



SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

Regulation for Quality Markets

Annual Report 2017-18

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Message from Chairman and CEO



Carlson Tong
Chairman

We remain squarely focussed on upholding fair and orderly markets to foster investor confidence.

In today's complex and increasingly interconnected markets, we are determined to tackle emerging regulatory challenges and keep pace with technological innovation to maintain healthy, sustainable market development. It is crucial that we press ahead with initiatives to strengthen the competitiveness of our markets and advance Hong Kong's position as an international financial centre (IFC) whilst ensuring appropriate investor protection.

Hong Kong as a leading IFC

Over the past few years, we prioritised three initiatives to lay the groundwork for Hong Kong's future development as a global financial centre connecting mainland China with the rest of the world.

First, we recognise that Hong Kong needs to attract a more diverse range of quality listings to enhance its competitiveness as a capital-raising centre, including emerging and innovative firms.

Second, Hong Kong has the potential to develop into a fully-fledged asset management centre. To help achieve this, we focus on enhancements to the local regulatory framework for funds, asset managers and service providers whilst expanding the potential markets for funds domiciled and managed in Hong Kong.

Thirdly, we are working on a number of initiatives to establish Hong Kong as the premier centre for managing Mainland risk via exchange-traded and other over-the-counter hedging tools, and as a booking hub for Asian derivatives.

With its unique relationship with the Mainland, Hong Kong clearly stands to benefit from greater cross-border connectivity and two-way capital flows. But

we must also ensure the needs of both Mainland and international investors are met amidst the Mainland's emergence as the world's second-largest economy and its integration with global capital markets.

Stock Connect is a game changer which provides unprecedented opportunities for Hong Kong. As a next step, we will pursue its further expansion as well as other mutual market access schemes, including Bond Connect, ETF¹ Connect and Mutual Recognition of Funds.

Responsive regulation for investor protection

As the financial industry becomes ever more complex and dynamic, we remain squarely focussed on upholding fair and orderly markets to foster investor confidence. Our position is clear—market development is founded on world-class regulatory standards.

We must adopt the right regulatory structure and approach to carry out our mandates. Our real-time, front-loaded approach emphasises earlier, more targeted intervention, allowing us to stay vigilant in getting ahead of threats to the integrity, safety and quality of our markets.

Using the full array of tools available to us, including the Securities and Futures (Stock Market Listing) Rules (SMLR), we now raise objections to listings or capital raisings and direct suspensions of listed companies' shares where necessary to safeguard the interests of investors. We also monitor licensed firms' financial and conduct risks and intervene quickly when we see problems. As a result of this real-time approach, we have already seen positive changes in market behaviour.

¹ Exchange-traded funds.



Our position is clear—market development is founded on world-class regulatory standards.



Ashley Alder
Chief Executive Officer

Our recent guidelines on online distribution and advisory platforms for investment products and baseline cybersecurity requirements for internet brokers were examples of how we proactively introduce new proposals and reforms to tackle evolving market risks, facilitate market development and protect investors.

New technologies provide convenience for investors but come with risks. We keep a close watch on cryptocurrencies and initial coin offerings, intervening where appropriate. We also launched the SFC regulatory sandbox for qualified firms to conduct regulated activities utilising financial technologies.

Data analytics are important to keep in step with fast-moving markets. To this end, we have introduced new initiatives to help us analyse data for regulatory purposes and address new technological developments.

Collaboration

The globalisation of market-based finance and increasing capital market connectivity make it essential that we collaborate closely with other regulators.

In particular, our cooperation with the China Securities Regulatory Commission (CSRC) enables us to manage common risks. The strength of our relationship and continued alignment of our interests will be key as the scope of mutual market access programmes broadens over time.

Globally, we take an active part in the international regulatory community, particularly through chairmanship of the IOSCO Board and our involvement in the Financial Stability Board, to ensure that we contribute to global policymaking which may have an impact on our markets.

We will also maintain close communication and seek to formalise and strengthen cooperation with local regulators and law enforcement agencies.

In our own operations, cross-divisional collaboration is now the norm as the issues we deal with require us to address them as “One SFC”. We have set up multi-disciplinary taskforces and a Risk Review Group to assess the opportunities and risks we face.

Looking to the future

Effective regulation together with strong investor protection and extensive collaboration with regulatory counterparts will provide a solid foundation for far greater overlap between expanding pools of international and Mainland liquidity in the years to come. Our strategic priorities are set out in more detail in the next chapter.

In our day-to-day work, we maintain robust financial controls and prudent resource allocation and remain committed to corporate social responsibility efforts.

As ever, we are grateful to the Board and our staff for their commitment, hard work and professionalism in yet another challenging year.

Carlson Tong
Chairman

Ashley Alder
CEO

Strategic Priorities

Strengthening the integrity and soundness of Hong Kong's securities and futures markets is at the heart of our mission to advance Hong Kong's position as a leading international financial centre. We strive to enhance our regulatory regime and establish closer cooperation with counterparts in Hong Kong, mainland China and overseas. In our daily operations, we seek to enhance efficiency and make optimal use of our resources.

Our approach

One year on, we are moving forward with our "front-loaded" regulatory approach which emphasises earlier, more targeted and systematic intervention to tackle market irregularities and corporate misconduct. This means delivering fast and responsive regulation and maximising the impact of our actions, with a particular focus on the greatest threats and systemic risks. Our new approach has already made an immediate, positive impact on the market.

Applying this approach to intermediary supervision helps promote earlier and more targeted behavioural change. Increasingly, we conduct thematic reviews of high-risk areas in addition to our routine inspections. We also issue more thematic guidance to keep the market informed about our priorities in a transparent manner and ensure that the reasons for our actions are clearly and promptly understood.

As the challenges we face continue to cut across all of our regulatory functions, we now adopt a "One SFC" approach, introducing organisational changes and cross-divisional teams to achieve closer collaboration and better efficiency at an operating level. One example of this is the establishment of "ICE" (Intermediaries, Corporates, Enforcement), a cross-divisional working group to tackle corporate misconduct and protect investors.

Our capital markets are increasingly sophisticated and technology-driven. We deploy resources to keep up with rapid technological innovation and understand how it intersects with our work. New initiatives help us manage evolving risks and analyse data for regulatory purposes. This will be a major theme in the years to come.



Current initiatives

The overall aim of our strategic priorities is to maintain quality markets, protect investors and ensure sustainable market development whilst addressing emerging threats and risks.

Listing matters

In response to changing market conditions and evolving risks, we exercise our statutory powers under the Securities and Futures (Stock Market Listing) Rules (SMLR)¹ and more generally under the Securities and Futures Ordinance (SFO) in the regulation of listing matters to intervene in serious cases at an early stage. This helps protect the investing public and suppress illegal and improper market practices. It also complements our enforcement work aimed at pursuing wrongdoers, seeking remediation and deterring misconduct.

At the policy level, we are conducting a review of listing regulation with The Stock Exchange of Hong Kong Limited (SEHK) to maintain market quality and address problematic listed company behaviour. The review covers regulatory issues relating to GEM², capital raisings, backdoor listings, continuing listing criteria and the delisting framework. As a result of this review, SEHK conducted public consultations on Listing Rules amendments³ and will consult the public on backdoor listings and continuing listing criteria.

¹ Under the SMLR, we may raise objections to listing applications or direct SEHK to suspend trading in a listed company's shares.

² Formerly known as the Growth Enterprise Market.

³ The public consultations cover Listing Rules amendments relating to GEM, capital raisings and the delisting framework.

We also worked with Hong Kong Exchanges and Clearing Limited (HKEX) to introduce a new listing regime allowing the listings of biotechnology companies which do not meet the financial eligibility requirements of the Main Board and innovative and high growth companies with weighted voting rights (WVR) structures. In addition, the new regime creates a new concessionary route for secondary listings to attract innovative companies which are primary-listed elsewhere.

We have adopted an enhanced audit approach to our statutory oversight of SEHK's listing function, including the vetting of initial public offerings, to focus on whether it is discharging its duties under the SFO, whether its systems and processes for performing its listing function are adequate and how well it manages conflicts of interest as a regulator and as part of a for-profit organisation. This approach clearly delineates the roles of the SFC as a regulator and of SEHK and HKEX as regulatees under the SFO. We will publish periodic supervisory review reports as we have done in the past.

Further to the conclusion of the joint SFC-SEHK consultation on proposed enhancements to SEHK's decision-making and governance structure for listing regulation, a new Listing Policy Panel has been set up as an advisory, consultative and steering body outside the SFC and SEHK to initiate and centralise discussions of listing policies with broader regulatory or market implications.

Our cross-divisional "ICE" working group tackles problems affecting the quality of our markets, initially focussed on price volatility in GEM stocks and GEM placings with a high concentration of shareholders. The "ICE" mission has now been broadened to cover more serious instances of misconduct in the listed market. Combining expertise and resources from across the organisation enables us to identify emerging problems and formulate strategies to address them proactively at an early stage.

We are analysing public responses to a consultation on proposed amendments to the Codes on Takeovers and Mergers and Share Buy-backs which ended in April 2018. The proposed changes aim to afford fair treatment for shareholders and protect the interests of those who participate in Hong Kong's securities markets.



Intermediaries

Over the past few years, the number of corporate and individual licensees reached new highs, whilst licensed firms and individuals engaged in more SFC-regulated activities. To achieve better regulatory outcomes, we refined our approach to licensing applications to focus on key risks. We also take a proactive supervisory approach to reducing conduct and prudential risks involving intermediaries and enhancing their governance and accountability.

A study we conducted last year showed that brokers' total margin loans had grown nine times between 2006 and 2017 with a significant deterioration in quality. We are reviewing brokers' securities margin financing business to identify ways to enhance risk management. We also conducted a review to assess the adequacy of large and medium-sized brokers' internal controls over the supervision of account executives who mainly serve retail investors. We will share our observations from these reviews with the industry.

In our daily supervision, we place a great deal of emphasis on senior management accountability to ensure proper conduct. Under the Manager-In-Charge (MIC) regime, more than 10,000 individuals were appointed by licensed corporations as MICs responsible for managing important functions. In addition, firms have taken concrete measures to enhance their governance structures, better delineating responsibilities amongst staff at the local and global levels and aligning the Responsible Officers' regime with the MIC regime. We will review firms' compliance with the MIC regime during inspections.

Strategic Priorities

On the policy side, we have now finalised proposed amendments to the Securities and Futures (Professional Investor) Rules to enhance market transparency and standardise the rules for prescribing professional investors. In May 2018, we concluded a consultation on the disclosure requirements for monetary and non-monetary benefits applicable to discretionary accounts, providing a six-month grace period for implementation. We also consulted the public on changes to the Securities and Futures (Financial Resources) Rules and on the application of suitability and other disclosure requirements to sales of complex products⁴ in an offline environment.

The use of instant messaging poses new supervisory and record-keeping challenges and we have provided guidance on the controls and procedures which firms are expected to put in place when receiving clients' orders via instant messaging services.

To more effectively monitor compliance during our inspections of brokers with high turnover, we commenced a data analytics project to develop standards for capturing and storing trading-related data. We also plan to release a revamped Business and Risk Management Questionnaire⁵ to enhance our collection of data on licensed corporations' business activities and risk exposures.

Asset management

Developing Hong Kong as an international, full-service asset management centre is one of our key strategic objectives. This is complemented by maintaining robust local regulations which align with international standards.

Over the years, we expanded the potential markets for Hong Kong public funds by entering into Mutual Recognition of Funds (MRF) arrangements with the Mainland, Australia, Malaysia, Taiwan, Switzerland and recently France. They allow Hong Kong's fund industry to tap overseas markets and provide additional investment opportunities for both local and overseas investors. We are exploring similar MRF arrangements with other overseas jurisdictions.

We will publish consultation conclusions on proposed amendments to the Code on Unit Trusts and Mutual Funds to update the regulatory regime for SFC-authorized funds and to address the risks posed by financial innovation and fast-moving market developments. We will also introduce enhanced fund data reporting requirements which will expand the scope, depth and frequency of the data submitted to us by Hong Kong-domiciled, SFC-authorized funds with regard to asset allocation, liquidity and securities financing and borrowing transactions.

For retail funds, we remain focussed on expanding distribution channels and enhancing market infrastructure. For example, we concluded a consultation in March 2018 on proposed Guidelines on Online Distribution and Advisory Platforms which will allow investors more flexibility to manage their investments online whilst providing additional protection for complex products.

We are also working with the China Securities Regulatory Commission (CSRC) and the Mainland and Hong Kong exchanges and clearing houses to broaden our mutual market access arrangements to include exchange-traded funds as eligible securities. In ongoing discussions with HKEX, industry participants and stakeholders, we continue to explore a viable business model for an exchange-based fund distribution platform.

We have been working intensively with the Financial Services and the Treasury Bureau on the introduction of the open-ended fund company (OFC) regime, which will provide the industry with an additional choice of investment fund vehicle. The new regime is expected to take effect in 2018 after the completion of the legislative process and the issuance of an OFC regulatory code.

Markets

We actively engage with Mainland authorities on initiatives which will bring mutual benefits to our markets and ensure the smooth operation of cross-border trading links. Trading via Stock Connect has grown over the past few years and we announced

⁴ These refer to products whose terms, features and risks are not reasonably likely to be understood by retail investors because of their complex structures.

⁵ All licensed corporations are required to submit the completed Business and Risk Management Questionnaire to the SFC every year.



increases in the daily quotas in April 2018⁶. We have also been working closely with the CSRC and other parties to widen the scope of Stock Connect, including expanding the coverage of eligible stocks.

The recently concluded SFC-CSRC memorandum of understanding (MoU) to facilitate regulatory and enforcement cooperation in the Mainland and Hong Kong futures markets laid the foundation to develop Hong Kong as a centre for managing exposure to the Mainland market. It recognises the importance of developing appropriate financial instruments and tools for investors in both markets to manage the risks underlying larger two-way capital flows. Through the MoU, we formalised arrangements to enhance supervisory assistance and information exchange on cross-boundary derivatives, futures exchanges and futures brokers.

We are developing an investor identification model for northbound trading under Stock Connect for implementation in the third quarter of 2018. For a similar regime for southbound trading to be introduced later, we will work with HKEX to establish an operational model.

Hong Kong is well placed to serve as Asia’s booking hub for derivatives. It is uniquely positioned to host markets for exchange-traded and over-the-counter (OTC) derivatives spanning equities, currency, fixed income and commodities for retail and wholesale risk management.

In line with other markets, an OTC derivatives regime is being implemented in phases in Hong Kong. In July 2017, we concluded a consultation on a proposed regulatory capital regime for licensed corporations engaged in OTC derivatives activities. We launched a joint consultation with the Hong Kong Monetary Authority (HKMA) in March 2018 to introduce trading determination criteria and Phase 2 clearing as well as the use of Legal Entity Identifiers in OTC derivatives trade reporting. Separately, we consulted the market to refine the scope of regulated activities under the OTC derivatives licensing regime. We will consult on margin requirements for non-centrally cleared OTC derivatives in the second quarter of 2018 and amendment rules for implementing OTC derivatives reform at a later stage.

We established a cross-divisional Risk Review Group to identify and assess the opportunities and risks we face as well as to engage with stakeholders to understand the potential business and regulatory implications of new and emerging issues.

Together with HKEX, we are reviewing the Volatility Control Mechanism⁷ (VCM) to ensure that it is aligned with international standards and to cope with local market developments. We are also working with key stakeholders to identify the changes needed to implement a paperless securities market and plan to consult on the proposed operational model in 2018.

Enforcement

To protect the interests of the investing public and send strong deterrent messages, we use the full spectrum of sanctions and remedies available to us under the SFO through criminal, administrative, compensatory and disciplinary actions. Under our new “front-loaded” approach, SFC divisions work together closely to tackle increasingly complex regulatory problems as “One SFC” and focus our resources on the most serious enforcement cases which pose the greatest threats to our markets.

We completed a reorganisation of the Enforcement Division and realigned its priorities with those of the SFC as a whole. Corporate fraud remains our top enforcement priority and we will target groups which

⁶ With effect from 1 May 2018, the new daily quota for each of the northbound trading links is RMB52 billion and the new daily quota for each of the southbound trading links is RMB42 billion.

⁷ The VCM imposes a price limit for trading in major constituent stocks and futures contracts for short periods under extreme price movements. HKEX introduced the VCM to its cash and derivatives markets in August 2016 and January 2017.

Strategic Priorities

collude to defraud investors. Our work also focuses on insider dealing and market manipulation, intermediary and sponsor misconduct and money laundering. In addition, we pool resources from across the organisation to combat mis-selling of financial products.

We encourage firms to report to us any suspected breaches of rules or regulations. Prompt and complete self-reporting demonstrates the soundness of a firm's internal control systems and helps detect trading misconduct. In enforcement investigations and proceedings, we recognise and reward firms and individuals' cooperation as this helps us investigate more serious legal or regulatory breaches and achieve timely and desirable enforcement outcomes.

We actively encourage the public to assist us with our investigation work by providing information about persons we seek but cannot trace in relation to our inquiries. Our website also provides an online form for the public to report corporate fraud and insider dealing.

Investors

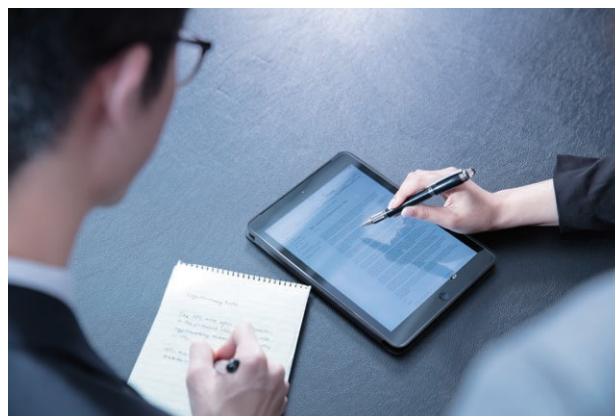
Protecting investors is one of our main regulatory objectives. To safeguard the interests of investors, we act as a standard setter, a gatekeeper and an enforcer of the laws governing the securities and futures markets.

In the conduct of our day-to-day work, we perform gatekeeping functions in licensing qualified corporations and individuals to ensure that they are fit and proper and authorising investment products offered to the public. We also supervise intermediaries and monitor their compliance with laws and regulatory standards, with a particular focus on their business conduct and financial soundness. We maintain fair and orderly markets for investors through our oversight of listing and takeovers matters as well as our supervision and monitoring of exchanges, clearing houses, share registrars and automated trading services providers. Where appropriate, we take enforcement action to combat misconduct and malpractice in our markets and seek redress for investors.

We maintain a robust regulatory regime for SFC- authorised funds and regularly enhance it to provide investors with appropriate safeguards. To address risks posed by financial innovation and fast-moving market developments, we recently proposed amendments

to the Code on Unit Trusts and Mutual Funds to strengthen requirements for key operators, provide flexibility for funds' investment activities with enhanced safeguards and introduce new fund types.

In light of significant investor interest in cryptocurrencies⁸ and the use of initial coin offerings (ICOs) to raise funds in Hong Kong, we took regulatory action against a number of cryptocurrency exchanges and ICO issuers and issued two statements alerting investors to their potential risks. We will remain vigilant in policing the market and monitor the latest developments.



As suitability obligations are the cornerstone of investor protection, we introduced new guidelines for online distribution and advisory platforms to provide retail investors with additional protection in relation to complex products. The guidelines also allow more flexibility for investors to manage their investments online.

In recognition of the potential risks to investors associated with WVR structures, there are important safeguards in HKEX's rules for the new listing regime which took effect on 30 April 2018, including the introduction of measures to protect non-WVR holders' right to vote and enhancements to corporate governance and disclosure requirements.

We completed a study of possible enhancements to the investor compensation regime and launched a consultation on proposed changes, including raising the compensation limit per investor in case of broker default, in April 2018.

⁸ Cryptocurrencies which are "securities" are subject to the securities laws of Hong Kong and fall within the jurisdiction of the SFC.

Improving financial literacy is essential to equip investors with the necessary knowledge and skills to make well-informed financial and investment decisions. The Investor Education Centre, an SFC-funded subsidiary, provides comprehensive financial information, tools and educational resources to help individuals manage their money wisely.

Technology

The accelerating pace of technological change and increasingly complex financial markets have transformed the way our markets operate, requiring the use of new regulatory technologies to keep pace. We now adopt a more structured approach to monitor market risks and opportunities and gather market intelligence.

During the year, we established the cross-divisional Market Intelligence Programme and a Data Analytics Group to draw on expertise from across the organisation to analyse data for regulatory purposes and address new technological developments.

To facilitate the use of innovative technology in delivering financial services, we launched the SFC regulatory sandbox in September 2017 to enable qualified firms⁹ to conduct regulated activities under some licensing conditions.



Regulatory collaboration

In keeping with Hong Kong's status as an international financial centre, it is vital that we work closely and build strong relationships with our regulatory counterparts, locally and around the world, and take an active role in global regulatory initiatives, including through our involvement in global regulatory bodies, information sharing and cooperation arrangements¹⁰.

