico (Chairman)	(appointed on 30 August 2019)
Mr Lui Kei Kwong, Keith (ex-Chairman)	(retired on 27 August 2019)
Mr Thomas Allan Atkinson	
Dr William Wong Ming Fung, SC, JP	
Mr Yiu Ka Yan Wilfred	(appointed on 1 April 2020)
Ms Kwok Hom Siu	(appointed on 1 April 2020)
Mr Tai Chi Kin Calvin	(retired on 31 March 2020)
Ms Mak Po Shuen	(retired on 31 March 2020)

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

Rico Leung

Chairman

11 May 2020

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 149 to 159, which comprise:

- the statement of financial position as at 31 March 2020;
- 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 statement of cash flows 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 2020, 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 HKSA's 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 HKSA's, 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.
- 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, 11 May 2020

Statement of profit or loss and other comprehensive income

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Income			
Interest income		1,846	1,534
Recoveries	4	(1)	1,074
		1,845	2,608
Expenses			
Auditor's remuneration		82	79
Bank charges		–	1
		82	80
Surplus and total comprehensive income for the year		1,763	2,528

The notes on pages 153 to 159 form part of these financial statements.

Unified Exchange Compensation Fund

Statement of financial position

As at 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$'000	2019 \$'000
Current assets			
Equity securities received under subrogation	4	–	1
Interest receivable		243	187
Accounts receivable		9	9
Fixed deposits with banks	6	92,879	88,338
Cash at bank	6	470	1,922
		93,601	90,457
Current liabilities			
Creditors and accrued charges	7	10,306	10,325
Relinquished trading rights payable to SEHK	8	1,250	800
		11,556	11,125
Net current assets		82,045	79,332
Net assets		82,045	79,332
Representing:			
Compensation fund		82,045	79,332

Approved and authorised for issue by the Securities Compensation Fund Committee on behalf of the Securities and Futures Commission on 11 May 2020 and signed on its behalf by

Rico Leung

Chairman

Wilfred Yiu

Committee Member

The notes on pages 153 to 159 form part of these financial statements.

Statement of changes in equity

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Trading rights deposits from SEHK (note 8) \$'000	Excess transaction levy from SEHK (note 9) \$'000	Additional contributions from SEHK and the SFC (note 10) \$'000	Other contributions (note 11) \$'000	Accumulated surplus \$'000	Contributions to Investor Compensation Fund (note 12) \$'000	Total \$'000
Balance at 1 April 2018	53,500	353,787	630,000	6,502	26,733	(994,718)	75,804
Net contributions from SEHK	1,000	-	-	-	-	-	1,000
Surplus and total comprehensive income for the year	-	-	-	-	2,528	-	2,528
Balance at 31 March 2019 and 1 April 2019	54,500	353,787	630,000	6,502	29,261	(994,718)	79,332
Net contributions from SEHK	950	-	-	-	-	-	950
Surplus and total comprehensive income for the year	-	-	-	-	1,763	-	1,763
Balance at 31 March 2020	55,450	353,787	630,000	6,502	31,024	(994,718)	82,045

The notes on pages 153 to 159 form part of these financial statements.

Unified Exchange Compensation Fund

Statement of cash flows

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

	Note	2020 \$' 000	2019 \$' 000
Cash flows from operating activities			
Surplus for the year		1,763	2,528
Adjustments for:			
Interest income		(1,846)	(1,534)
Recoveries		1	–
		(82)	994
(Decrease)/increase in creditors and accrued charges		(19)	22
Increase in relinquished trading rights payable to SEHK		450	50
Net cash generated from operating activities		349	1,066
Cash flows from investing activities			
Increase in fixed deposits other than cash and cash equivalents		(61,350)	–
Interest received		1,790	1,445
Net cash (used in)/generated from investing activities		(59,560)	1,445
Cash flows from financing activities			
Net trading rights deposits from SEHK		950	1,000
Net cash generated from financing activities		950	1,000
Net (decrease)/increase in cash and cash equivalents		(58,261)	3,511
Cash and cash equivalents at beginning of the year		90,260	86,749
Cash and cash equivalents at end of the year	6	31,999	90,260

Analysis of the balance of cash and cash equivalents

	2020 \$' 000	2019 \$' 000
Fixed deposits with banks	31,529	88,338
Cash at bank	470	1,922
	31,999	90,260

The notes on pages 153 to 159 form part of these financial statements.

Notes to the financial statements

For the year ended 31 March 2020 (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 the 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, it 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 (2019: 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 detailed in note 4; replenishments from SEHK detailed in note 15; other contributions detailed in note 11; and excess transaction levy received before the SFO became effective from 1 April 2003 detailed in note 9.