Led by our Chief Executive Officer Mr Ashley Alder, the Board of the International Organization of Securities Commissions (IOSCO) aims to make IOSCO's work more relevant to its wider membership, promote interaction between members from emerging and developed markets and clarify the intersection between IOSCO's policy work and that of the Financial Stability Board (FSB). Recent discussions within IOSCO have focussed on cryptocurrencies, ICOs, cybersecurity and financial technologies. Mr Alder is also a member of the FSB's Plenary and Steering Committee and our senior staff actively participate in IOSCO's and FSB's committees and working groups.

Locally, we work closely with the HKMA and HKEX on both policy and operational levels. Over the past year, we joined hands with the Independent Commission Against Corruption (ICAC) and the Hong Kong Police in some of our operations. To formalise and strengthen cooperation in combating financial crime, we entered into an MoU with the Hong Kong Police in August 2017 for case referrals and joint investigations as well as the exchange and use of information and the mutual provision of investigative assistance.

As the Mainland and Hong Kong markets integrate, the expansion of cross-border capital flows and intermediary activity must be safeguarded by a strong regulatory partnership. To manage common risks and seek regulatory assistance and enforcement cooperation, we strengthened our relationships with the CSRC and other Mainland regulatory authorities, with whom our regulatory interests are increasingly aligned.

⁹ To qualify, a firm must either be a licensed corporation or a start-up firm which intends to carry on a regulated activity. It must be fit and proper, utilise innovative technologies and be able to demonstrate a genuine and serious commitment to carry on regulated activities through the use of financial technologies.

¹⁰ These include developing protocols for joint actions with the ICAC and the Hong Kong Police.

Mission and Mandates

Mission statement

As a financial regulator in an international financial centre, the SFC strives to strengthen and protect the integrity and soundness of Hong Kong's securities and futures markets for the benefit of investors and the industry.

Mandates

Our work is defined and governed by the Securities and Futures Ordinance (SFO), which sets out our powers, roles and responsibilities. We have six statutory objectives:

- Maintain and promote a fair, efficient, competitive, transparent and orderly securities and futures industry
- Help the public understand the workings of the industry
- Provide protection for the investing public
- Minimise crime and misconduct in the industry
- Reduce systemic risks in the industry
- Assist the Government in maintaining Hong Kong's financial stability

In 2012, the SFO was amended to broaden our statutory investor education objective. As a result, we delegated our education function to a subsidiary, the Investor Education Centre, which provides financial education and information to consumers. Another subsidiary, the Investor Compensation Company Limited, was established in 2003 to manage and administer claims against the Investor Compensation Fund. It provides a measure of protection for investors in cases of broker default.

Regulatory functions

Our work can be divided into the following areas:

Intermediaries

We set standards and qualifying criteria for corporations and individuals operating in our markets under the SFO. To protect the investing public, we allow only "fit and proper" persons to be licensed.

We supervise licensed intermediaries to ensure financial soundness and compliance with business conduct requirements through off-site monitoring and on-site inspections. Our approach aims to detect risks early and through timely intervention prevent them from spreading. We promote the industry's awareness of emerging issues and encourage proper market conduct by providing appropriate guidance.

We work closely with local and overseas regulatory counterparts and participate in international supervisory fora to enhance cooperation and coordination.

Investment products

To develop Hong Kong as a full-service international asset management centre and preferred place for fund domicile, we formulate policies and support initiatives relating to the regulation of the asset management industry.

We maintain a robust regulatory regime for investment products offered to the public in Hong Kong under the SFO. We perform gate-keeping functions in authorising investment products and monitor compliance with disclosure and other requirements.

We require offering documents of retail investment products to be accurate and to provide adequate information for investors to make informed decisions.

Listings and takeovers

We oversee all listing and takeovers matters in Hong Kong, including vetting of listing applications, disclosure requirements for listed companies, corporate conduct and the listing-related functions of The Stock Exchange of Hong Kong Limited (SEHK).

Empowered by the Securities and Futures (Stock Market Listing) Rules and more generally under the SFO, we intervene in serious corporate cases at an early stage to carry out our statutory objectives. We may raise objections to listing applications or direct SEHK to suspend trading in a listed company's shares.

On a daily basis, we monitor company announcements to identify misconduct or irregularities. We facilitate the fair treatment of investors in corporate activities such as mergers, takeovers and share buy-backs.

Market infrastructure

We formulate policies to facilitate the development of market infrastructure and to build links with Mainland and international markets. We also collect quantitative information about the financial markets as a means to help reduce systemic risks.

We conduct day-to-day supervision and monitoring of exchanges and clearing houses, share registrars and authorised automated trading services providers.

Enforcement

Through our surveillance, investigative and disciplinary work, we combat misconduct and malpractice in the securities and futures markets. Where appropriate, we take action to remedy the effects of market misconduct by applying to the court for injunctive and remedial orders.

We work with other law enforcement agencies and overseas regulatory bodies on investigations where required.

Our major enforcement actions include criminal prosecution and market misconduct, civil and disciplinary proceedings.

Regulatory collaboration

To ensure our regulatory framework is aligned with global standards, we actively participate in the International Organization of Securities Commissions and other global rule-setting fora. We work closely with local and Mainland authorities to support Hong Kong's long-term strategic development amid the opening of Mainland financial markets.

Stakeholders

We maintain close communication with stakeholders to help them understand our work and the rationale behind it. When formulating policies, we consult the industry and the investing public through a variety of channels.

History and background

The securities and futures markets in Hong Kong were largely unregulated until 1974 when legislation was introduced to regulate the industry following a market crash the previous year. Under the legislation, regulation was conducted on a part-time basis by two separate commissions, one for securities and another for commodities trading.

Another major market crash in 1987 triggered the formation of the Securities Review Committee chaired by chartered accountant Ian Hay Davison. Its report, released in 1988, recommended the establishment of a single statutory body outside the civil service, headed and staffed by full-time professionals and funded primarily by the market.

It also proposed that this body be vested with broad investigative and disciplinary powers so it could properly carry out its regulatory functions.

In May 1989, the SFC was officially established as an independent statutory regulator. Further reviews to improve the regulatory regime were conducted after the 1997 Asian financial crisis. The SFO came into effect on 1 April 2003, consolidating and modernising the statutes previously regulating Hong Kong's securities and futures markets.

The SFC has been funded through fees and transaction levies since the early 1990s. It has not had any requirement for Government funding.

Corporate Governance

We strive to promote transparency, accountability and integrity. Sound corporate governance is essential to ensure we carry out our regulatory functions properly and effectively.

Governance framework

We are committed to maintaining an effective corporate governance framework comprising a well-defined management structure, high standards of conduct, comprehensive operational and financial control procedures and independent checks and balances. This framework is in line with best governance practices for public bodies including those set out in *Corporate Governance for Public Bodies – A Basic Framework*, published by the Hong Kong Institute of Certified Public Accountants.

Board

The SFC Board plays a key role in ensuring that we carry out our duties effectively by supervising and directing our work. It sets the SFC's overall direction, provides strategic guidance on policy making and oversees the work of the Executive Committee (ExCo).

Constitution

The Securities and Futures Ordinance (SFO) stipulates the constitution and proceedings of our Board. Members are appointed for a fixed term by the Chief Executive of the Hong Kong Special Administrative Region (HKSAR) or the Financial Secretary under delegated authority, and their appointment terms and conditions are determined by the HKSAR Government. Board members' emoluments for the year are detailed on page 113.

As of 31 March 2018, the Board comprised eight Non-Executive Directors (NEDs), including the Chairman; and six Executive Directors (EDs), including the Chief Executive Officer (CEO).

Coming from diverse backgrounds, NEDs bring to the Board a wide range of experience and expertise as well as a variety of independent perspectives.

See pages 16-23 for the full list of Board members and their biographies.

Key components of our governance framework



Chairman and CEO

The non-executive Chairman and the CEO are charged with separate and distinct roles and responsibilities.

Chairman

- Leading the Board in setting the SFC’s policies, strategy and overall direction
- Monitoring the executive team’s performance
- Counselling the CEO on how the organisation is run

CEO

- Assuming executive responsibility for day-to-day operations of the SFC
- Developing strategic objectives, including setting the SFC’s agenda and priorities, and implementing them as agreed with the Board

- Assigning responsibilities to senior management and supervising their work
- Reporting regularly to the Board

Executive Directors and Non-Executive Directors

Our EDs and NEDs play different but complementary roles. The EDs are responsible for the daily operations of the SFC and each has executive duties in key functions including listings and takeovers, corporate conduct, intermediaries, market infrastructure and operators, investment products and enforcement. The NEDs provide guidance on and monitor the performance of the organisation’s functions.

Corporate Governance

Governance practices

We strive to uphold high standards of corporate governance and establish clear and proper policies and processes to facilitate the working of an efficient and accountable Board through the following practices.

- Arrange for the Board to hold monthly meetings and quarterly policy meetings as well as special and off-site meetings.
- Provide Board members with relevant information before meetings to enable thorough consideration of agenda items.
- Circulate draft minutes of the Board meetings to members for comment.
- Furnish Board members with information regarding our operations and financial condition on a monthly basis.
- Keep the Board apprised of our policies and operations as appropriate.
- Require Board members to observe policies regarding conflicts of interest.

- Provide induction briefings as well as ongoing training on various topics to enable the NEDs to better understand the organisation and their responsibilities.

The Board regularly conducts a self-assessment exercise to improve its effectiveness. The exercise examines basic board responsibilities and assesses the performance of individual members. The findings, reported to the Board on an anonymous basis, are discussed by the Board.

The Commission Secretariat is tasked with ensuring good corporate governance. It supports the Board and senior management, assists them in dealing with organisation-wide policies and initiatives and facilitates Board proceedings according to relevant policies and procedures. It also liaises with Board members, organises their meetings and acts as the central contact point with the Government, the Legislative Council (LegCo) and its members, fellow regulators and other public bodies. The Commission Secretary serves as the secretary to the Board, ExCo and Advisory Committee.

Behind the scenes

The Commission Secretariat plays an essential but often invisible role in maintaining good corporate governance at the SFC.

As the bridge between the Board and the rest of the organisation, it ensures that the Board's decisions are effectively communicated to our staff for execution. The Board discusses strategic priorities, policy directions and other matters at its regular meetings and annual offsite retreat. Maintaining proper records of these discussions is an indispensable part of the Commission Secretariat's work.

Proper procedures are a prerequisite for effective governance, and another major duty of the Commission Secretariat is to serve as gatekeeper for our internal processes and ensure we operate within our remit as set out in the SFO. It handles complaints against the SFC or its staff and assists the Commission Secretary, who serves as the data privacy officer, in administering the SFC's data privacy policy.



It also follows up on our responses to the annual review reports of the Process Review Panel^a.

More broadly, the Commission Secretariat keeps an eye on emerging and sensitive issues, providing advice and proposing appropriate responses to the Chairman and the CEO. In managing our communications with the Government and LegCo, it is on the frontline of our efforts to align our priorities with the development of Hong Kong as a leading international financial centre.

^a See Committees, panels and tribunal on pages 170-178.

Board appointments

During the year, Mr Ashley Alder was re-appointed as the CEO for a three-year term with effect from 1 October 2017. Ms Julia Leung was re-appointed as ED of Intermediaries with an additional role of Deputy Chief Executive Officer for three years effective 2 March 2018.

Three NEDs were re-appointed for two-year terms: Mr Albert Au (from 26 May 2017), Ms Mary Ma and Mr Lester Huang (both from 15 November 2017).

Board meetings

Regular Board meetings are held at least monthly. In addition, the Board meets quarterly to conduct in-depth discussions of policy issues and also convenes special meetings as needed. An annual off-site meeting sets out strategic objectives and management priorities.

Last year, 16 Board meetings were held with an average attendance rate of 84%.

Meeting attendance record

Meetings attended/held	Board	Audit Committee	Budget Committee	Investment Committee	Remuneration Committee	Executive Committee
Chairman						
Carlson Tong	16/16	–	–	4/4	2/3	–
Executive Directors						
Ashley Alder	13/16	–	1/1	1/4	–	21/22
Thomas Atkinson	13/16	–	–	–	–	19/22
Christina Choi	14/16	–	–	–	–	20/22
Brian Ho	15/16	–	–	–	–	18/22
Julia Leung	15/16	–	1/1	–	–	20/22
Keith Lui	15/16	–	–	3/4	–	22/22
Non-Executive Directors						
Albert Au	11/16	2/2	1/1	3/4	2/3	–
Edward Cheng	13/16	–	–	–	2/3	–
Lester Huang	15/16	–	1/1	–	3/3	–
Teresa Ko	10/16	2/2	1/1	–	2/3	–
Mary Ma	13/16	2/2	1/1	4/4	3/3	–
Kelvin Wong	14/16	2/2	–	4/4	2/3	–
William Wong	12/16	2/2	–	–	3/3	–
Senior Director and Chief Counsel						
Andrew Wan	–	–	–	4/4	–	21/22
Andrew Young	–	–	–	–	–	19/22

Board members

Carlson TONG SBS, JP

Chairman



From 20 October 2012
Current appointment expires
on 19 October 2018

Other SFC-related positions

- Chairman: Investment Committee and Advisory Committee
- Member, Remuneration Committee
- Member: Nominations Committee and SFC (HKEC Listing) Appeals Committee
- Member, Process Review Panel for the Securities and Futures Commission

Current offices and public service

- Chairman, University Grants Committee
- Member, Financial Leaders Forum, the HKSAR Government
- Board Member, Airport Authority Hong Kong
- Member, Exchange Fund Advisory Committee, Hong Kong Monetary Authority
- Member, Banking Advisory Committee, Hong Kong Monetary Authority
- Member, Listing Nominating Committee, Hong Kong Exchanges and Clearing Limited
- Member, Independent Commission on Remuneration for Members of the Executive Council and the Legislature, and Officials under the Political Appointment System of the HKSAR

Past offices and public service

- Chairman, Hong Kong Sports Institute Limited (2012-2017)
- Chairman, English Schools Foundation (2011-2015)
- Chairman, Employees' Compensation Insurance Levies Management Board (2007-2013)
- KPMG: Chairman, KPMG China (2007-2011); Chairman, KPMG Asia Pacific and Member, KPMG Global Board (2009-2011)
- Main Board and Growth Enterprise Market Listing Committee, The Stock Exchange of Hong Kong Limited: Chairman (2006-2008), Member (2002-2006)

Ashley ALDER JP

Chief Executive Officer



From 1 October 2011
Current appointment expires
on 30 September 2020

Other SFC-related positions

- Chairman, Nominations Committee
- Member: Budget Committee and Investment Committee
- Member: Advisory Committee and SFC (HKEC Listing) Committee

Public service

- Board of International Organization of Securities Commissions: Chairman (since May 2016); Vice-Chairman (Dec 2015-May 2016)
- Member, Financial Leaders Forum, the HKSAR Government
- Council Member, Treasury Markets Association
- Vice President, The Hong Kong Institute of Bankers

Past SFC position

- Executive Director, Corporate Finance (2001-2004)

Past offices

- Herbert Smith: Partner and Head of Asia (2004-2011); Partner (1994-2001); Associate (1986-1994)

Notes: Except for the Chairman, CEO and Deputy CEO, other board members are listed in alphabetical order. The Nominations Committee nominates members of the Takeovers and Mergers Panel, the Takeovers Appeal Committee and the Disciplinary Chair Committee. See pages 170-178 for information about SFC external committees.

Julia LEUNG SBS

Deputy Chief Executive Officer and Executive Director, Intermediaries



From 2 March 2015
Current appointment expires on 1 March 2021

Other SFC-related positions

- Chairman, Academic and Accreditation Advisory Committee
- Chairman, Fintech Advisory Group
- Member, Budget Committee
- Member, Advisory Committee and SFC (HKEC Listing) Committee

Past offices and public service

- Julius Fellow, International Economics, Chatham House (2014)
- Under Secretary for Financial Services and the Treasury, the HKSAR Government (2008-2013)
- Executive Director, Hong Kong Monetary Authority (2000-2008)

Publication

- *The Tides of Capital* (London: OMFIF Press, 2015)

Thomas ATKINSON

Executive Director, Enforcement



From 3 May 2016
Current appointment expires on 2 May 2019

Other SFC-related positions

- Member: Securities Compensation Fund Committee, Investor Compensation Fund Committee and SFC (HKEC Listing) Committee

Past offices

- Director of Enforcement, Ontario Securities Commission (2009-2016)
- President and CEO, Market Regulation Services Inc. (2001-2007)
- Vice President, Regulation Services, Toronto Stock Exchange (1996-2001)
- Assistant Crown Attorney, Ontario Court of Justice (1993-1996)

Corporate Governance

Albert AU BBS

Non-Executive Director



From 26 May 2015
Current appointment expires
on 25 May 2019

Other SFC-related positions

- Chairman, Audit Committee
- Deputy Chairman, Budget Committee
- Member: Investment Committee and Remuneration Committee
- Member, SFC (HKEC Listing) Appeals Committee

Current offices and public service

- Special Advisor, BDO Limited
- Chairman, Professional Services Advisory Committee, Hong Kong Trade Development Council
- Café de Coral Holdings Limited: Independent Non-Executive Director and Chairman of Audit Committee
- Independent Non-Executive Director, Hong Kong International Theme Parks Limited
- Independent Non-Executive Director, AAC Technologies Holdings Inc.

Past public service

- Vice Chairman (2012-2018); Board Director & Hon. Treasury (2008-2012), Hong Kong Coalition of Professional Services Limited
- Corruption Prevention Advisory Committee, Independent Commission Against Corruption: Chairman (2012-2017) and Member (2007-2011)
- Member, Advisory Committee on Corruption, Independent Commission Against Corruption (2012-2017)
- Member, Hong Kong Housing Authority (2011-2017)
- Hong Kong Productivity Council: Council Member and Chairman of Audit Committee (2010-2015)
- Member, Air Transport Licensing Authority (2007-2013)
- Member, General Committee, Federation of Hong Kong Industries (2007-2013)
- President, Hong Kong Institute of Certified Public Accountants (2008)

Edward CHENG SBS, JP

Non-Executive Director



From 1 January 2017
Current appointment expires
on 31 December 2018

Other SFC-related positions

- Member, Remuneration Committee
- Member, SFC (HKEC Listing) Appeals Committee

Current offices and public service

- Deputy Chairman and Chief Executive, Wing Tai Properties Limited
- Chairman, Lanson Place Hospitality Management Limited
- Member, Chief Executive's Council of Advisers on Innovation and Strategic Development
- Independent Non-Executive Director, Orient Overseas (International) Limited
- Independent Non-Executive Director, Standard Chartered Bank (Hong Kong) Limited

Past SFC-related positions

- Member, Takeover and Mergers Panel (1994-2005) and Takeovers Appeal Committee (1994-2005)

Past public service

- Chairman, University Grants Committee (2011-2015)
- Chairman, Urban Renewal Authority (2004-2007)
- Member, Commission on Strategic Development (2013-2017)
- Board Member, Airport Authority Hong Kong (2011-2017)
- Council Member, Hong Kong Polytechnic University (2006-2009)
- Member, Operations Review Committee, Independent Commission Against Corruption (1997-2013)
- Member, Advisory Committee on Corruption, Independent Commission Against Corruption (2004-2009)
- Member, Steering Committee on Innovation and Technology (2004-2008)
- Member, Executive Committee, Hong Kong Housing Society (2000-2004)
- Council Member, Education University of Hong Kong (formerly known as The Hong Kong Institute of Education) (2000-2002)
- Council Member, City University of Hong Kong (2003-2007)
- Council Lay Member, Hong Kong Institute of Certified Public Accountants (2004-2005)

Christina CHOIExecutive Director,
Investment Products

From 1 August 2016
Current appointment expires
on 31 July 2019

Other SFC-related positions

- Chairman: Committee on Real Estate Investment Trusts and Products Advisory Committee
- Member: Advisory Committee and SFC (HKEC Listing) Committee

Public service

- Member, Financial Services Advisory Committee, Hong Kong Trade Development Council
- Member, Asian Financial Forum Steering Committee, Hong Kong Trade Development Council

Past SFC position

- Senior Director, Investment Products (2012-2016)

Past offices

- Partner, Clifford Chance (2001-2004)

Corporate Governance

Brian HO

Executive Director,
Corporate Finance



From 28 August 2006
Current appointment expires
on 27 August 2018

Other SFC-related positions

- Chairman, Public Shareholders Group
- Member: Committee on Real Estate Investment Trusts and Nominations Committee

Public service

- Member, Listing Nominating Committee, Hong Kong Exchanges and Clearing Limited

Past SFC position

- Senior Director, Corporate Finance (2000-2006)

Lester HUANG JP

Non-Executive Director



From 15 November 2015
Current appointment expires
on 14 November 2019

Other SFC-related positions

- Deputy Chairman, Remuneration Committee
- Member, Budget Committee
- Member, SFC (HKEC Listing) Appeals Committee

Current offices and public service

- P.C. Woo & Co: Managing Partner and Co-Chairman
- Member, Hospital Authority
- President, The Hong Kong Federation of Youth Groups
- Fellow, Hong Kong Institute of Directors
- Chairman, Council of the City University of Hong Kong
- Chairman, Standing Committee on Language Education and Research

Past public service

- Chairman, Board of Advisors of Radio Television Hong Kong (2010-2016)
- Non-Executive Director, Urban Renewal Authority Board (2013-2016)
- Director, The Hong Kong Mortgage Corporation Limited (2009-2016)
- President, The Law Society of Hong Kong (2007-2009)
- Member, Exchange Fund Advisory Committee, Hong Kong Monetary Authority (2010-2016)
- Member, Standing Committee on Judicial Salaries and Conditions of Service (2010-2015)

Teresa KO JP

Non-Executive Director



From 1 August 2012
Current appointment expires
on 31 July 2018

Other SFC-related positions

- Deputy Chairman, Takeovers and Mergers Panel
- Member: Audit Committee, Budget Committee and Remuneration Committee
- Member: Investor Compensation Fund Committee, Nominations Committee, Securities Compensation Fund Committee, SFC (HKEC Listing) Appeals Committee and Takeovers Appeal Committee
- Chairman, Investor Compensation Company Limited

Current offices and public service

- Freshfields Bruckhaus Deringer: China Chairman and Partner
- Chairman, Standing Committee on Disciplined Services Salaries and Conditions of Service
- Trustee, IFRS Foundation

Past public service

- Council Member, The Hong Kong University of Science and Technology (2013-2016)
- Member, Expert Advisory Committee for Mergers and Acquisitions, China Securities Regulatory Commission (2012-2016)
- Member, Exchange Fund Advisory Committee, Hong Kong Monetary Authority (2010-2016)
- Member, Standing Committee on Disciplined Services Salaries and Conditions of Services (2011-2013)
- Listing Committee, The Stock Exchange of Hong Kong Limited: Chairman (2009-2012); Deputy Chairman (2006-2009)
- Member, Standing Committee on Company Law Reform (2005-2011)
- Independent Director, Travel Industry Council of Hong Kong (2005-2010)

Keith LUI

Executive Director,
Supervision of Markets



From 28 August 2006
Current appointment expires
on 27 August 2018

Other SFC-related positions

- Chairman: Investor Compensation Fund Committee and Securities Compensation Fund Committee
- Member, Investment Committee
- Member: SFC (HKEC Listing) Committee
- Director, Investor Compensation Company Limited

Public service

- Member, Risk Management Committee, Hong Kong Exchanges and Clearing Limited

Past SFC positions

- Senior Director, Supervision of Markets (2004-2006)
- Senior Director, Corporate Affairs (2002-2004)
- Commission Secretary (2001-2004)

Mary MA

Non-Executive Director



From 15 November 2013
Current appointment expires
on 14 November 2019

Other SFC-related positions

- Chairman, Budget Committee
- Member: Audit Committee, Investment Committee and Remuneration Committee
- Member, SFC (HKEC Listing) Appeals Committee

Current offices

- Managing Partner, Boyu Capital
- Independent Non-Executive Director, Lenovo Group Limited
- Non-Executive Director: Unilever PLC and Unilever N.V.

Past offices and public service

- Non-Executive Director, Stelux Holdings International Limited (2012-2016)
- Non-Executive Director, Wumart Stores (2010-2014)
- Member, Listing Committee, The Stock Exchange of Hong Kong Limited (2009-2013)
- Independent Non-Executive Director, Standard Chartered Bank (Hong Kong) Limited (2004-2013)
- Non-Executive Director, Daphne International Holdings Limited (2009-2011)
- Partner, TPG Capital and Co-Chairman, TPG China (2007-2011)
- Director, Shenzhen Development Bank (2007-2010)
- Member, Dean's Council of the Kennedy School of Harvard University (2002-2007)
- Senior Vice President and Chief Financial Officer, Lenovo Group Limited (1990-2007)
- Director, Bureau of International Co-operation, Chinese Academy of Sciences (1978-1990)

Dr Kelvin WONG JP

Non-Executive Director



From 20 October 2012
Current appointment expires
on 19 October 2018

Other SFC-related positions

- Deputy Chairman: Audit Committee and Investment Committee
- Member, Remuneration Committee
- Member, SFC (HKEC Listing) Appeals Committee
- Chairman, Investor Education Centre

Current offices and public service

- COSCO SHIPPING Ports Limited: Executive Director and Deputy Managing Director
- Immediate Past Council Chairman, The Hong Kong Institute of Directors
- Member, Financial Reporting Council
- Member, Operations Review Committee, Independent Commission Against Corruption

Past offices and public service

- Council Chairman, The Hong Kong Institute of Directors (2009-2014)
- Convenor-cum-Member, Financial Reporting Review Panel (2013-2016)
- Member, Standing Committee on Company Law Reform (2010-2016)
- Member, Main Board and Growth Enterprise Market Listing Committee, The Stock Exchange of Hong Kong Limited (2007-2013)

Dr William WONG sc

Non-Executive Director



From 1 August 2014
Current appointment expires
on 31 July 2018

Other SFC-related positions

- Chairman, Remuneration Committee
- Member, Audit Committee
- Member: Nominations Committee and SFC (HKEC Listing) Appeals Committee

Current offices and public service

- Senior Counsel, Des Voeux Chambers
- Fellow, Chartered Institute of Arbitrators
- Deputy Chairman, Private Columbaria Appeal Board
- Deputy Chairman, Municipal Services Appeal Board
- Deputy Chairman, The Board of Review (Inland Revenue Ordinance)
- Panel Member, Insurance Appeals Tribunal
- Chairman, Hong Kong Bar Association Special Committee on Arbitration
- Chairman, Hong Kong Bar Association Special Committee on International Law
- Vice Chairman, Hong Kong Bar Association Special Committee on China Practice Development
- Vice Chairman, Hong Kong Bar Association Special Committee on Barristers Qualification Examination
- Member, Hong Kong Bar Association Special Committee on Greater China Affairs
- Trustee, Board of Trustees, United College, The Chinese University of Hong Kong
- Director, The Hong Kong Middle Temple Society

Past public service

- Member, Hong Kong Bar Association Special Committee on Solicitors' Rights of Audience (1998-2000)

Corporate Governance

SFC committees

Board committees

We have four board committees, each chaired by an NED and with a focus on clearly-defined areas of the SFC's operations. The presence and active participation of the NEDs provide an effective check and balance on the SFC's management decisions.

Committee	Membership	Responsibilities	Meetings
Audit Committee	Five NEDs	<ul style="list-style-type: none"> Reviews annual financial statements Recommends the appointment of external auditors Coordinates the scope of the external audit and reviews audit findings Examines management procedures to ensure effective financial and internal controls 	2
Budget Committee	Four NEDs and two EDs [^]	<ul style="list-style-type: none"> Examines and approves the parameters and bases used in the annual budget Conducts the mid-year budget review Reviews the annual budget and makes recommendations to the Board 	1
Investment Committee	Four NEDs, two EDs and a Senior Director [^]	<ul style="list-style-type: none"> Advises on the SFC's fund management policies, strategies and investment guidelines Recommends the appointment of investment managers and advisers and monitors their performance including compliance with the investment guidelines Advises on investment risk management and asset allocation and monitors the performance of investments 	4
Remuneration Committee	Eight NEDs	<ul style="list-style-type: none"> Reviews the structure and level of staff remuneration Reviews trends in remuneration packages and recommends adjustments Considers other matters as required, including recommendations to the Government on EDs' remuneration and re-appointment 	3

[^] In a non-voting capacity.

External committees

External committees are set up under the SFO and comprise a large number of members outside the organisation who reflect the diverse views of market participants. They play important roles in the governance of the SFC.

The Advisory Committee offers insight and advice on policy matters related to the performance of the SFC's functions. The majority of members are external representatives appointed by the Financial Secretary under authority delegated by the Chief Executive of the HKSAR. The Committee is headed by the Chairman and its members include the CEO and not more than two other EDs.

Each regulatory committee specialises in a specific area such as market supervision, investment products, shareholders' rights and interests, listings, takeovers and mergers, and the compensation fund. Appointed by the Board, members include NEDs, EDs, industry representatives and other stakeholders. There were 15 regulatory committees as at the end of March 2018.

See pages 170-178 for the external committees' responsibilities and membership lists.

Executive Committee

ExCo is the highest executive body within the organisation. It performs administrative, financial and management functions as delegated by the Board and ensures that the SFC functions effectively. ExCo is chaired by the CEO and includes all other EDs, the Chief Counsel, and the Chief Financial Officer and Senior Director of Corporate Affairs.

ExCo meets regularly to consider policy and operational proposals and funding requests from different divisions of the organisation. During the year, 22 ExCo meetings were held with an average attendance rate of 91%.

Standards of conduct

As a regulator, we require a high standard of integrity and conduct from our staff to promote and maintain public confidence. In addition to complying with relevant legal obligations, staff are required to adhere to our code of conduct which spells out our standards in detail and covers confidentiality, conflicts of interest, personal investments and acceptance of gifts and

hospitality. Each staff member is given a copy of the code. Failure to comply with the code may result in disciplinary action.

Accountability and transparency

Stringent policies and procedures are in place to ensure that we act with credibility, fairness and transparency.

Delegation of authority

We have a system of delegation of authority to clearly delineate the authority of the Board and different levels of the executive management. The Board delegates certain regulatory powers and functions to EDs, with power to sub-delegate to staff in their respective divisions, as permitted under the SFO, to facilitate the discharge of their duties in our daily operations.

Budgeting

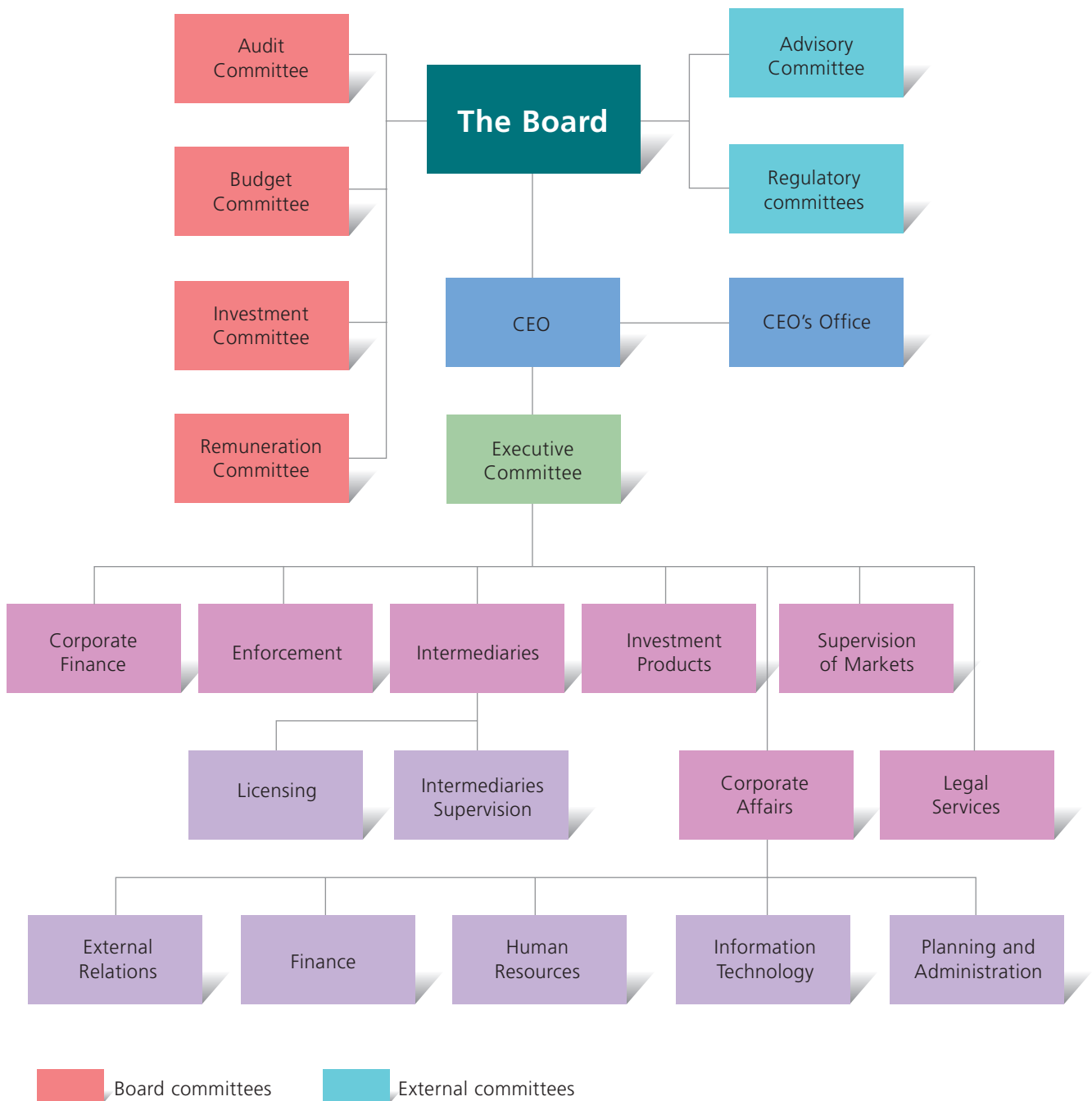
To maintain effective fiscal control and to plan for the coming year and beyond, we follow a disciplined approach in preparing our budget, which is based on a policy of tightly controlling expenditures. We make prudent assumptions, exercise robust financial control and identify areas where resources could be deployed to meet the SFC's strategic objectives, priorities and operational needs. Divisions' spending requests for the following year are critically assessed during the budget process. The annual budget, after consideration by the Budget Committee and approval by the Board, is submitted to the Financial Secretary for approval and then tabled before LegCo. We also appear before the LegCo's Panel on Financial Affairs to present our budget each year.

Investment

We aim to achieve long-term financial sustainability and attach great importance to the prudent management of our reserves, which are managed according to investment guidelines approved by the Financial Secretary. We have delegated responsibility for the selection, retention and management of the investments of our Reserve Fund and the Investor Compensation Fund to external investment managers. We regularly review their performance including their compliance with the investment guidelines. The external managers have confirmed that they adopt the Principles of Responsible Ownership¹ in their undertakings to manage these investments.

¹ Issued by the SFC in March 2016, these principles, which are voluntary, aim to provide guidance on how investors should fulfil their ownership responsibilities in relation to investments in Hong Kong listed companies.

Organisational structure



Note: CEO's Office includes four units, namely the Commission Secretariat, International Affairs, Mainland Affairs and Press Office.

Financial control and reporting

To help us uphold a high standard of integrity and exercise vigorous controls over the use of public funds, we engage an independent external firm to conduct an annual review of our financial control policies and procedures to ensure they are practical and robust.

We voluntarily observe applicable requirements stipulated in the Hong Kong Companies Ordinance when preparing our financial reports, and adopt the Hong Kong Financial Reporting Standards for preparing financial statements and disclosing financial information. We follow good market practice to ensure that our financial reports are transparent and informative.

Our practices include:

- Selecting relevant accounting policies and applying them consistently
- Appointing an external firm to conduct an interim review and annual audit
- Presenting our interim and annual financial statements to the Audit Committee for consideration
- Seeking the Board's approval of quarterly and annual financial statements and publishing them in our quarterly and annual reports
- Reporting key financial data to the Board and ExCo on a monthly basis
- Providing regular reports to the Government
- Attending meetings at LegCo, including meetings of the Panel on Financial Affairs, to explain policy initiatives and other issues of public interest

Handling complaints and grievances

We extend our principles of accountability and transparency to our complaints handling procedures. Reports of improper practices of the SFC or our staff

can be made under our procedures for handling complaints against the SFC or its employees. These cover dissatisfaction with the manner in which the SFC or our staff carried out or failed to carry out our duties. Detailed procedures for members of the public to lodge a complaint with us are available on our website.

Efficient use of resources

We regularly review our corporate resources and space requirements to ensure that we operate efficiently, identify our needs and strategic priorities, and allocate resources accordingly.

To formulate effective regulatory responses in the context of rapidly-evolving markets, we set up cross-divisional project teams to work on policies or initiatives related to the work of multiple divisions.

Stakeholder communication

We engage a wide range of stakeholders including the Government, LegCo members, the financial services industry, regulatory counterparts and the general investing public in a proactive, timely and effective manner².

We respond to public enquiries orally and in writing while striving to meet our performance pledges. We conduct public consultations and publish consultation conclusions before implementing a rule change. Annual and quarterly reports keep the public informed of our key regulatory work and finances. We issue industry-related publications, reports and surveys to address more specialised topics. Press releases announce our regulatory actions and other SFC news.

We also reach out to stakeholders to explain and clarify our policies and procedures and we discuss specific regulatory issues at seminars and other events.

We adopt an open approach to disclosing information subject to the secrecy provisions of the SFO. Our corporate website (www.sfc.hk) provides up-to-date, easily accessible public and industry information, which is constantly reviewed and enriched.

² See Stakeholder communication on pages 73-79.

Corporate Governance

We emphasise effective internal communication within the organisation. Besides utilising our intranet and internal circulars, we organise regular CEO Sharing Sessions and briefings by senior executives on the work of various divisions to keep our staff informed of the latest developments and current priorities.

In October 2017, a staff member from External Relations, Corporate Affairs received The Ombudsman's Awards 2017 for Officers of Public Organisations³.

Risks

In a dynamic market environment, it is paramount for us to timely and systematically identify, assess and manage external and internal risks to perform our regulatory functions effectively.

External risks

Our market contingency plan sets out measures for dealing with emergency situations which may affect Hong Kong's securities and futures markets. Rehearsing the plan on a regular basis helps us react promptly, appropriately and in a coordinated manner when a crisis arises.

A cross-divisional Risk Review Group was set up during the year to establish a structured process to monitor potential and emerging risks facing the SFC and gather market intelligence⁴. The group regularly reports to ExCo, and in turn to the Board.

Internal risks and control

We are subject to possible internal risks associated with our operations, including financial risks and threats to our information and office security. Internal control measures are in place to address these risks.

Our financial control policies and procedures define the scope and responsibility of the administrative, financial and management functions, including the appointment of consultants, fee collection, investments, expenditures

and budgeting. These policies and procedures are designed to ensure accountability and transparency and to conform to rigorous controls on the use of public funds. Periodically, we conduct a holistic review to ensure they are current, practical and robust.

In addition, an annual financial control review conducted by an independent external firm includes a risk-based review of our internal controls to assess our adherence to them and to evaluate and enhance their adequacy. The scope of each review is approved by the Audit Committee and the findings, together with recommendations, are submitted to ExCo for consideration and reported back to the Audit Committee. This year, the review covered specific areas including banking and investment procedures as well as information technology security, financial reporting and staff benefits, and led to subsequent revisions to related policies and procedures.

We put the following measures in place to provide for safe and smooth operations:

- A regularly updated business resumption plan addresses readily identifiable risks, including technical problems, fires, natural disasters and other emergencies. The scope of the plan covers office premises, communications and computer services.
- An information security policy provides guidance on how to protect the confidentiality and integrity of information. The policy is revised from time to time to keep up with technological and other changes in the way we operate.
- Access controls protect our information and systems from unauthorised access, use or modification.
- Office access controls safeguard against unauthorised entry to our premises.
- A data privacy policy to facilitate staff's compliance with the Personal Data (Privacy) Ordinance.

³ See Stakeholder communication on pages 73-79.

⁴ See Risk assessment on page 68.

Independent checks and balances

Independent bodies provide external checks and balances on our operational work to ensure fairness in our decision making, observance of due process and proper use of our regulatory powers. Apart from scrutiny by the Process Review Panel and the Securities and Futures Appeals Tribunal, we are subject to judicial review by the courts and indirect oversight by the Ombudsman.

Independent body	Relevant functions	SFC-related tasks handled
<p>Process Review Panel</p> <ul style="list-style-type: none"> An independent panel established by the Chief Executive of the HKSAR in 2000 Comprises representatives from various sectors and two ex-officio members, namely the SFC Chairman and a representative from the Department of Justice 	<ul style="list-style-type: none"> Reviews and advises on the adequacy of our internal procedures and operational guidelines, including those for the handling of complaints and licensing applications, inspection of intermediaries, product authorisation, corporate finance transactions and the exercise of investigation and disciplinary powers 	<ul style="list-style-type: none"> Reviewed 62 cases and published its annual report in October 2017
<p>Securities and Futures Appeals Tribunal</p> <ul style="list-style-type: none"> Chaired by current or former judges appointed by the Chief Executive of the HKSAR and comprising two other members drawn from a panel appointed by the Financial Secretary under delegated authority 	<ul style="list-style-type: none"> Reviews specified decisions made by the SFC Has power to confirm, vary or set aside decisions made by the SFC (and where a decision is set aside, substitute any other decision it considers appropriate) or refer the matter back to the SFC with directions 	<ul style="list-style-type: none"> Received requests to review four new cases Decided on one case brought forward from 2015-16 Allowed two cases received in 2017-18 to be withdrawn
<p>The Ombudsman</p>	<ul style="list-style-type: none"> Handles public complaints against the SFC and its staff for alleged maladministration 	<ul style="list-style-type: none"> Commenced eight preliminary inquiries
<p>Courts</p>	<ul style="list-style-type: none"> Handle judicial reviews of SFC decisions 	<ul style="list-style-type: none"> Handled seven judicial review cases

Performance pledges

In fulfilling our regulatory roles, we pledge to be responsive to the public, market participants and intermediaries under our supervision.