The Fund defines "capital" as including all elements of the Fund less contributions to the ICF (note 12) and less contributions from SEHK (trading rights deposits from SEHK detailed in note 8).

Notes to the financial statements

For the year ended 31 March 2020 (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. 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.

(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.

At the end of each reporting period, the fair value of the equity securities received under subrogation is remeasured, with any resultant gain or loss being included in "Recoveries" in statement of profit or loss and other comprehensive income. Dividend income, if any, is also included in "Recoveries".

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(c) Recognition of income (cont'd)

(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.

(d) Impairment of financial assets

The Fund assesses on a forward-looking basis the expected credit losses associated with its financial assets carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

(e) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and fixed deposits with banks with original maturities of three months or less that are readily convertible to known amounts of cash.

(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 an 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 an outflow of economic benefits is remote.

(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 Fund or an entity related to the Fund.
 - (vi) The entity is controlled or jointly controlled by a person identified in (a).

Unified Exchange Compensation Fund

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

3. Significant accounting policies (cont'd)

(h) Related parties (cont'd)

(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.

4. Recoveries/Equity securities received under subrogation

For the year ended 31 March 2019, the Fund recognised as recoveries the payment from the liquidator of C.A. Pacific Securities Ltd. and C.A. Pacific Finance Ltd (for the year ended 31 March 2020: nil).

As at 31 March 2020, the equity securities received under subrogation amounted to \$142 (as at 31 March 2019: \$1,191). The balance as at 31 March 2020 is too small to appear on the statement of financial position which is expressed in thousands of dollars.

5. 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.

6. Fixed deposits with banks and cash at bank

The effective interest rates on bank deposits at 31 March 2020 ranged from 1.06% p.a. to 2.33% p.a. (2019: 1.31% p.a. to 2.00% p.a.). The balances of deposits at both 31 March 2020 and 31 March 2019 mature within one year.

Reconciliation to cash and cash equivalents

	2020 \$'000	2019 \$'000
Cash at bank	470	1,922
Fixed deposits with banks	92,879	88,338
Amounts shown in the statement of financial position	93,349	90,260
Less: Amounts with an original maturity of beyond three months	(61,350)	–
Cash and cash equivalents in the statement of cash flows	31,999	90,260

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

7. Creditors and accrued charges

Creditors and accrued charges comprised mainly compensation payments re-established for those cheque payments that were not cleared for more than 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 HKFRS 9, Financial instruments 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.

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

According to Section 104 of the repealed Securities Ordinance, SEHK contributes to the SFC 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 \$2,000,000 in respect of 40 new trading rights were received from SEHK and deposits of \$600,000 in respect of 12 relinquished trading rights were refunded to SEHK. As at 31 March 2020, 25 trading rights totalling \$1,250,000 were relinquished but not yet refunded (2019: 16 trading rights totalling \$800,000 were relinquished but not yet refunded).

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

	2020 \$'000	2019 \$'000
Balance brought forward	54,500	53,500
Add: new trading rights issued	2,000	1,350
Less: relinquished trading rights refunded	(600)	(300)
Adjustment for: increase in relinquished trading rights payable to SEHK	(450)	(50)
Balance carried forward	55,450	54,500

9. 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. A portion of this balance was contributed to the ICF and note 12 provides more details on the contributions made to the ICF.

10. Additional contributions from SEHK and the SFC

Following the revisions 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 from 1998 to 2001. A portion of this balance was contributed to the ICF and note 12 provides more details on the contributions made to the ICF.

Notes to the financial statements

For the year ended 31 March 2020 (Expressed in Hong Kong dollars)

11. Other contributions

In October 1993, a member of SEHK made a special contribution of \$3,500,000 to the Fund 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 \$3,002,000 to the Fund under the provisions of the Exchanges (Special Levy) Ordinance. A portion of this balance was contributed to the ICF and note 12 provides more details on the contributions made to the ICF.

12. 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 from the Fund up to 31 March 2020 amounted to \$994,718,000 (2019: \$994,718,000), no further contributions has been made to the ICF since 1 April 2005.

13. Related party transactions

The Fund has related party relationships with the ICF and the SFC. There were no related party transactions during the years ended 31 March 2020 and 2019.

14. Financial risk management

The Fund's interest bearing assets mainly comprise fixed 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 2020, it was 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 \$929,000 (2019: \$883,000). 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 2020 (Expressed in Hong Kong dollars)

15. 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 2020, 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:

	2020 \$'000	2019 \$'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 to request replenishment from SEHK in the near future.