		Cases meeting the pledge		
		2017/18	2016/17	2015/16
Applications for subordinated loan or modification/waiver of requirements under SFO				
Commence review of application upon receipt	2 business days	100%	100%	95%
Authorisation of investment products¹				
Take-up of applications upon receipt	5 or 2 business days ²	100%	100%	100%
Preliminary response to applications after take-up for investment-linked assurance schemes (ILAS) and paper gold schemes	7 business days	100%	100%	100%
Preliminary response to applications after take-up for other products	14 business days	100%	100%	100%
Enquiries				
Preliminary replies	5 business days	100%	100%	100%
Processing of licensing applications³				
Corporations	15 weeks	100%	100%	100%
Representatives (provisional licences)	7 business days	100%	100%	100%
Representatives (normal licences)	8 weeks	100%	100%	100%
Representatives (responsible officers)	10 weeks	99% ⁴	100%	99%
Transfer of accreditation	7 business days	97% ⁴	97%	98%
Complaints against intermediaries and market activities				
Preliminary response	2 weeks	99.8% ⁵	99.7%	99.9%

¹ Different performance pledges were applicable before the implementation of the revamped fund authorisation process on 9 November 2015.

² The pledge of five business days is applicable to the following products:

- Unit trusts and mutual funds (including eligible Mainland funds seeking authorisation under the Mutual Recognition of Funds (MRF) arrangement between the Mainland and Hong Kong with effect from 9 May 2016)
- Mandatory provident fund products (including pooled investment funds)
- Pooled retirement funds

The pledge of two business days is applicable to other products including MRF funds (prior to 9 May 2016), ILAS, paper gold schemes and real estate investment trusts.

³ During the year, we processed 15,913 applications that were subject to performance pledges, 13,602 of which were processed within the applicable period. The completion of the vast majority of the remaining 2,311 applications was delayed for reasons beyond our control (eg, unresolved fitness and properness issues, outstanding vetting requests, applicants failing to provide essential information, requests by applicants that we delay finalising their applications). To more accurately reflect our performance, these applications are not included in the percentages stated.

⁴ The delay was usually short and resulted from unexpected complications, such as abnormal increases in our workflow and resulting resourcing difficulties.

⁵ Five cases failed to meet the pledge.

Since 2017, performance pledges for our work on takeovers and mergers matters are published on our corporate website. During the year, 99.9% of takeovers and mergers-related applications and transactions met the performance pledges. Details of the response time are listed in the following table.

Consultations and rulings under sections 6 and 8 of the Introduction to the Codes on Takeovers and Mergers and Share Buy-backs (Codes)	
<i>Applications for rulings and consultations with the Executive</i>	
– All ruling applications and consultations under the Codes (except for those set out below)	5 business days ⁶
– Applications for rulings that are conditional on obtaining shareholders' approval in a general meeting	Normally within 5 business days before the relevant general meeting
– Fast track EFM/EPT applications and EFM/EPT annual confirmations ⁷	10 business days
– All other EFM/EPT applications	21 business days
Comments and clearance of announcements and documents under Rule 12 of the Takeovers Code	
<i>First draft of firm intention announcement under Rule 3.5 of the Takeovers Code</i>	
– No complex Code issues involved	2 business days
– Complex Code issues involved	3 business days ⁸
<i>All other announcements (including revised drafts)</i>	
– No complex Code issues involved	1 business day
– Complex Code issues involved	3 business days ⁸
<i>All drafts of shareholders' documents⁹</i>	5 business days

⁶ If the subject matter involves complex Code issues, the time limit will be extended to 21 business days and the applicants will be informed of this.

⁷ EFMs and EPTs refer to exempt fund managers and exempt principal traders as defined under the Codes.

⁸ The parties will be informed of the longer time needed.

⁹ Including offer documents, offeree board circulars, whitewash circulars, scheme documents and share buy-back circulars.

Our People

As the markets we regulate become more complex, we increasingly rely on professional staff with specialised expertise in carrying out surveillance and investigations. Working in a more collaborative manner within the organisation also allows us to deliver faster and more responsive regulation.

Investigation specialists

To combat crime and misconduct in the securities and futures markets, our enforcement team depends on a staff of professionals from different backgrounds. Some previously served with other law enforcement agencies where they gained significant experience in investigatory work.

With pride and care

Working at the SFC after more than 30 years with the Hong Kong Police Force has been “an eye-opening experience,” related Armond Chan, former Chief Superintendent, Commercial Crime Bureau and SFC Director of Enforcement. In the past seven years with the SFC, Chan had to adjust to our different objectives and use of a wider spectrum of sanctions and remedies to take action against wrongdoers and protect investors. “SFC staff are highly self-motivated and they have more diverse backgrounds and expertise,” Chan said.

Ex-police staff like Chan have helped us better understand the police force’s procedures and working methods and this has improved cooperation.



Armond Chan

“As we handle increasingly complex cases, enhanced collaboration with other counterparts and law enforcement bodies is more important than ever,” Chan explained.

Under Chan’s experienced leadership, our field searches became larger in scale and more frequent, and he helped us substantially enhance our ability to investigate and take action against misconduct. More recently, he noted, the SFC’s new front-loaded regulatory approach has similarities to an intelligence-led policing strategy, which emphasises preventive measures and more effective collaboration.

All for integrity

A number of SFC staff formerly served with the Independent Commission Against Corruption (ICAC), the city’s agency committed to keeping Hong Kong fair and just. Joining the SFC, they quickly found that the skill sets the two agencies require are very similar, they related.

“Staff of both organisations come across a lot of sensitive and confidential information during investigations, so a high level of integrity is an essential requirement,” said Marky Wong, Senior Manager of Enforcement, who joined us from the ICAC. She emphasised that a clear and unbiased mind, personal commitment, impartiality and attention to detail are the main requirements for effective investigators.

Superior investigation skills are crucial for all law enforcement bodies, noted Raymond Tam, Manager of Enforcement, adding that white-collar crime investigations such as insider dealing and market manipulation can be more complicated than the ICAC cases he dealt with. “We have to handle our enforcement targets using a more tactful and gentle approach than what we used at the ICAC,” Tam reflected.

Jimmy Tong, Director of Enforcement, has no doubt that the investigative knowledge and skills he acquired as an ICAC investigator are highly relevant to his work at the SFC, and remain so even as rapid changes in the financial markets require regulators to adapt quickly to stay on top of emerging challenges. He stressed that investigations require team work at all times. “The work of investigators is like a football team – each person plays a role and collaborates with teammates to achieve a common goal.”

Multi-disciplinary cooperation

As part of our front-loaded, real-time approach to regulation, we established a cross-divisional working group designated ICE (Intermediaries, Corporates, Enforcement) to develop and implement an organisation-wide strategy to tackle listed company misconduct. Members include our Chief Executive Officer, the Executive Directors of our Intermediaries, Corporate Finance and Enforcement divisions, and other working-level staff.

Working collaboratively

For Anthony Wong, Senior Manager of Intermediaries and a member of the working group, drawing on expertise from across the organisation has helped make ICE a valuable force multiplier. "The combination of expertise and resources allows us to undertake larger and more focussed actions," he said. For instance, ICE recently conducted the SFC's largest-ever search operation which pulled together about 130 officers.

Gloria Kwok, Director of Enforcement, described the working group as a formalised platform for different parts of the SFC to coordinate their actions in response to issues in the market. "This helps increase efficiency and effectiveness and maximise the impact of our work," she explained.

“
Each investigator plays a role
and collaborates with teammates
to achieve a common goal.
”

Notable problems tackled by ICE included the price volatility of some stocks listed on GEM¹ and the increasing number of transactions by listed companies at apparently unreasonable prices. Our response combined enhanced supervision and investigations as well as communicating our expected standards of conduct in a public statement and guidelines for the industry.

Amanda Wong, Associate Director of Corporate Finance, said this clearly demonstrated that ICE's work is aligned with the "One SFC" approach. "Actions which have a bigger impact can more effectively convey clear messages to the industry about our concerns."

Teamwork is very important in this kind of multi-disciplinary endeavour, the members of the working group agreed. They work closely towards a common goal and that is the key to success.



Marky Wong, Jimmy Tong and Raymond Tam

¹ Formerly known as the Growth Enterprise Market.

Highlights

Key figures for 2017-18

8,461

requests for trading and account records

280

cases initiated for investigation

97

individuals and corporations subject to ongoing civil proceedings

\$483 million

in fines on licensees

8,294

new licence applications

301

risk-based on-site inspections of intermediaries

309

listing applications reviewed

401

takeovers-related transactions and applications

As of 31 March 2018:

2,799

authorised collective investment schemes including

758

Hong Kong-domiciled funds

44,358

licensees and registrants including

2,702

licensed corporations

83

industry circulars

112

Fintech-related enquiries

83

senior executives' speaking engagements

2,689

complaints against intermediaries and market activities

The following tables highlight our work during 2017-18. More details are provided in subsequent chapters.

Regulation	
Listing regulation	Issued conclusions jointly with The Stock Exchange of Hong Kong Limited (SEHK) to a consultation on proposed enhancements to SEHK's decision-making and governance structure for listing regulation
Senior management accountability	Fully implemented the Manager-In-Charge regime for licensed corporations on 16 October 2017
Online platforms	Concluded a consultation on proposed guidelines on the design and operation of online platforms and the application of the suitability requirement
Asset management	Concluded a consultation on proposed enhancements to asset management regulation and point-of-sale transparency
Public funds	Launched a consultation on proposed amendments to the Code on Unit Trusts and Mutual Funds which seek to ensure that regulations for public funds remain robust and aligned with international standards and market developments
Cybersecurity	Concluded a consultation on proposals to reduce and mitigate hacking risks in internet trading and issued guidelines on cybersecurity baseline requirements along with a circular on good industry practices
OTC derivatives	Concluded a consultation on the proposed regulatory capital regime for licensed corporations engaged in over-the-counter (OTC) derivatives activities
Position limits	The position limit regime for futures and options contracts took effect on 1 June 2017
Anti-money laundering	Introduced revised guidelines incorporating provisions in the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) (Amendment) Ordinance 2018

Listings, takeovers and corporate conduct	
Listing applications	Reviewed 309 listing applications received via SEHK
Takeovers matters	Supervised 401 takeovers-related transactions and applications
Listing Policy Panel	Signed an addendum to the Memorandum of Understanding Governing Listing Matters following which a new Listing Policy Panel was established
Belt and Road	Issued a statement on listing applications of infrastructure project companies
Corporate transaction valuations	Issued a guidance note on directors' duties regarding valuations in corporate transactions together with a statement on the liability of valuers and a circular to financial advisers
Industry guidance	The inaugural issue of the <i>SFC Regulatory Bulletin: Listed Corporations</i> provided guidance on the manner in which the SFC performs some of its functions under the Securities and Futures (Stock Market Listing) Rules

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Highlights

Intermediary licensing, conduct and practices	
Licensing	<p>The number of licensees and registrants in Hong Kong reached a record high of 44,358, of which 2,702 were licensed corporations</p> <p>Published a new <i>Licensing Handbook</i> and revamped the licensing section of the SFC website</p>
On-site inspections	Conducted 301 risk-based on-site inspections and noted over 1,400 incidents of breaches of the SFC's rules
Sandbox	Launched the SFC Regulatory Sandbox to provide a confined regulatory environment for qualified firms to operate regulated activities under the Securities and Futures Ordinance
Cryptocurrencies	Issued statements and circulars on the potential regulatory implications of fundraising using initial coin offerings or cryptocurrencies
Sponsors	Issued a report on deficiencies in sponsor work
Sale of in-house products	A joint circular with the Hong Kong Monetary Authority (HKMA) reminded firms about their expected standards for managing conflicts of interest arising from the sale of in-house products in the same financial group
Industry guidance	<p>The inaugural issue of the <i>SFC Compliance Bulletin: Intermediaries</i> provided guidance on the SFC's regulatory and supervisory priorities</p> <p>Issued 83 circulars to the industry covering a wide range of topics including best execution, client facilitation and anti-money laundering</p>



Markets and products	
Stock Connect	<p>Stock Connect now covers 1,500 Mainland stocks and 460 Hong Kong stocks, representing more than 80% of the two markets' combined market capitalisation</p> <p>The daily quotas under Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect were expanded fourfold to RMB52 billion for northbound trading and RMB42 billion for southbound trading, effective from 1 May 2018</p>
Funds	<p>The total number of authorised collective investment schemes rose to 2,799, of which 758 were Hong Kong-domiciled funds</p> <p>Formally adopted a revamped process for applications for the approval of post-authorisation changes and authorisation of revised offering documents for SFC-authorized funds</p>
Mutual recognition of funds	Signed a memorandum of understanding (MoU) with Autorité des Marchés Financiers on mutual recognition of funds, allowing eligible French and Hong Kong public funds to be distributed in the other market through a streamlined vetting process

Enforcement	
Surveillance	Made 8,461 requests for trading and account records from intermediaries as a result of surveillance of untoward price and turnover movements
Investigations	Completed 254 investigations and laid 54 criminal charges against 11 individuals and three corporations and secured convictions against nine persons and five corporations
Disciplinary actions	Disciplined 15 corporations, two responsible officers and 14 licensed representatives, resulting in total fines over \$483 million
Notable cases	Fined HSBC Private Bank (Suisse) SA a record sum of \$400 million for material systemic failures in the sale of structured products in the run-up to the global financial crisis in 2008
	Reprimanded and fined three companies of the Credit Suisse group a total of \$39.3 million over a series of internal control failures
	The Market Misconduct Tribunal (MMT), in its heaviest financial sanction to date, ordered Gu Chujun (former chairman and chief executive officer of Greencool Technology Holdings Limited) to disgorge approximately \$481 million of profit
	The MMT ruled that Mayer Holdings Limited and nine of its former directors and senior executives failed to disclose inside information as soon as reasonably practicable and fined them a total of \$10.2 million
Guidance on cooperation	Issued an updated Guidance Note on Cooperation with the SFC to highlight the benefits of cooperating in our investigations and enforcement proceedings

Stakeholder communication	
SFC Regulatory Forum 2018	<p>This year's Regulatory Forum, a full-day, biennial event to promote dialogue with a wide range of stakeholders, focussed on initiatives to enhance Hong Kong's competitiveness as a capital raising centre with around 900 participants from the financial industry, listed companies and regulatory and professional bodies in attendance</p> 
Financial technology (Fintech)	<p>Organised a full-day programme jointly with the HKMA to discuss regulatory issues related to Fintech development</p> <p>Held a forum for around 180 industry experts and representatives from licensed corporations to share their observations and good practices on algorithmic trading</p>
Industry publications	Published 15 thematic publications including the <i>Enforcement Reporter</i> , <i>Takeovers Bulletin</i> and two new bulletins

Highlights

Regulatory collaboration	
International	Hosted the second EU-Asia Pacific Forum on Financial Regulation in Hong Kong
Mainland China	Reached an agreement with the China Securities Regulatory Commission (CSRC) on the introduction of an investor identification regime for northbound trading under Stock Connect
Local	Conducted joint search operations with the Independent Commission Against Corruption to combine our enforcement powers and investigative tools
MoUs	Entered into an MoU with the Hong Kong Police to formalise and strengthen cooperation in combating financial crime
	Entered into MoUs with the CSRC on supervisory and enforcement cooperation on matters concerning futures and on personnel exchanges
	Entered into an MoU with the Financial Conduct Authority providing for consultation, cooperation and information exchange in the supervision of regulated entities which operate on a cross-border basis in Hong Kong and the UK
Fintech	Signed separate Fintech cooperation agreements with the financial regulators in the UK, Australia, Dubai, Malaysia and Switzerland



Operational Review

We endeavour to ensure stability, competitiveness and orderliness in the financial markets through our principal areas of work: intermediaries, investment products, listings and takeovers, market infrastructure and trading, and enforcement.

Intermediaries

We license qualified corporations and individuals to operate as intermediaries in our markets under the Securities and Futures Ordinance (SFO). As part of our ongoing supervision, we conduct on-site inspections and off-site monitoring of licensed corporations¹ and explain our regulatory focus and concerns to the industry. We closely monitor market and technological developments and adapt our approach accordingly.

Licensing

We received 8,294 new licence applications during the year, an increase of 6% from a year earlier. As of 31 March 2018, the number of licensees and registrants totalled 44,358, up 3% from last year, while the number of licensed corporations increased 9% to 2,702 in the same period. These were both record highs since the implementation of the regulatory regime under the SFO on 1 April 2003.

We extended the annual licence fee waiver for one year to 31 March 2019.

Regulatory enhancements

Senior management accountability

The Manager-In-Charge (MIC) regime for licensed corporations was fully implemented on 16 October 2017 following a six-month transition period (see sidebar on page 41).

Also on 16 October 2017, the Hong Kong Monetary Authority (HKMA) issued a circular requiring registered institutions to submit their up-to-date management structure information and organisational charts to both the HKMA and the SFC by April 2018.

¹ Broadly, licensed corporations include securities brokers, futures dealers, leveraged forex traders, fund managers, investment advisers, sponsors and credit rating agencies.

Intermediaries

Suitability obligations

To provide tailored guidance to the industry on the design and operation of online platforms and clarify how the suitability requirement would operate in an online environment, we concluded a public consultation in March 2018 on proposed guidelines for online distribution and advisory platforms. The guidelines will become effective in April 2019. We also launched a further consultation on requirements applicable to the offline sale of complex products.

In a January 2018 circular, we reminded intermediaries of their obligations to comply with the suitability requirement and in particular about the SFC's expected standards for product due diligence, measures to identify whether the suitability obligation has been triggered, assessments of suitability frameworks and the retention of compliance records.

Cybersecurity

To reduce and mitigate hacking risks associated with internet trading, we launched a two-month public consultation in May 2017. Subsequently, we held cybersecurity awareness workshops and presentations for licensed corporations including two workshops co-hosted with the Hong Kong Police and Hong Kong Computer Emergency Response Team Coordination Centre.

Upon concluding the consultation in October 2017, we issued guidelines on cybersecurity baseline requirements, including two-factor authentication for system login, along with a circular on good industry practices for cybersecurity and information technology risk management. The two-factor authentication requirement took effect on 27 April 2018 and other requirements will become effective on 27 July 2018.

Asset managers

Following the publication of consultation conclusions in November 2017, enhancements to asset management regulation in light of international developments will take effect in November 2018 and enhancements to point-of-sale transparency to better address conflicts of interest in the sale of investment products will become effective in August 2018. A further consultation on disclosure requirements applicable to discretionary accounts was concluded in May 2018.

In view of the growing number of firms licensed for asset management activities, we issued circulars in July and September 2017 to highlight irregularities and common instances of non-compliance in managing funds and discretionary accounts. Asset managers were reminded of the SFC's expected standards, including to perform their roles responsibly with due skill, care and diligence, in the best interests of their clients and the integrity of the market.

Licensees

	Corporations [^]		Representatives		Responsible Officers		Total [^]		
	As at 31.3.2018	As at 31.3.2017	As at 31.3.2018	As at 31.3.2017	As at 31.3.2018	As at 31.3.2017	As at 31.3.2018	As at 31.3.2017	Change
Stock exchange participants	563	512	12,096	11,068	2,043	1,830	14,702	13,410	9.6%
Futures exchange participants	115	112	884	921	188	196	1,187	1,229	-3.4%
Stock exchange and futures exchange participants	74	69	4,831	4,914	536	522	5,441	5,505	-1.2%
Non-stock/non-futures exchange participants	1,950	1,791	15,784	16,086	5,174	4,730	22,908	22,607	1.3%
Total	2,702	2,484	33,595	32,989	7,941	7,278	44,238	42,751	3.5%

[^] These figures exclude 120 registered institutions as at 31 March 2018 and 121 as at 31 March 2017.

MIC regime

The objective of the MIC regime is to heighten awareness of senior management accountability and enhance corporate governance. Under the regime, licensed firms are required to submit management structure information, including about MICs of eight core functions and organisational charts, in a standardised format. MICs of overall management oversight (OMO) and key business line (KBL) are

expected to be responsible officers (ROs) in respect of the regulated activities they oversee.

Since the launch of the MIC regime, many firms have taken concrete measures to enhance their governance structures, including strengthening the composition of their boards, clearly delineating the job responsibilities and reporting lines of individual senior managers and better aligning senior management accountability with the RO regime.

10,600
MICs

62%
of MICs are licensees

2,000
RO applications from
MICs of OMO or KBL

Note: Data as of 31 March 2018. Some MICs are not required to be licensed because they do not conduct regulated activities. They are primarily responsible for managing operations or control functions such as compliance, risk management, finance, information technology and anti-money laundering.

Over-the-counter derivatives

As part of comprehensive reforms to enhance Hong Kong's regulatory regime for over-the-counter (OTC) derivatives activities and to strengthen the management of conduct and financial risks in transactions and business dealings with related parties, we launched a public consultation in December 2017 on proposed refinements to the scope of regulated activities under the OTC derivatives regime. Other proposals related to licensing fees, insurance, competence and training requirements under the regime and, more broadly, requirements for licensed corporations to properly manage financial exposures to group affiliates and other connected persons.

Financial Resources Rules

In July 2017, we published consultation conclusions on the proposed regulatory capital regime for licensed corporations engaged in OTC derivatives activities and other changes to the Securities and Futures (Financial Resources) Rules (FRR). In parallel, we further consulted on a number of modified and additional proposals as well as draft FRR amendments which are not specific to OTC derivatives activities.

Financial resolution regime

The financial resolution regime under the Financial Institutions (Resolution) Ordinance, which came into operation on 7 July 2017, vests the SFC with powers to effect the orderly resolution of certain licensed corporations.

We worked with the HKMA, the Insurance Authority and the Financial Services and the Treasury Bureau on the 2017 Financial Stability Board Peer Review which examined the framework for the resolution of financial institutions in Hong Kong.

Anti-money laundering

In February 2018, we gazetted revised guidelines to incorporate provisions reflecting the amendments in the recently enacted Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) (Amendment) Ordinance 2018. A circular was issued on the same day to draw licensed corporations and affiliates' attention to the need to review their existing policies and procedures and ensure continued compliance. The revised guidelines came into effect in March 2018.

Intermediaries

Credit rating agencies

After assessing information provided by the SFC, the European Securities and Markets Authority announced in November 2017 that Hong Kong would retain its status as one of the equivalence jurisdictions for credit rating agencies (CRA) under the new requirements in the European Union (EU) CRA Regulation effective 1 June 2018. Accordingly, financial institutions in the EU may continue to use credit ratings prepared by SFC-licensed CRAs for regulatory purposes.

Monitoring compliance

We employ various tools, including on-site reviews and off-site monitoring, in supervising licensed corporations with a focus on their financial risks and how they conduct business.

On-site reviews

On-site reviews, which include prudential visits and routine, special and thematic inspections, are a key supervisory tool for understanding a firm's business operations, risk management and internal controls and gauging its compliance with legal and regulatory requirements. This includes assessing whether it acts with due skill, care and diligence and adopts proper business conduct, procedures and practices.

During the year, we conducted 301 risk-based on-site inspections, including thematic inspections on a range of issues. We enhanced our case management system and implemented a new risk assessment system to improve the efficiency of our inspections.



Ms Julia Leung, Deputy Chief Executive Officer and Executive Director of Intermediaries, speaks at an industry seminar

Off-site monitoring

We conduct off-site monitoring through regular interaction with licensed corporations to understand their business models and their plans to identify and assess risks. We assess the financial soundness of licensed corporations mainly through analysis of the regular financial returns they submit. We also utilise intelligence from a variety of sources and follow up on complaints and self-reported breaches. In addition, we examine applications by licensed corporations for subordinated loans and rule modifications or waivers. This helps us form a holistic view of the business profiles of licensed corporations.

Breaches noted during on-site inspections

	2017/18	2016/17	2015/16
Internal control weaknesses ^a	535	598	571
Breach of Code of Conduct ^b	320	441	388
Non-compliance with anti-money laundering guidelines	175	201	223
Failure to safekeep client money	59	62	45
Failure to safekeep client securities	38	58	41
Others	349	395	416
Total	1,476	1,755	1,684

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

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

Note: Also see Table 4 in Breakdown of SFC activity data on pages 163-169 for more details.

Statistical information and financial position of the Hong Kong securities industry

	As at 31.12.2017	As at 31.12.2016	As at 31.12.2015
Securities dealers and securities margin financiers	1,222	1,104	1,002
Active clients	1,657,931	1,556,695	1,501,816
Total assets (\$ million)	1,337,404	1,078,521	1,089,976

	12 months to 31.12.2017	12 months to 31.12.2016	12 months to 31.12.2015
Total value of transactions ^a (\$ million)	73,901,390	63,495,134	84,787,467
Total operating profit (\$ million)	23,539	14,131	26,404

^a The total value of transactions includes trading in equities, bonds and other securities in Hong Kong and overseas.

Note: Data were extracted from the monthly financial returns submitted under the Securities and Futures (Financial Resources) Rules by corporations licensed for dealing in securities or securities margin financing. Figures reported by an overseas-incorporated licensed corporation that carries out its principal business activities outside Hong Kong and operates in Hong Kong as a branch office were excluded. Also see Table 8 in Breakdown of SFC activity data on pages 163-169 for more details.

Industry guidance and communication

We stay on top of market developments and explain our supervisory focus to the industry through circulars, frequently-asked questions (FAQs) and other communications. Where necessary, we also publish reports to highlight deficiencies and good practices observed during our thematic inspections. We also met with various industry associations during the year.

Securities brokers

To examine the accuracy of brokers' records of client assets and balances, we engaged an independent accounting firm to conduct a circularisation exercise for selected client accounts. We notified the industry of the exercise in a July 2017 circular and will share key findings from the exercise after it is completed.

We also conducted a review to assess the adequacy of internal controls over the supervision of account executives by large- and medium-sized brokers mainly serving retail investors. Where appropriate, we will share our observations and provide further guidance to the industry on areas of concern.

Securities margin financing

In light of the volatility in small-cap stocks and some licensed corporations' excessive exposure to securities collateral which was highly concentrated and illiquid, we issued a circular in October 2017 to firms providing securities margin financing to remind them to vigilantly monitor risks and adopt prudent margin lending and risk management policies. We also communicated our concerns to the broker community through industry seminars and conferences.

Liquidity risk management

In December 2017, we issued a circular to provide additional guidance on establishing and maintaining prudential risk management practices for client money, liquidity and the concentration risks of funding sources within group affiliates.

Best execution

Further to the best execution rules laid down in the Code of Conduct², we issued a circular with a thematic report in January 2018 to provide more guidance to the industry on our expected standards of firms' conduct and internal controls in delivering best

² Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

Intermediaries



Ms Leung explains the SFC's policy initiatives in a radio interview

execution. The report highlighted observations from a thematic review and provided examples of good industry practices as well as those which did not meet our expected standards.

Client facilitation

Although we highlighted common deficiencies associated with client facilitation in a 2014 supervisory briefing, we identified a number of inconsistent practices in recent routine inspections. In light of this, we issued a circular in February 2018 to provide more guidance to the industry on our expected standards for firms' conduct and internal controls in this area.

Sponsors

Following a thematic inspection of sponsors, we issued a circular in March 2018 to remind licensed corporations carrying out sponsor work of the expected standards of conduct and due diligence practices and to urge them to critically review and enhance their internal systems and controls. The deficiencies we identified from the inspection were discussed in an accompanying report.

Prime services and equity derivatives

In October 2017, we commenced a thematic review of prime services and related equity derivatives business conducted by major investment banks in Hong Kong to obtain an overview of the industry landscape, business practices, key risks and the investment banks' controls and identify potential issues for future policy and supervision initiatives. We will share our observations with the industry.

Futures brokers

Following the publication of our *Report on the fact-finding exercise on retail futures brokers* in April 2017, we issued a circular to futures brokers in June 2017 setting out key areas of regulatory concern, including the assessment criteria for established clients under the rules of the Hong Kong Futures Exchange Limited and setting-off arrangements between a client's different trading accounts, along with expected standards of conduct and internal controls.

Cryptocurrencies

We issued a statement and a circular on initial coin offerings (ICOs) in September 2017 to make the industry aware of the potential regulatory implications of fundraising using cryptocurrencies or digital tokens in view of their growing popularity. In a December 2017 circular on cryptocurrency-related products and derivatives, we reminded cryptocurrency operators of the legal and regulatory requirements in Hong Kong.

In February 2018, we urged investors to be cautious about the associated risks as we took regulatory action against a number of cryptocurrency exchanges and issuers of ICOs. Subsequently, in March 2018, an issuer halted its ICO to the Hong Kong public and agreed to unwind ICO transactions for Hong Kong investors.

Conflicts of interest

In a November 2017 joint circular with the HKMA, we reminded intermediaries about our expected standards for managing conflicts of interest arising from the sale of in-house products in the same financial group. The circular also provided examples of good practices observed during joint thematic reviews of selected conglomerate financial groups.

Alternative liquidity pools

From 2016 to 2017, we undertook a thematic review of the operations of selected licensed corporations' alternative liquidity pools (ALPs) to assess whether they complied with the requirements in the Code of Conduct and to gather market information. In April 2018, we published a circular together with a report summarising the findings and good practices identified in the thematic review and providing an overview of the ALP landscape in Hong Kong.

SFC Compliance Bulletin

We launched the *SFC Compliance Bulletin: Intermediaries* to provide guidance to intermediaries and other market practitioners on the SFC's regulatory and supervisory priorities. The first issue, published in December 2017, highlighted the importance of managing conflicts of interest in selling practices and asset management and provided an overview of industry demographics.

Algorithmic trading

We held a forum in May 2017 for around 180 industry experts and representatives from licensed corporations to share their observations and good practices for algorithmic trading.

Anti-money laundering

We gave presentations to about 1,800 management and compliance practitioners on anti-money laundering and counter-terrorist financing at three SFC seminars and six others organised by industry associations.

Licensing Handbook

To provide easier access to licensing information, we published a new *Licensing Handbook* in April 2017 which consolidates information contained in various publications and FAQs. We also revamped the licensing section of the SFC website. Hyperlinks were included in the handbook and webpages for convenient cross-referencing of statutory provisions.

A framework for Fintech

Financial technology (Fintech) continues to evolve rapidly with the active participation of both start-ups and incumbent financial institutions. We closely monitor these developments with a focus on how they intersect with our rules and regulations. Through various forms of engagement, we keep track of the emergence of new business models which have implications for our regulatory work.

We are open to discussions with firms utilising innovative technologies who demonstrate a serious commitment to carry out regulated activities which may enhance investment choice and quality as well as benefit investors and the Hong Kong markets at large. Accordingly, we launched the SFC Regulatory Sandbox in September 2017 to provide a confined regulatory environment for qualified firms to operate regulated activities under the SFO before their technologies are applied on a full scale.

In September 2017, we issued a circular to clarify the "relevant industry experience" requirement for ROs of Fintech companies looking to be licensed.

We consider all relevant factors in assessing an RO application, including the firm's principal business model, governance structure and the competence of its key personnel. For instance, where the regulated activity carried out by a licensed corporation is based on the utilisation of a highly innovative technology, an RO applicant's direct experience with the technology may be essential for integrating the technology into the regulated activity.

In October 2017, we co-organised a full-day programme with the HKMA to discuss Fintech-related regulatory issues. The event was part of Hong Kong Fintech Week sponsored by InvestHK.

During the year, we worked with the Investor Education Centre to publish educational materials and also participated in public educational campaigns on risks associated with ICOs and cryptocurrencies.

To foster cross-border collaboration, we entered into Fintech cooperation agreements with the UK, Australia, Malaysia, Dubai and Switzerland.

Intermediaries

Investor compensation

We completed a study of ways to enhance Hong Kong's investor compensation regime and in April 2018 launched a public consultation on proposed enhancements for better investor protection.

The Investor Compensation Company Limited, a wholly-owned SFC subsidiary, received one claim against the Investor Compensation Fund and processed six claims during the year.

Investor compensation claims

	2017/18	2016/17	2015/16
Received	1	10	39
Processed	6	19	450
– Compensation payments made	3	14	413
– Rejected	3	4	19
– Withdrawn	0	1	4
– Reconsidered	0	0	14



Net asset value of compensation funds

	As at 31.3.2018 (\$ million)	Change	As at 31.3.2017 (\$ million)	Change	As at 31.3.2016 (\$ million)
Unified Exchange Compensation Fund ^a	75.8	4%	72.9	2.1%	71.4
Investor Compensation Fund ^b	2,361.2	3.5%	2,280.4	3.1%	2,210.9
Total	2,437	3.5%	2,353.3	3.1%	2,282.3

^a See pages 149-162 for the financial statements of the Unified Exchange Compensation Fund (UECF). The Investor Compensation Fund (ICF) was established by the SFO on 1 April 2003 to replace the UECF. After settlement of all claims against the UECF and its other liabilities, any remaining balance will be transferred to the ICF.

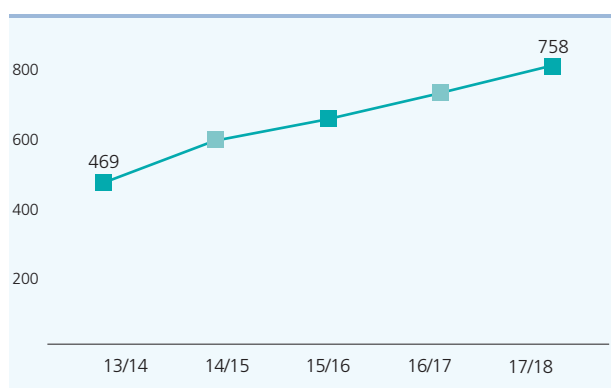
^b See pages 130-148 for the financial statements of the ICF.

Investment products

We authorise and regulate investment products offered to the public and monitor their ongoing compliance with regulatory requirements.

Our vision is to formulate policies which facilitate market growth and product innovation while supporting the development of Hong Kong as a leading asset management centre and preferred place of fund domicile.

Hong Kong-domiciled SFC-authorized funds



Facilitating market development Authorisations

As of 31 March 2018, a total of 2,799 SFC-authorized collective investment schemes (CIS) were on offer to the public. During the year, we authorised 134 CIS, comprising 120 unit trusts and mutual funds, one investment-linked assurance scheme (ILAS) and 13 mandatory provident fund (MPF) pooled investment funds.

We also authorised 114 unlisted structured investment products for public offering.

Authorised CIS

	As at 31.3.2018	As at 31.3.2017	As at 31.3.2016
Unit trusts and mutual funds	2,215	2,203	2,133
ILAS	299	300	301
Pooled retirement funds	34	34	34
MPF schemes	31	35	37
MPF pooled investment funds	194	182	173
Others	26 ^a	26	26
Total	2,799	2,780	2,704

^a Comprising 15 paper gold schemes and 11 real estate investment trusts (REIT).

Unlisted structured investment products

	2017/18	2016/17	2015/16
Unlisted structured investment products ^a	114	100	94
Authorisations granted under section 105 of the SFO ^b	84	84	85

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

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

ETFs and leveraged and inverse products

The total number of SFC-authorized exchange-traded funds (ETF) listed on The Stock Exchange of Hong Kong Limited stood at 134 (including 27 leveraged and inverse (L&I) products) as of 31 March 2018. In January 2018, we published a research paper on the Hong Kong ETF market and related topical issues in light of recent local and international developments. This paper is intended to provide context for future policy discussions.

Investment products

Renminbi products

We facilitate the development of renminbi products for offering to the public in Hong Kong. The total number of SFC-authorized unlisted funds and ETFs investing onshore in the Mainland securities markets¹ stood at 57 and 32 respectively as of 31 March 2018.

Mutual recognition of funds

France

In July 2017, we signed a Memorandum of Understanding (MoU) on mutual recognition of funds (MRF) with Autorité des Marchés Financiers. The MoU allows eligible French and Hong Kong public funds to be distributed in the other market through a streamlined vetting process. This opens up the opportunity for Hong Kong funds to be sold directly to retail investors in a leading European Union market.

To facilitate the implementation of this arrangement, we held an industry briefing in July 2017. We also issued a circular, frequently asked questions and an

information checklist to provide guidance on specific requirements and application procedures.

Switzerland

As of 31 March 2018, four SFC-authorized funds were approved by the Swiss Financial Market Supervisory Authority for distribution to retail investors in Switzerland under the Switzerland-Hong Kong MRF arrangement.

Mainland China

We granted authorisation for 50 Mainland funds under the Mainland-Hong Kong MRF scheme while the China Securities Regulatory Commission (CSRC) authorised 11 Hong Kong funds as of 31 March 2018.

ETF Connect

We work closely with the CSRC as well as stock exchanges and clearing houses in the Mainland and Hong Kong to study technical issues and proposals for implementing ETF Connect.

SFC-authorized renminbi investment products

	As at 31.3.2018
Unlisted products	
Unlisted funds investing onshore through RQFII, Stock Connect, Bond Connect and CIBM	57
Unlisted funds investing primarily in offshore dim sum bonds, fixed income securities and money market instruments	18
Paper gold schemes with renminbi features	1
Recognised Mainland funds under Mainland-Hong Kong Mutual Recognition of Funds	50
Unlisted structured investment products with renminbi features ^a	100
Listed products	
ETFs investing onshore through RQFII, Stock Connect, Bond Connect and CIBM	32
Renminbi gold ETFs ^b	1
Renminbi REITs	1

^a The number is on a "one product per key facts statement" basis.

^b Only includes gold ETF denominated in renminbi.

¹ These unlisted funds and ETFs are renminbi-denominated funds which primarily invest in Mainland securities markets through the Renminbi Qualified Foreign Institutional Investor (RQFII) quota, Stock Connect, Bond Connect and the China Interbank Bond Market (CIBM).

Revamped post-authorisation process

On 1 February 2018, we formally adopted the revamped process for applications for approval of post-authorisation changes (including scheme changes, termination, merger and withdrawal of authorisation) and authorisation of revised offering documents for SFC-authorized funds². The revamped process increases procedural transparency, enables timely notification of post-authorisation changes to investors and makes more efficient use of our resources.

Open-ended fund companies

In June 2017, we launched a public consultation on the Securities and Futures (Open-ended Fund Companies) Rules and the Code on Open-ended Fund Companies, which set out the detailed legal and regulatory requirements applicable to the new open-ended fund companies (OFC) structure. The OFC regime will broaden the choice of investment fund vehicles. Consultation conclusions were published in May 2018 and the regime will take effect following the completion of the legislative process.

New system for investment product information management

In 2017, we put in place a new Investment Product Management system to facilitate our product authorisation work, which involves processing large volumes of data and information. The system captures all case-related information for both product applications and post-authorisation matters, while simplifying and standardising processes and workflows.

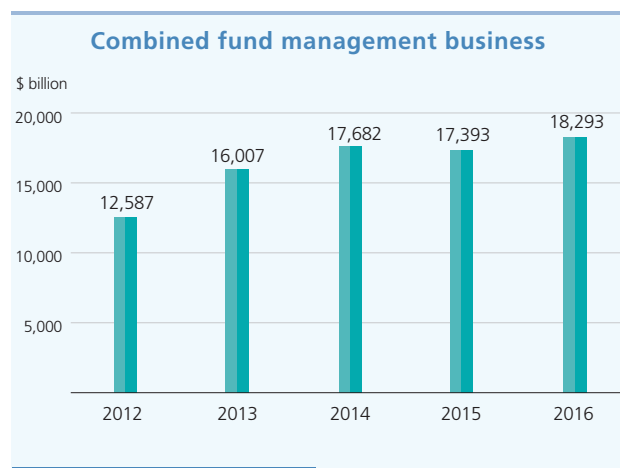
This helps us closely monitor performance pledges^a and data accuracy, greatly enhancing operational efficiency. Moreover, the new system is more fully integrated with our other systems, including the SFC Online Portal^b, allowing us to collect timely data from the industry for regulatory purposes and monitor market risks more effectively.

^a See performance pledges on page 30 for details.
^b The SFC Online Portal enables market participants to file documents, make submissions and pay fees to the SFC electronically.

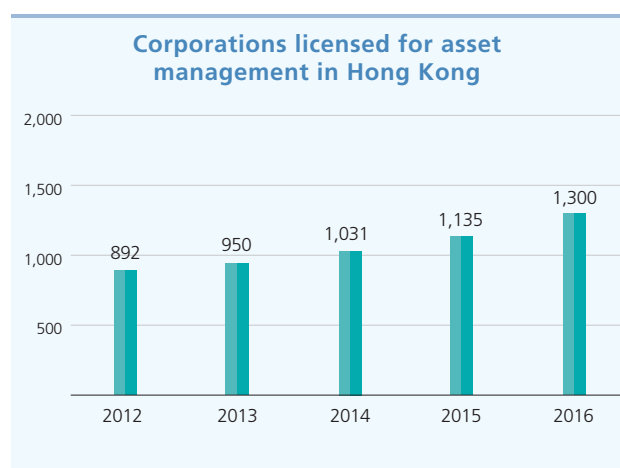
Fund management activities

We published the 18th annual Fund Management Activities Survey in July 2017. Hong Kong’s combined fund management business increased by 5.2% year-on-year to \$18,293 billion as of 31 December 2016, while private wealth management business grew by 9% to \$5,203 billion.

The number of corporations licensed for asset management in Hong Kong also increased by 14.5% in 2016, while the number of staff who engaged in activities other than sales and marketing increased by 3.7% year-on-year to 11,115 in 2016.



Source: Fund Management Activities Survey



² Excluding mandatory provident funds authorised only under the SFC Code on MPF Products.

Investment products



Ms Christina Choi, Executive Director, Investment Products speaks at the MPFA's Workshop on Governance of MPF Trustees

Enhanced regulation

Asset management

Following a public consultation concluded in November 2017, enhancements to asset management regulation proposed in light of international developments will come into effect in November 2018. In addition, enhancements to point-of-sale transparency to better address conflicts of interest in selling investment products, including by governing the use of the term "independent" by intermediaries, will become effective in August 2018. We also launched a further consultation on disclosure requirements applicable to discretionary accounts.

Online distribution and advisory platforms

In May 2017, we launched a three-month public consultation on proposed guidelines for online distribution and advisory platforms which provide tailored guidance to the industry on the design and operation of online platforms and clarify how the suitability requirement would operate in the online environment. We published consultation conclusions and launched a further consultation on proposed requirements applicable to offline sale of complex products in March 2018. The guidelines will become effective in April 2019.

Code on Unit Trusts and Mutual Funds

To update the regulatory regime for SFC-authorized funds, we launched a three-month public consultation in December 2017 on proposed amendments to the Code on Unit Trusts and Mutual Funds³ which seek to ensure that the regulations governing public funds remain robust and aligned with international standards and market developments. Key proposals include strengthening requirements for key operators, providing greater flexibility and enhanced safeguards for funds' investment activities and introducing new fund types, including active ETFs.

Surveillance and monitoring

As part of our ongoing surveillance and monitoring work, we closely monitor the liquidity of SFC-authorized funds through reports from their managers on any unusual or untoward activities, including significant redemptions, suspensions of dealing and liquidity problems. We regularly review abnormal fluctuations of the daily unit prices of Hong Kong-domiciled public funds as compared with their respective peer groups. We also monitor ETFs and L&I products through analysing data related to pricing, exposure to counterparties and, in the case of L&I products, daily rebalancing activities.

We regularly conduct surveillance of the marketing materials of SFC-authorized funds and fund managers' websites to ascertain whether they comply with regulatory requirements.

We also conduct routine surveillance of advertisements and handle complaints about property-related or other suspected arrangements which may be CIS. We raised around 40 enquiries about suspicious CIS during the year.

³ Consequential amendments were also proposed to the SFC Code on MPF Products, the Code on Pooled Retirement Funds and the Code on Investment-Linked Assurance Schemes.

Listings and takeovers

We oversee listing and takeovers matters in Hong Kong, including takeovers and merger activities, vetting of listing applications, disclosure requirements, corporate conduct and the listing-related functions of The Stock Exchange of Hong Kong Limited (SEHK). We review listing and takeovers policies to promote the development of a fair and orderly securities market in Hong Kong.

Listing policy

On 15 September 2017, the SFC and SEHK issued conclusions to their joint consultation on proposed enhancements to SEHK's decision-making and governance structure for listing regulation. The conclusions paper clarifies the role of the SFC as the statutory regulator which administers the Securities and Futures Ordinance (SFO) and the Securities and Futures (Stock Market Listing) Rules (SMLR), and

which supervises, monitors and regulates the activities carried on by SEHK. It also clarifies SEHK's role as the regulator administering the Listing Rules¹.

In March 2018, the SFC and SEHK signed an addendum to the Memorandum of Understanding Governing Listing Matters², following which a new Listing Policy Panel³ was established as an advisory, consultative and steering body to initiate and centralise discussions on listing policy with broader regulatory or market implications.

Given the high level of interest in infrastructure investment opportunities in developing markets, such as those related to the Mainland's "Belt and Road" initiative, we issued a statement in April 2017 setting out the factors we take into account when reviewing the listing applications of infrastructure project companies.

Explaining SMLR

Under our new, front-loaded regulatory approach, we engage in targeted intervention at an early stage to suppress illegal, dishonourable and improper market practices and protect the integrity of financial markets and the interests of investors. This new approach has increased our direct presence in more crucial listing matters which fall within the scope of the SMLR^a or the SFO.

Section 6(2) of the SMLR empowers us to raise objections to a listing of shares (including by listed companies). If it is likely that an objection would be raised, we will promptly issue a "letter of mindedness to object" (LOM)^b to the applicant setting out our substantive concerns, which we then discuss with the applicant and its advisers.

This is a departure from the SFC's previous approach where comments on initial public offering (IPO) applications were raised via SEHK. It is more efficient for an applicant to communicate directly with the SFC regarding our concerns.

^a SMLR is subsidiary legislation of the SFO.

^b An LOM sets out the substantive concerns of the SFC along with detailed reasons.

^c This decision is subject to review by the Securities and Futures Appeals Tribunal.

If the applicant's response to an LOM fails to address our concerns, we will issue a final decision notice to raise objections^c. Cases handled so far involve doubtful financial projections and false or misleading information related to suppliers. In one case, a listed company failed to address our concerns about a share placement to be conducted at a substantial discount to a small group of subscribers and had to cancel the placement.

Section 8 of the SMLR empowers the SFC to direct the suspension of trading in a listed company's shares. Unless urgent action is required by circumstances such as protecting investors, the SFC would normally first issue a "show cause letter" setting out its concerns and give the company an opportunity to respond.

In July 2017, we published the first issue of the *SFC Regulatory Bulletin: Listed Corporations*, providing guidance on our new regulatory approach.

¹ SEHK will be the primary front-line regulator and will remain the contact point for all listing applications save in respect of concerns raised by the SFC under the SMLR.

² The Memorandum of Understanding Governing Listing Matters was signed in January 2003.

³ The Listing Policy Panel consists of 12 members comprising senior representatives of the SFC, the Listing Committee, Hong Kong Exchanges and Clearing Limited (HKEX) and the Takeovers and Mergers Panel. It is not a committee under the SFC, HKEX or SEHK.

Listings and takeovers

We issued a guidance note in May 2017 on directors' duties regarding valuations in corporate transactions together with a statement on the liability of valuers for the disclosure of false or misleading information.

Jointly, the SFC and SEHK are conducting a holistic review of listing regulation which seeks to address issues relating to GEM⁴, capital raisings and the delisting framework under the Listing Rules.

SEHK issued a consultation paper on proposed changes to the regulation of GEM on 16 June 2017 and published consultation conclusions on 15 December 2017. The ensuing changes, which took effect on 15 February 2018, include:

- removing the streamlined process for GEM transfers to the Main Board;
- introducing a mandatory public offering requirement of at least 10% of the total offer size for all GEM initial public offerings (IPOs);
- increasing the minimum cash flow requirement for GEM applicants from \$20 million to \$30 million; and
- increasing the minimum market capitalisation of Main Board applicants at the time of listing from \$200 million to \$500 million.

In September 2017, SEHK launched a consultation which sought to address concerns about abusive fundraisings by some listed companies as well as a separate consultation on proposals to streamline the delisting procedures for suspended stocks.



Mr Brian Ho, Executive Director, Corporate Finance speaking at the Conference on Business Ethics for Listed Companies 2017

In response to market feedback to SEHK's June 2017 New Board Concept Paper, SEHK announced a proposal in December 2017 to expand the existing listing regime by allowing the listing on the Main Board of companies from emerging and innovative sectors. In February 2018, SEHK issued a consultation paper on proposals and draft rules to introduce a new listing regime for companies with weighted voting rights structures, biotechnology companies not meeting the financial eligibility tests under the current listing rules and overseas-listed companies seeking a secondary listing in Hong Kong. The new listing regime was implemented on 30 April 2018.

As of 3 July 2017, disclosure of interests notices must be submitted via Hong Kong Exchanges and Clearing Limited's new electronic filing system⁵. A three-month transition period was provided.

⁴ Formerly known as the Growth Enterprise Market.

⁵ The Disclosure of Interests Online System. This requirement follows the commencement of mandatory electronic filing provisions under Part XV of the SFO.

New listing applications

	2017/18	2016/17	2015/16
Total listing applications ^a	309	245	218
Cases lapsed/withdrawn/rejected during the year	27	38	26
Cases returned	3	5	3
New listings ^b	203	148	131

^a Including applications for transfer from GEM to the Main Board (2017/18: 22; 2016/17: 18; 2015/16: 12).

^b Including successful transfers from GEM to the Main Board (2017/18: 17; 2016/17: 6; 2015/16: 12).

IPO applications

We vet listing applications and raise enquiries on the basis of insufficient or inadequate disclosures, and object to a listing if it appears to us that it would not be in the interest of the investing public or in the public interest for the securities to be listed.

We received 309 listing applications via SEHK during the year, up 26% from 245 last year. We shared with SEHK our comments or concerns on 299 of them. Three listing applications were returned by SEHK, and an eight-week moratorium⁶ was imposed because the application proofs or related documents were not substantially complete.

To tackle serious disclosure and public interest issues, we issued seven LOMs to listing applicants directly during the year (see sidebar on page 51). Subsequently, we issued final decision notices to object to two of these applicants because their responses failed to address our concerns⁷. Of the other five, two were withdrawn, two lapsed⁸ and one was still being vetted at the end of the reporting period.

Corporate conduct

We monitor company announcements on a daily basis to identify corporate misconduct and irregularities in disclosures, including failure to disclose information in a timely manner and false or misleading disclosures. We also focus on transactions and corporate actions which are potentially detrimental to shareholders, paying particular attention to serious misbehaviour.

We use our information gathering power under section 179⁹ to raise enquiries with listed companies and, where our concerns are not addressed satisfactorily, intervene directly.

Takeovers matters

In Hong Kong, takeovers, mergers, privatisations and share buy-backs affecting public companies are regulated by the Codes on Takeovers and Mergers and Share Buy-backs, which aim to afford equal treatment of shareholders, to mandate disclosure of timely and adequate information to enable shareholders to make informed decisions as well as to ensure a fair and informed market.

⁶ The respective applicants can only submit a new listing application with a new application proof more than eight weeks after the return.

⁷ After our objection, one of these applicants resubmitted a listing application and was subsequently listed after addressing our concerns.

⁸ After a lapse, one applicant resubmitted a listing application and was subsequently listed after addressing our concerns.

⁹ Section 179 of the SFO gives the SFC the power to compel the production of records and documents from persons related to a listed company in relation to fraud or other misconduct.

Listings and takeovers

Takeovers and Mergers Panel rulings

The Takeovers and Mergers Panel met in April 2017 to consider the application by Television Broadcasts Limited (TVB) for a whitewash waiver in relation to a share buy-back offer it announced in January 2017. The panel ruled that full disclosure should be made of the shareholding and ownership structure of Young Lion Holdings Limited¹⁰. It also ruled on how the shareholders' resolution to approve the whitewash waiver should be voted¹¹.

In May 2017, TVB applied to the High Court of Hong Kong to commence a judicial review of the panel's April decision on how shareholder votes should be counted, which the High Court quashed following a September 2017 hearing. Other aspects of the panel's ruling, including full disclosure of Young Lion's shareholding and ownership structure, were not part of the judicial review and remain valid.

ICE

This year, the SFC cross-divisional unit designated ICE (Intermediaries, Corporates, Enforcement)^a recorded significant progress in tackling problems affecting the quality of our markets.

One major issue was the unusual price volatility in GEM stocks. The average first day price gain for GEM stocks which listed by way of placing was 743% in 2015 and 530% in 2016. Mobilising ICE, we issued two statements in January 2017 to remind listed companies and sponsors of their obligations to ensure compliance with the GEM Listing Rules, including that conditions exist for an open, orderly and informed market at the time of listing.

When we also exercised our powers under SMLR to object to GEM placings with a high concentration of shareholders, this had an immediate impact. Some companies delayed sub-standard listing plans and others changed their offerings to include a public offer tranche. In the year following the January statements, the average first-day price gain for GEM stocks was only 23%, and shareholding concentrations in newly-listed GEM companies were also lower.

Another longstanding problem was the use of unrealistic valuations to support suspicious asset disposals or acquisitions by listed companies. In May 2017, ICE coordinated the issuance of a

guidance note on directors' duties, a circular to financial advisers and a statement on the liability of valuers to remind them of their responsibility to uphold shareholders' interests when corporate assets are acquired or disposed.

In June 2017, ICE authorised one of the largest search operations in our history, pulling together over 100 staff to search multiple premises of interrelated companies. These companies comprised one of several groups working in coordination to extract value from unsuspecting investors by conducting apparently legitimate transactions which may not make any business sense beyond a very superficial level. The investigations were based on suspicions that market manipulation and financing transactions designed to defraud minority shareholders could be involved.

In March 2018, ICE issued a circular that identified continued deficiencies in sponsor work and urged licensed corporations to critically review and enhance their systems and controls to comply with the expected standards and the relevant codes, rules and regulations when carrying out sponsor work.

ICE allows us to deploy the full spectrum of our regulatory tools through tighter cross-divisional collaboration, whilst keeping a close watch on market developments to identify emerging problems and formulate strategies to address them proactively at an early stage.

^a The unit, which pools resources from the Intermediaries, Corporate Finance and Enforcement divisions, was established in 2016 in response to the increasing prevalence of regulatory issues relating to corporate behaviour and conduct.

¹⁰ Young Lion together with its concert parties holds 29.9% of TVB's shares and could hold up to 41.2% following the buy-back.

¹¹ The panel also ruled that TVB's whitewash waiver should be granted subject to a majority of votes cast in favour of a shareholders' resolution to approve the offer (without adjustment), and the whitewash waiver should not be put before TVB's shareholders for a separate vote.

Takeovers activities

Investigations and enquiries remained an important focus of our supervision and regulation of takeovers activities. We sanctioned a number of parties for breaching the Takeovers Code during the year:

- In August 2017, we publicly censured and imposed a 24-month cold shoulder order against Yeung Wing Yee for failing to making a general offer after acquiring over 30% of the shares in Union Asia Enterprise Holdings Limited, depriving the company's shareholders of the right to receive an offer.
- In the same month, we also publicly censured China Life Insurance (Overseas) Company Limited for breaching the dealing disclosure requirements during the privatisation of Glorious Property Holdings Limited.
- In September 2017, we publicly censured Chen Chi-Te and Kenneth C.M. Lo (both directors of Taiwan Cement Corporation) for breaching the dealing provisions during the company's proposed privatisation of TCC International Holdings Limited.
- In December 2017, Zhang Qiang was publicly censured for acquiring shares in Feishang Non-metal Materials Technology Limited within six months after the close of an offer at above the offer price.

Takeovers activities

	2017/18	2016/17	2015/16
General and partial offers under Code on Takeovers and Mergers	59	73	50
Privatisations	11	13	7
Whitewash waiver applications	41	37	51
Other applications under Code on Takeovers and Mergers [^]	289	365	323
Off-market and general offer share buy-backs	1	4	1
Other applications under Code on Share Buy-backs [^]	0	2	3
Total	401	494	435

[^] Including stand-alone applications and those made during the course of a Code-related transaction.
Note: Also see Table 3 in Breakdown of SFC activity data on pages 163-169 for more details.

- In March 2018, Nomura International (Hong Kong) Limited and Lee Yuen Yee, Annisa were publicly criticised for failure to comply with requirements for research reports and profit forecasts during a possible offer for West China Cement Limited.

Code amendments

We launched a three-month consultation on proposed amendments to the Codes on Takeovers and Mergers and Share Buy-backs in January 2018. Key proposals enhance investor protection by increasing the voting approval threshold for whitewash waivers to 75% of independent shareholders and empowering the Takeovers and Mergers Panel to require compensation to be paid to shareholders who have suffered as a result of a breach of the codes.

Other proposed amendments clarify the obligations of persons dealing with the Takeovers Executive¹², the Takeovers and Mergers Panel and the Takeovers Appeal Committee in all codes-related transactions, including their prompt cooperation and assistance and the provision of true, accurate and complete information.

We made changes to the Introduction to the Codes on Takeovers and Mergers and Share Buy-backs to introduce a new section 19.1 in July 2017 to align them with the newly effective Financial Institutions (Resolution) Ordinance as well as a new note to section 4.2 in April 2018 to bring them in line with the new listing regime for companies from emerging and innovative sectors.

¹² Refers to the Executive Director of the SFC's Corporate Finance Division or his delegate.

Market infrastructure and trading

To ensure orderly markets, we supervise and monitor exchanges and clearing houses in Hong Kong. During the year, we made progress on a number of initiatives to enhance the securities and futures markets.

Supervision of HKEX

On-site inspection

We conduct regular on-site inspections of the non-listing-related operations of Hong Kong Exchanges and Clearing Limited (HKEX). In August 2017, we conducted an inspection of its cash market clearing and settlement operations, focusing on the admission and monitoring of clearing participants as well as depository, custodian and nominee services.

Recognised clearing houses

During the year, we worked on risk management initiatives to improve the resilience of recognised clearing houses in Hong Kong and better comply with international standards published by the Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions. We worked with HKEX to enhance the clearing houses' recovery plans for managing extreme market situations and also approved measures to strengthen clearing guarantee funds, including risk-based contributions from the clearing houses and more timely collection of collateral from clearing members. In addition, we began to develop resolution plans for the clearing houses under the Financial Institutions (Resolution) Ordinance which came into effect on 7 July 2017.

Closing Auction Session

In July 2017, we approved HKEX's launch of Closing Auction Session (CAS) Phase 2¹ which expanded the list of securities to constituents of the Hang Seng Composite SmallCap Index and allowed regulated short-selling orders to be placed during CAS.

New products

We approved a number of derivative products proposed by HKEX to meet the trading and hedging needs of market participants (see table below).

Hong Kong as a risk management centre

As mainland China continues to open up and integrate with global capital markets, it is vital to enhance Hong Kong's role as the premier risk management centre for Mainland risk and a booking hub for Asian derivatives.

A-share futures

To enable Hong Kong to develop A-share index futures in due course, we entered into a memorandum of understanding (MoU) with the China Securities Regulatory Commission (CSRC) on 28 December 2017 which facilitates supervisory and enforcement cooperation in the Mainland and Hong Kong futures markets and enhances supervisory assistance and information exchange on cross-boundary derivatives, futures exchanges and futures brokers.

Derivative products approved

	Trading commencement date
Physically-settled gold futures contracts	10 July 2017
Cash-settled iron ore futures contract	13 November 2017

¹ CAS Phase 1 was launched in July 2016 to facilitate trade execution of major index constituents and all exchange-traded funds at closing prices.

OTC derivatives

In line with the Group of Twenty’s commitment to reform the over-the-counter (OTC) derivatives market, we have been working with the Hong Kong Monetary Authority (HKMA) to implement an OTC derivatives regulatory regime in Hong Kong in phases².

Phase 2 mandatory reporting of OTC derivatives transactions, covering all five major asset classes³, came into effect on 1 July 2017.

In response to market requests, we launched a joint HKMA-SFC consultation in April 2017 and implemented subsidiary legislation to adjust the scope of the term “OTC derivative product” under the Securities and Futures Ordinance (SFO). Engaging with market participants, we identified issues relating to the scope of regulated activities, on which we consulted the market in December 2017⁴, and are proposing refinements to address them.

In March 2018, we issued another joint HKMA-SFC consultation on enhancements to the OTC derivatives regulatory regime to mandate the use of Legal Entity Identifiers⁵ for the reporting obligation, expand the clearing obligation and adopt a trading determination process for introducing a platform trading obligation.

OTC Clear

For mandatory clearing purposes, we designated OTC Clearing Hong Kong Limited (OTC Clear) as a central counterparty for Hong Kong dollar basis swaps in June 2017. We also approved OTC Clear’s new products, including non-deliverable interest rate swaps in Asian currencies, cross-currency swaps for Hong Kong dollar vs US dollar and deliverable FX forwards and swaps.

Mutual market access

Stock Connect

We are in discussions with the Mainland authorities to further expand the scope of eligible securities under Stock Connect, which allows Hong Kong and Mainland investors to trade eligible stocks in each other’s markets.



Mr Keith Lui, Executive Director of Supervision of Markets, at the WFC Global Conference of Central Securities Depositories 2017

Stock Connect now covers some 1,500 Mainland stocks and 460 Hong Kong stocks, representing more than 80% of the two markets’ combined market capitalisation.

As of 31 March 2018, southbound trading from Shanghai and Shenzhen into Hong Kong reached a net inflow of RMB723.8 billion since the programme’s launch. Through northbound trading, international investors bought in RMB389.7 billion worth of A-shares as of that date.

The daily quotas were increased to RMB52 billion for each of the northbound trading links and RMB42 billion for each of the southbound trading links effective 1 May 2018.

Since inception, Stock Connect accounted for an increasing share of Hong Kong’s market turnover. On average, daily southbound trading reached 7% of total trading in Hong Kong from January to March 2018, compared to 6% in 2017 and 3% in 2016. Northbound trading also increased to 2% of the Mainland’s total market turnover, compared to 1% in 2017 and 0.3% in 2016.

² We implemented two phases of mandatory reporting—Phase 1 reporting came into effect on 10 July 2015 and Phase 2 on 1 July 2017. The first phase of mandatory clearing became effective on 1 September 2016.

³ Including interest rates, foreign exchange, credit, commodities and equities.

⁴ See Intermediaries on pages 39-46.

⁵ A unique 20-digit, alpha-numeric code which identifies entities in a financial transaction.

Market infrastructure and trading

Bond Connect

On 29 June 2017, we approved the automated trading services (ATS) application of Bond Connect Company Limited, a Hong Kong-based joint venture established by HKEX and the China Foreign Exchange Trade System & National Interbank Funding Center, to facilitate the operation of Bond Connect. Northbound trading under the scheme, launched on 3 July 2017, allows Hong Kong and overseas investors to invest in the China Interbank Bond Market. We are collaborating with other regulatory authorities to closely monitor the scheme's operations.

Market enhancements

Investor identification

We worked with HKEX and the Mainland exchanges and clearing house to develop an investor identification model for northbound trading under Stock Connect to facilitate market surveillance. To this end, we reached an agreement with the CSRC in November 2017 and announced the expected launch of the model in the third quarter of 2018⁶. We also agreed to develop a similar model for southbound trading after the northbound trading model is implemented.

Position limit regime

Following the conclusion of a public consultation in March 2017, the enhanced position limit regime for the futures market took effect on 1 June 2017. The regime expanded the scope of excess position limits which can be granted to qualified market participants. Amendments were made to the Securities and Futures (Contracts Limits and Reportable Positions) Rules as

well as the SFC's Guidance Note on Position Limits and Large Open Position Reporting Requirements. Since implementation, we have received more enquiries about and applications for excess position limits.

Automated trading services

Under the SFO, two regimes regulate ATS providers. Part III of the SFO authorises those offering facilities similar to those of a traditional exchange or clearing house and Part V licenses intermediaries providing dealing services with ATS as an added facility. During the year, trades conducted on authorised trading venues were mainly in commodity futures, benchmark index futures and options, bonds, equities and exchange-traded funds.

Over the past year, we approved 12 applications from overseas regulated exchanges and electronic trading facilities. The average daily trading volume of futures contracts originating from Hong Kong to authorised overseas exchanges was about 326,000 contracts for the 12 months ended 31 March 2018.

Short position reporting

In November 2017, we published a Short Position Reporting Service User Guide and frequently asked questions on our website. This followed the March 2017 expansion of short position reporting requirements to all securities which are permitted for short-selling under the rules of The Stock Exchange of Hong Kong Limited.

During the year, aggregated short positions for these securities accounted for 1.3% to 1.6% of the total market capitalisation of these securities.

ATS providers

	As at 31.3.2018	As at 31.3.2017	As at 31.3.2016
Under Part III	57	49	38
Under Part V	24	24	24

⁶ On 30 November 2017, HKEX issued an information paper, *Investor ID Model for Northbound Trading Under Stock Connect*, which sets out operational details of the regime.

Enforcement

Combating crime and misconduct in the securities and futures markets is crucial to maintain Hong Kong's status as an international financial centre. To send strong deterrent messages, protect investors and ensure fair and efficient markets, we focus on high-impact cases which pose the greatest risks to the investing public.

Our tools under the SFO

We use the full spectrum of sanctions and remedies available to us under the Securities and Futures Ordinance (SFO), including through criminal, administrative, compensatory and disciplinary actions.

We have broad powers to hold directors and individuals responsible for misconduct committed by the companies they manage. We can discipline licensed intermediaries through reprimands, fines¹ and suspensions or revocations of licences, and apply to the court for injunctive and remedial orders against wrongdoers in favour of victims.

Our work in figures

280
cases initiated

254
investigations completed

31
disciplinary
actions

8,461
requests for trading and account records[^]

54
criminal charges laid

22
cases with search
warrants executed

[^] These requests were made to intermediaries as a result of our surveillance of untoward price movements and turnover.
Note: Data as of 31 March 2018.

¹ Fines paid by intermediaries in disciplinary actions go into the general revenue of the Government.

Enforcement

To effectively communicate our enforcement priorities and new approach to the industry and stakeholders, we issued two issues of the *Enforcement Reporter* and spoke at public and private events and interviews.

We allocated resources to harder, more serious cases, reducing our overall caseload by setting aside or not taking up low-priority cases.

During the year, we commenced 280 investigations and laid 54 criminal charges against 11 individuals and three corporations and secured convictions against nine persons and five corporations.

We obtained disqualification and restorative orders against 28 persons and two corporations. Civil actions seeking financial redress and other remedial orders against 97 persons and corporations in 22 cases are pending before the court.

Disciplinary action was taken against 16 persons and 15 corporations. In addition, we commenced two cases before the MMT against two corporations and 11 persons for alleged late disclosure of inside information.

We also issued 277 compliance advice letters to address areas of regulatory concern and raise standards of conduct and compliance in the industry.

Market surveillance

On a daily basis, we monitor trading on The Stock Exchange of Hong Kong Limited and the Hong Kong Futures Exchange Limited and conduct preliminary inquiries to detect possible market manipulation or insider dealing. We also engage with firms to review how they perform their monitoring and surveillance.

During the year, we initiated an organisation-wide market surveillance intelligence project to collect and analyse data to identify market conduct risks².

Our surveillance of untoward price and turnover movements resulted in 8,461 requests for trading and account records from intermediaries. We also received and assessed 172 notifications from intermediaries³ regarding suspicious equity and derivative trading. The number of market surveillance cases rose 16% year-on-year.

30
disqualification and
restorative orders

\$483 million
in fines

97
individuals and corporations subject to
ongoing civil proceedings

23
high shareholding
concentration announcements

277
compliance advice
letters issued

² See Risk assessment on page 68.

³ Intermediaries are required to report clients' suspected market misconduct to the SFC under the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

We posted 23 announcements on our website reminding the investing public to exercise caution when trading in shares of listed companies where a small number of shareholders hold a high concentration of shares.

Enforcement actions

Corporate fraud and misbehaviour

Corporate conduct remains our top enforcement priority, especially when it relates to listed companies. Under our new approach, we engage in targeted intervention at an early stage to suppress illegal and improper market practices. We also increased our direct presence in more crucial listing matters which fall within the scope of the Securities and Futures (Stock Market Listing) Rules (SMLR) or the SFO⁴.

During the year, we suspended trading in the shares of 12 listed companies under section 8 of the SMLR for suspected misleading financial statements and corporate fraud and to protect investors from harm. We investigated 21 sponsor firms, and issued 13 notices of proposed disciplinary actions against eight firms and four sponsor principals. We are considering similar disciplinary notices and other enforcement actions against other firms and sponsor principals.

We conducted joint search operations with the Independent Commission Against Corruption in appropriate cases, efficiently using the enforcement powers and investigative tools of the two authorities to gather evidence of financial crimes.

We commenced legal proceedings under section 214 of the SFO in one case in the Court of First Instance (CFI) where we are seeking disqualification orders against Far East Holdings International Limited's former managing director and chief executive officer, Duncan Chiu, a former non-executive director and a former company secretary and financial controller for alleged misconduct towards the company and its shareholders.

We also commenced proceedings in the MMT alleging that Fujikon Industrial Holdings Limited failed to disclose inside information as soon as reasonably practicable and executive directors Yeung Chi Hung and Chow Lai Fung were reckless or negligent in causing the alleged breach.

Other notable cases during the year included:

- The MMT, in its heaviest financial sanction to date, ordered the former chairman and chief executive officer of Greencool Technology Holdings Limited, Gu Chujun, to disgorge approximately \$481 million of profit from grossly overstating financial statements over a five-year period. The MMT also made a cold shoulder order⁵ against Gu for five years as well as a cease and desist order to prohibit him from engaging in future market misconduct. He and four other former senior executives were also disqualified from serving as a director or being involved in the management of any listed company in Hong Kong for three to five years.
- The MMT ruled that Mayer Holdings Limited and nine of its former directors and senior executives failed to disclose inside information as soon as reasonably practicable and fined them a total of \$10.2 million. The MMT also imposed disqualification orders against the senior executives for periods ranging from 12 to 20 months and ordered the company to appoint an independent professional adviser to review its procedures for compliance with the corporate disclosure regime. The company and eight of the senior executives have filed appeals.
- The CFI disqualified the former chairman of Hanergy Thin Film Power Group Limited, Li Hejun, and four former independent non-executive directors of Hanergy from being a director for three to eight years for serious breaches of director's duties. It also ordered Li to procure the payment of outstanding receivables due to Hanergy from its parent company and affiliates.
- For materially overstating its turnover and understating its bank borrowings in its initial public offering (IPO) prospectus or subsequent results announcements, the CFI ordered Qunxing Paper Holdings Company Limited, its former chairman and vice-chairman Zhu Yu Guo and his son, Zhu Mo Qun, as well as a subsidiary, to compensate investors who subscribed for shares in its IPO or purchased them in the secondary market between 2007 and 2011. The CFI also ordered that payments be made to a corporate investor, which subscribed for its unlisted warrants in 2011.

⁴ See Listings and takeovers on pages 51-55.

⁵ An order which prohibits a person from dealing directly or indirectly in Hong Kong's financial markets.

Enforcement



Mr Thomas Atkinson, Executive Director, Enforcement, addresses the Pan Asian Regulatory Summit 2017

- The CFI ordered Tong Shek Lun, former chairman and director of Starlight Culture Entertainment Group Limited, Ko Lai King Kinny and Chung Wai Yu Regina, two other former executive directors, to pay compensation of around US\$890,000 for their misconduct relating to a disposal of subsidiaries by Starlight in September 2008, and disqualified them for five to seven years.

Insider dealing and market manipulation

Key enforcement actions included:

- The CFI, by consent, ordered Sun Min to pay over \$15.6 million to 51 investors affected by her insider dealing in the shares of China Huiyuan Juice Group Limited.
- The CFI, by consent, ordered Augustine Cheong Kai Tjeh, a former senior executive of an affiliate of Titan Petrochemicals Group Limited, and his mother Gan Ser Soon, to pay investors for their insider dealing in the shares of Titan in 2012.
- The Court of Appeal (CA) upheld the decision of the CFI which ruled in favour of the SFC's insider dealing and fraud case against two solicitors, Betty Young Bik Fung and Eric Lee Kwok Wa, and Lee's two sisters. In March 2018, the CA granted leave to Lee and his two sisters for taking their case to the Court of Final Appeal (CFA) in relation to the interpretation of section 300 of the SFO arising from fraudulent or deceptive transactions involving foreign securities.

- The CA dismissed our leave application to appeal to the CFA against the MMT's findings that Yiu Hoi Ying and Marian Wong Nam, two former executives of Asia Telemedia Limited, had not engaged in insider dealing. In February 2018, our leave application was granted by the CFA on the basis that the questions we raised are of great general or public importance.
- We commenced criminal proceedings against Au-Yeung Siu Pang for alleged insider dealing in the shares of China CBM Group Company Limited by selling, and counselling or procuring another person to sell China CBM shares in March 2012.
- We issued restriction notices to four securities firms relating to suspected market manipulation by their clients. The SFC was not investigating these brokers, which cooperated with our investigation.
 - Caitong International Securities Co., Limited, Pacific Foundation Securities Limited and Yuanta Securities (Hong Kong) Company Limited were prohibited from dealing with or processing assets held in client accounts which are related to suspected market manipulation in the shares of GME Group Holdings Limited.
 - Interactive Brokers Hong Kong Limited was prohibited from dealing with or processing assets held in a client account which is related to suspected insider dealing in the shares of Bloomage BioTechnology Corporation Limited.

Intermediary misconduct

During the year, we disciplined 15 corporations, two responsible officers and 14 licensed representatives, resulting in total fines of \$483 million. Key disciplinary actions included:

- HSBC Private Bank (Suisse) SA was fined a record sum of \$400 million after the Securities and Futures Appeals Tribunal (SFAT) upheld our disciplinary action against the bank for material systemic failures in the sale of structured products in the run-up to the global financial crisis in 2008 (see sidebar on page 63).

Record fine for failures in selling structured products

In November 2017, the SFAT upheld our findings and fined HSBC Private Bank (Suisse) SA^a \$400 million for material systemic failings in the sale of Lehman Brothers-related structured notes (LB-Notes) and leveraged forward accumulators which caused substantial losses to clients. The bank was also suspended from advising on securities for one year and partially suspended from dealing in securities.

While investigating over 80 investor complaints^b, we found material systemic deficiencies in the bank's sale of these products. The bank was aware of Lehman Brothers' deteriorating financial condition and had materially reduced its own exposure. Nevertheless, it continued to sell LB-Notes up to two weeks before Lehman Brothers' September 2008 collapse without disclosing the identity of the issuer or providing warnings to clients about the increasing credit risk during the sales process.

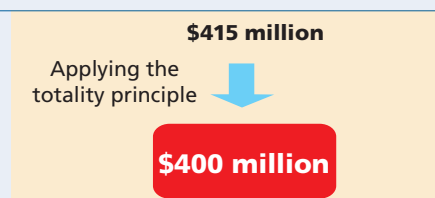
Although the bank assigned LB-Notes the riskiest rating, it allowed clients categorised with low or medium risk tolerance levels to purchase them without keeping proper records of the justifications for allowing these transactions. It also failed to implement adequate systems and controls to prevent clients from being overly exposed to accumulators.

The SFAT's determination confirms our approach in imposing a fine for each area of culpable conduct and using the number of complaints as the multiplier in assessing the appropriate fine^c (see the diagram below). The record fine is a stern warning for regulated persons to adhere to principles of professional conduct.

Our standards are designed to protect all investors including clients of retail or private banks. We will take action when breaches of the standards occur and substantial sanctions may result.

Calculating the fine

Nature of misconduct	Fine for each act of misconduct		Number of affected complainants		Total
LB-Notes: Failures to inform clients of issuer risk	\$5 million	X	15	=	\$75 million
LB-Notes: Suitability failures	\$5 million	X	55	=	\$275 million
Leveraged forward accumulators: Suitability failures	\$5 million	X	13	=	\$65 million



^a HSBC Private Bank (Suisse) SA is a registered institution under the SFO to carry on business in Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities.
^b Referred by the Hong Kong Monetary Authority.
^c Using the number of complaints as the multiplier may not be appropriate in every case. The appropriate approach in each case will depend on its facts.

Enforcement

- We reprimanded and fined Guoyuan Securities Brokerage (Hong Kong) Limited \$4.5 million for failing to conduct proper enquiries to mitigate the risks of money laundering and terrorist financing when processing third-party fund transfers for clients.
- UBS Securities Asia Limited was reprimanded and fined \$4.5 million for failing to put in place effective controls to record transactions and client consents for its facilitation trading activities.
- Promising Securities Company Limited was reprimanded and fined \$3.5 million for allowing unlicensed staff to perform regulated functions and failing to ensure the effective segregation of sales and settlement, giving the settlement staff an opportunity to misappropriate client assets.
- We reprimanded and fined iSTAR International Futures Co. Limited⁶ \$3 million for failing to comply with anti-money laundering and counter-terrorist financing requirements when processing third-party fund transfers, while Wu Biwei, its former responsible officer and managing director, was suspended for six months.
- The CFA granted leave to Moody's Investors Service Hong Kong Limited to appeal in the matter of our disciplinary action in relation to its special comment report published in 2011.
- CLSA Limited was reprimanded and fined \$9 million for its internal control failures in its client facilitation services and its reporting obligations⁷. In making the determination, we took into account that CLSA undertook a review with the SFC to address our regulatory concerns and cooperated in resolving them, and that CLSA's board of directors pledged to take reasonable steps to rectify its internal control failures in relation to avoidance of conflicts of interest.
- Deutsche Bank AKTIENGESELLSCHAFT and its wholly-owned subsidiary Deutsche Securities Asia Limited were reprimanded and fined a total of \$8.3 million over their regulatory breaches related to short position reporting, unlicensed regulated activities and segregation of client monies. In making the determination, we considered the two companies' cooperation and remedial measures to strengthen internal controls and systems.
- We reprimanded and fined Interactive Brokers Hong Kong Limited \$4.5 million for failures related to its electronic and algorithmic trading systems. In making the determination, we considered the firm's cooperation and that it agreed to arrange an independent review of these systems.

We also secured convictions for breaches of the SFO by two corporations:

In four cases, we took disciplinary action against the following corporations after resolving our concerns with them:

- Credit Suisse (Hong Kong) Limited, Credit Suisse Securities (Hong Kong) Limited and Credit Suisse AG were reprimanded and fined a total of \$39.3 million over a series of internal control failures, including in segregating client securities and in ensuring product suitability. In making the determination, we considered Credit Suisse's agreement to engage an independent reviewer to investigate our regulatory concerns and review their internal controls, as well as their cooperation.
- ETRADE Securities (Hong Kong) Limited was convicted of actively marketing to the Hong Kong public US brokerage services provided by E*TRADE Securities LLC, which was not licensed by the SFC. This was the first criminal conviction secured by the SFC against a firm for marketing unlicensed activities carried out outside Hong Kong.
- QMIS Securities Limited and its former responsible officer, Huang Kuang Cheng, were convicted and fined for making false or misleading representations when submitting licensing information to the SFC.

⁶ Now known as Rifa Futures Limited.

⁷ Intermediaries are required to report to the SFC immediately about any suspected or actual material breach of any applicable legal and regulatory requirements by themselves or persons they employ or appoint to conduct business with clients under the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

Other disciplinary actions

Unauthorised trading

Company/Name	Conduct	Action	Date
Danny Fung Kwong Shing	Conducted 772 unauthorised transactions in his client's account and fabricated telephone order recordings to mislead his employer	Fined \$542,071 and banned from re-entering the industry for life	23.11.2017
Shum Kam Ming	Conducted unauthorised transactions in a client's account and provided false account statements	Banned from re-entering the industry for life	25.9.2017
Yeung Leung Yuen	Conducted unauthorised transactions in a client's account	Banned from re-entering the industry for three years	7.11.2017
Tsap Wai Ping	Caused invitations to subscribe for shares in the US to be issued to the investing public without authorisation from the SFC	Banned from re-entering the industry for two years	19.5.2017

Criminal conviction

Company/Name	Conduct	Action	Date
Daniel Chen Chi Lik	Convicted of theft	Banned from re-entering the industry for life	20.4.2017

Internal control failures

Company/Name	Conduct	Action	Date
Standard Chartered Securities (Hong Kong) Limited	Internal control failures related to short-selling orders and regulatory breaches	Reprimanded and fined \$2.6 million	18.12.2017
EFG Bank AG	Failure to ensure compliance with regulatory requirements when dealing in futures contracts	Reprimanded and fined \$2 million	11.1.2018

Enforcement

Regulatory breaches

Company/Name	Conduct	Action	Date
FXCM Asia Limited ^a	Failure related to under-segregation of client money and regulatory breaches	Reprimanded and fined \$2 million	13.12.2017
Yip Ka Ying, Abbie	Attempted to conceal a trade execution error and trading loss from her employer	Banned from re-entering the industry for 18 months	13.12.2017

^a Now known as Rakuten Securities Hong Kong Limited.

Note: See Table 6 in Breakdown of SFC activity data on pages 163-169 for details of the less significant disciplinary actions.

Enhanced cooperation

We are actively developing a long-term strategic relationship with the China Securities Regulatory Commission (CSRC) to ensure effective enforcement collaboration in surveillance and joint investigations. During the year, we held regular high-level meetings, organised a staff secondment programme and hosted a CSRC-SFC joint training workshop in Xiamen. In December 2017, we entered into a memorandum of understanding (MoU) on supervisory and enforcement cooperation concerning futures, which enhances supervisory assistance, enforcement cooperation and information exchange relating to cross-boundary derivatives as well as futures exchanges and brokers.

Locally, we signed an MoU with the Hong Kong Police in August 2017 to formalise and strengthen cooperation in combating financial crime. We also closely collaborated with the Hong Kong Monetary Authority to investigate authorised institutions' misconduct under the SFO and with the Department of Justice on securities fraud, insider dealing, market manipulation and other offences.

In December 2017, we issued an updated Guidance Note on Cooperation with the SFC to highlight the benefits of cooperating in our investigations and enforcement proceedings. New measures encourage cooperation which helps the SFC investigate more serious legal or regulatory breaches and achieve timely and desirable enforcement outcomes. At the same time, we updated our Disciplinary Proceedings at a Glance guide.

New system to manage large volume of documents

Enforcement cases have become more complex and many now involve significant quantities of data and documents.

In early 2017, we enhanced our litigation support system to provide a centralised platform to manage data and documents for investigation and litigation purposes across the entire organisation.

The system enables us to search, review and analyse a large amount of litigation-related data more easily and to prepare exhibits for court proceedings more efficiently.

In addition, more users from different divisions can now readily access and review information in the system on an as-needed basis, facilitating cross-divisional cooperation.

Since its launch, more than 600 cases were handled using the enhanced system and over seven million documents were uploaded.

Enforcement activities

	2017/18	2016/17	2015/16
S179 ¹ inquiries commenced	24	27	24
S181 ² inquiries commenced (number of letters sent)	261 (8,461)	301 (8,960)	286 (7,997)
S182 ³ directions issued	274	407	507
Investigations started	280	414	515
Investigations completed	254	591	436
Individuals/corporations charged in criminal proceedings	14	10	20
Criminal charges laid ⁴	54	46	107
Notices of Proposed Disciplinary Action ⁵ issued	29	49	35
Notices of Decisions ⁶ issued	32	56	42
Individuals/corporations subject to ongoing civil proceedings	97	126	100
Compliance advice letters issued	277	548	453
Cases with search warrants executed	22	34	31

¹ Section 179 of the SFO gives the SFC the power to compel the production of records and documents from persons related to a listed company in relation to fraud or other misconduct.

² Section 181 of the SFO gives the SFC the power to require information from intermediaries about trading transactions, including the identity information of the ultimate clients, the particulars and instructions relating to the transactions.

³ Section 182 of the SFO gives the SFC the power to investigate SFO offences, market misconduct, fraud, misfeasance and disciplinary misconduct.

⁴ The SFC brought a total of 54 criminal charges against 11 individuals and three corporations.

⁵ A notice issued by the SFC to regulated persons that it proposes to exercise its disciplinary powers, on grounds that they appear to be guilty of misconduct or not fit and proper.

⁶ A notice that sets out the SFC's decision and its reasons to take disciplinary action against regulated persons.

Note: Also see Table 7 in Breakdown of SFC activity data on pages 163-169 for more details.

Risk assessment

As markets become more complex and interconnected, we adopt a holistic, structured approach to assessing risk using new regulatory technologies to collect and analyse large volumes of data and information.

Identifying interconnected parties

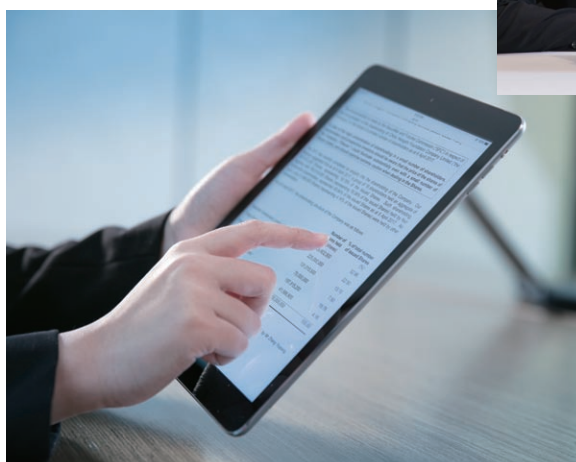
The Market Intelligence Programme uses the latest technologies to enhance our capability to identify conduct risks in our markets, including potential misconduct by interconnected parties. Data collected from our operations and public sources is analysed to isolate patterns and connections between individuals, companies and transactions which may indicate conduct risks.

Diving deep in the data

By applying new data analytic technologies and techniques to complex issues, the newly-established Data Analytics Group will allow us to carry out more effective market surveillance as well as to monitor and address prudential and systemic risks in a comprehensive manner.

Monitoring market dynamics

The Risk Review Group brings together staff with a variety of expertise from across the organisation to monitor market risks as well as market development opportunities and to understand the potential business and regulatory implications of new and emerging issues, particularly those which may pose challenges to our regulatory and supervisory efforts.



Global regulatory engagement

We actively participate in global regulatory policymaking through our involvement in international standard-setting bodies and our engagement with overseas counterparts.

IOSCO

We play an active role in the International Organization of Securities Commissions (IOSCO) which develops, implements and promotes adherence to internationally-recognised standards for securities regulation. Since our Chief Executive Officer Mr Ashley Alder was appointed as Chairman of the IOSCO Board¹ in May 2016, we worked closely with the IOSCO Secretariat to enhance the relevance of IOSCO's work to the Board and the wider membership as well as to coordinate the policy work of IOSCO and the Financial Stability Board (FSB).

This year, the IOSCO Board discussed a wide range of issues including market conduct, initial coin offerings (ICOs), cybersecurity, financial technologies (Fintech), sustainability reporting, the European Union (EU) Data Privacy Regulation, asset management and the use of behavioural insights in retail investor protection. In May 2018, Mr Alder was reappointed as Chairman of the IOSCO Board for a two-year term.

- In June 2017, the IOSCO Task Force on Market Conduct, also chaired by Mr Alder, issued its final report on the tools and approaches used by IOSCO members to discourage, identify, prevent and sanction misconduct by individuals in wholesale markets.
- In January 2018, the IOSCO Board issued a public statement highlighting the risks related to ICOs. We also participated in IOSCO's ICO Consultation Network and the IOSCO Working Group on Data Analytics.

The SFC is represented in all eight IOSCO policy committees, the Assessment Committee, the Committee on Emerging Risks and all key task forces and working groups.

- During the year, a Director of Intermediaries Supervision joined the Committee on Regulation



IOSCO Board meeting in Madrid

of Market Intermediaries which discussed retail over-the-counter (OTC) leveraged products and conflicts of interest during the capital-raising process.

- As a member of the Committee on Investment Management, we take part in initiatives including formulating and publishing IOSCO's recommendations and good practices to improve liquidity risk management for collective investment schemes. We also chair a new workstream on exchange-traded funds to identify key issues and risks which may require IOSCO's further oversight or action.
- We actively participate in the Committee on Enforcement and the Exchange of Information and the Multilateral Memorandum of Understanding Screening Group, which aims to prevent and detect breaches of securities laws and regulations in global financial markets. We also undertake a number of initiatives to support the implementation of the Enhanced MMoU² to foster greater cross-border enforcement cooperation and assistance among securities regulators.

Mr Alder co-chairs the Committee on Payments and Market Infrastructures (CPMI) – IOSCO Steering Group, which coordinates regulatory policy work, including oversight and supervision, related to central counterparties and the monitoring of the implementation of the Principles for Financial Market Infrastructures³.

¹ IOSCO's governing and standard-setting body.

² The Enhanced Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information, established in 2017, provides a mechanism for sharing investigative material and providing assistance with respect to alleged misconduct.

³ These are the international standards issued by IOSCO and the CPMI for financial market infrastructures to strengthen financial stability.

Global regulatory engagement

Financial Stability Board

As an active participant in the work of the FSB, we maintain close collaboration with the Hong Kong Monetary Authority, Insurance Authority and the Government of the Hong Kong Special Administrative Region (HKSAR) on FSB initiatives related to the securities sector.

- As Chairman of the IOSCO Board, Mr Alder is a member of the FSB's Plenary and its Steering Committee, which focus on monitoring the progress of the Group of Twenty (G20) reforms including those related to cybersecurity, misconduct risks and market-based finance. We also sit on the FSB's Standing Committee on Standards Implementation (SCSI) and participate in its Implementation Monitoring Network, which considers the effects of the G20 reforms.
 - To ensure the views of Asian markets and securities regulators are reflected in policy recommendations, we are a member of the FSB Regional Consultative Group for Asia, to which we contribute views on policy from Hong Kong's perspective.
 - During the year, we participated in various FSB workstreams and exercises, including the *Global Shadow Banking Monitoring Report 2017* and surveys on financial stability and cybersecurity and crypto-assets. We took part in the FSB Working Group on Governance Frameworks which focuses on mapping the responsibilities of senior management to mitigate misconduct risk. We also participated in the FSB Cyber Lexicon Working Group to foster a common understanding of cybersecurity terminology across the financial sector.
 - We are a member of the FSB's Workstream on Other Shadow Banking Entities, contributing to the implementation of the FSB's January 2017 recommendations to address vulnerabilities in asset management activities, including liquidity mismatches between fund investments and the redemption terms and conditions for open-ended fund units, and leverage within investment funds.
- Together with the HKSAR Government and other Hong Kong financial regulators, we responded to a peer review conducted by the SCSI covering Hong Kong's implementation of OTC derivatives market reforms and its resolution framework for financial institutions. Published in February 2018, the peer review noted that Hong Kong made good progress in both areas.

Mainland China

We work closely with Mainland authorities to support Hong Kong's long-term strategic development as Mainland financial markets continue to open up. We regularly hold high-level discussions with the China Securities Regulatory Commission (CSRC) on Stock Connect, cross-boundary enforcement and supervisory cooperation. Working groups were established to follow up on various cooperation initiatives. We also discussed regulatory updates and supervisory cooperation with the China Banking Regulatory Commission⁴.

In November 2017, together with the Financial Secretary Mr Paul Chan and Secretary for Financial Services and the Treasury Bureau Mr James Lau, our Chairman Mr Carlson Tong met with CSRC Chairman Mr Liu Shiyu in Beijing to discuss the development of Hong Kong's financial markets and regulatory cooperation with the Mainland.



High-level meeting with the CSRC in September 2017

⁴ The China Banking Regulatory Commission and the China Insurance Regulatory Commission were merged in April 2018 to form the China Banking and Insurance Regulatory Commission.

In the same month, we reached an agreement with the CSRC on proposals to introduce an investor identification regime for northbound trading under Stock Connect. We entered into a memorandum of understanding (MoU) in December 2017 on supervisory and enforcement cooperation on matters concerning futures. We also met with the CSRC to exchange information on Hong Kong brokers' preparedness to trade products listed on the Shanghai International Energy Exchange.

This year saw the launch of Bond Connect, the increase of the daily quotas under Stock Connect⁵ and the expansion of Hong Kong's Renminbi Qualified Foreign Institutional Investor investment quota⁶ following our high-level discussions with Mainland authorities.



SFC-CSRC enforcement cooperation meeting

Enforcement cooperation with the Mainland

We strengthened our collaboration with the CSRC following the introduction of new programmes providing for mutual market access between Hong Kong and the Mainland. Prior to the launch of Shanghai-Hong Kong Stock Connect, we established an enforcement cooperation mechanism^a which enables the exchange of information and intelligence with Mainland regulators. Since then, we collaborated extensively with the CSRC on cross-boundary enforcement to ensure orderly market operations and investor protection in both markets.

In December 2017, we held the fifth regular SFC-CSRC high-level meeting on enforcement cooperation, including investigations of major cases, as well as ways to enhance the implementation of the Stock Connect MoU and make cross-boundary enforcement cooperation more efficient. Other topics on the agenda were information notifications, evidence handling, staff exchanges and joint training.

^a In October 2014, the SFC and the CSRC signed an MoU on strengthening cross-boundary regulatory and enforcement cooperation under Shanghai-Hong Kong Stock Connect.

We engaged in discussions with Mainland authorities to formulate new Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) measures⁷ relating to the securities sector. These included enhancing the mechanism for closer financial cooperation and cross-boundary renminbi fund flows, expanding the scope of eligible securities under Stock Connect, assessing the progress of the Mainland-Hong Kong Mutual Recognition of Funds scheme as well as supporting the development of offshore risk management business. During the year, the CSRC granted approval for two Hong Kong financial institutions to set up multi-licensed joint venture securities companies on the Mainland.

We actively support the HKSAR Government in strengthening Hong Kong's cooperative relationship with Guangdong, Beijing, Shanghai and other regions to facilitate access to the Mainland market by Hong Kong's financial services sector.

We organised five training programmes and seminars for senior executives from Mainland authorities and organisations to enhance their understanding of our regulatory work. In December 2017, the SFC and the CSRC co-organised a case study training session in Xiamen where both regulators and the US Securities and Exchange Commission shared their experience in investigating breaches of disclosure rules, fraudulent offerings and market manipulation.

⁵ The new daily quotas are RMB52 billion for each of the northbound trading links and RMB42 billion for each of the southbound trading links with effect from 1 May 2018.

⁶ The quota was increased from RMB270 billion to RMB500 billion on 4 July 2017.

⁷ Two new CEPA agreements – the Investment Agreement and the Agreement on Economic and Technical Cooperation – were signed between the HKSAR Government and the Mainland's Ministry of Commerce on 28 June 2017 and implemented on 1 January 2018.

Global regulatory engagement



Fintech cooperation agreement with FINMA

Bilateral agreements

We collaborate with overseas counterparts to keep abreast of emerging regulatory issues. During the year, we signed separate Fintech cooperation agreements with the UK Financial Conduct Authority (FCA), Australian Securities and Investments Commission, Dubai Financial Services Authority, Securities Commission Malaysia and the Swiss Financial Market Supervisory Authority (FINMA).

In July 2017, we entered into an MoU with the UK FCA providing for consultation, cooperation and information exchange in the supervision of regulated entities which operate on a cross-border basis in Hong Kong and the UK.

We signed an MoU with Autorité des Marchés Financiers in the same month to allow eligible French and Hong Kong public funds to be distributed in each other's market through a streamlined vetting process.

In November 2017, we attended the ninth MoU meeting with the Taiwan Financial Supervisory Commission to discuss topics including anti-money laundering and Fintech regulation.

Other engagement

In December 2017, we hosted the second EU-Asia Pacific Forum on Financial Regulation, co-chaired by Mr Alder, in Hong Kong. Regulators from the EU and the Asia-Pacific region discussed the cross-border regulatory implications of EU regulations, sustainable finance, Fintech, asset management and fund passporting.

Effective 18 August 2017, Mr Tong and Mr Alder were appointed members of the Financial Leaders Forum for a two-year term. Set up by the HKSAR Government, the forum provides a platform to discuss strategic and forward-looking proposals to strengthen Hong Kong's position as an international financial centre.

We maintained regular dialogues with overseas regulators including the Swiss FINMA and the US Federal Reserve to share intelligence and updates on the supervision of global financial institutions. We also participated in regional supervisory colleges to discuss the oversight of global investment banks with our regulatory counterparts.

In August 2017, we entered into an MoU with the Hong Kong Police to formalise and strengthen cooperation in combating financial crime. The MoU covers case referrals, joint investigations, investigative assistance and the exchange and use of information, and establishes a framework for closer collaboration on policy, operational and training issues.

We handle investigatory requests from and send requests to overseas regulators under various cooperative arrangements⁸.

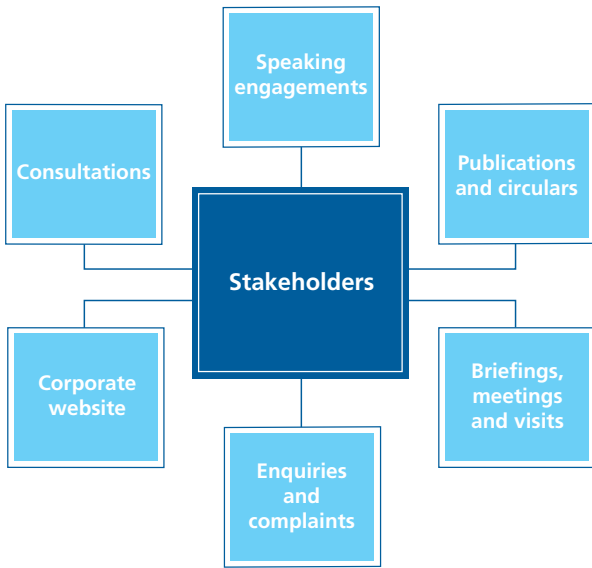
Requests for regulatory cooperation

	2017/18		2016/17		2015/16	
	Received	Made	Received	Made	Received	Made
Enforcement-related requests for assistance	136	104	155	112	92	160
Licensing-related requests for assistance	112	1,178	125	1,101	124	1,104

⁸ Including the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information which was established in 2002.

Stakeholder communication

We strive to help stakeholders understand our work and provide them with up-to-date regulatory information through timely, concerted and effective outreach. We use multiple channels to engage with a wide range of stakeholders.



Industry

In March, we organised the SFC Regulatory Forum 2018 attended by around 900 participants from the financial industry, listed companies and regulatory and professional bodies. This biennial event is a platform for us to discuss the latest regulatory developments with our stakeholders (see sidebar on pages 76-77).

We maintain an open and productive dialogue with industry associations, professional bodies and other market participants. We also regularly organise meetings and briefings to keep industry participants informed about regulatory developments.

When we propose rules under the Securities and Futures Ordinance (SFO), we consistently exceed statutory requirements for public consultation. We consult the public on proposed non-statutory codes and guidelines, as well as amendments to them, before they are implemented. We issue consultation papers containing detailed proposals and hold both formal and informal discussions with relevant stakeholders to seek their views as part of the consultation process.

Publications and other communications

	2017/18	2016/17	2015/16
Press releases	138	134	114
Consultation papers	11	4	5
Consultation conclusions	8	2	9
Industry-related publications	15	13	11
Codes and guidelines ^a	10	4	3
Circulars to industry	83	74	68
Corporate website average daily page views ^b	67,664	59,952	51,020
General enquiries	7,494	6,532	7,033

^a Includes updates to previous versions.

^b The average number of webpages browsed per day during the reporting period.

Stakeholder communication



SFC Chairman Mr Carlson Tong at the HSBC Financial Dialogue Series 2018

After completing our analysis, we issue a consultation conclusions paper summarising the main comments received and setting out our conclusions. We published 11 consultation papers and eight consultation conclusions in the year.

During the year, our senior executives took part in 83 speaking engagements on various topics within our remit. We supported 13 seminars or events organised by industry bodies.

In October 2017, our senior executives spoke at a full-day programme we organised with the Hong Kong Monetary Authority (HKMA) to discuss regulatory issues related to financial technology (Fintech) development. The programme was part of Hong Kong Fintech Week sponsored by InvestHK. We also engaged with a wide range of stakeholders including financial institutions, industry organisations and start-ups through the SFC Fintech Contact Point¹, which handled 112 enquiries during the year.

Our publications aim to update the industry on our regulatory work, topical issues and other developments. This year, we published 15 thematic publications, including periodic newsletters, market reviews and surveys.

We launched two new publications during the year. The *SFC Regulatory Bulletin: Listed Corporations*, launched in July 2017, provided guidance on the manner in which we perform some of our functions under the Securities and Futures (Stock Market Listing) Rules and the SFO regarding listed corporations and other listing matters. In December 2017, the first edition of the *SFC Compliance Bulletin: Intermediaries* reminded the industry of the importance of managing conflicts of interest in selling practices and asset management.

Circulars and frequently-asked questions are posted on the SFC website to help the industry better understand our regulatory requirements. This year, we issued 83 industry circulars informing industry participants about various matters, including anti-money laundering, over-the-counter derivatives transactions, investment product distribution, securities margin financing and regulated activities involving cryptocurrency-related products and derivatives.

Government

By attending Legislative Council (LegCo) meetings, including meetings of the Panel on Financial Affairs and relevant Bills Committees, we provide legislators with details of our policy initiatives, explain the rationale behind our work and answer questions. We also respond to enquiries and complaints referred to us or raised by LegCo members and other government agencies.

¹ The SFC Fintech Contact Point was launched in March 2016 as a dedicated portal to receive enquiries and requests related to Fintech.



Hong Kong Fintech Week 2017

Through regular meetings and reports, we maintain close liaison with the Financial Services and the Treasury Bureau and provide updates on our regulatory initiatives. We also provide assistance and information to other government bureaux and departments on various issues.

Regulatory counterparts

We play an active role in international regulatory cooperation through our participation in both the International Organization of Securities Commissions and the Financial Stability Board².

To enhance regulatory cooperation, we maintain close contact with local, Mainland and overseas regulatory counterparts. During the year, we signed four memoranda of understanding (MoU) with other authorities and exchanges and held more than 40 MoU meetings. In addition, we signed five cooperation agreements with overseas regulators on the development and application of Fintech, and received visitors and delegates from Mainland and overseas authorities.

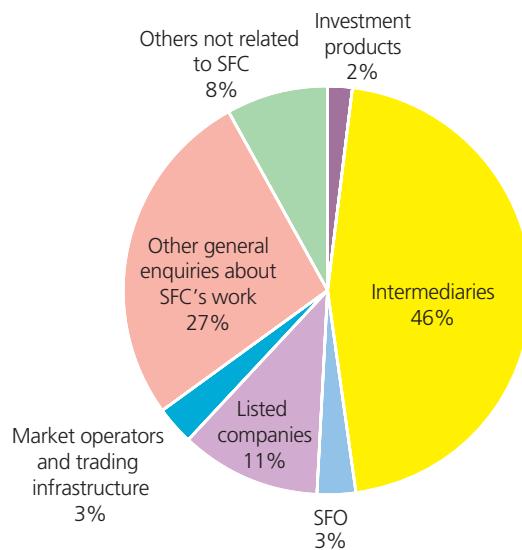
The public

We address public concerns and enquiries regarding the securities and futures markets. During the year, we received a total of 7,494 general enquiries by phone or in writing.

Complaints against intermediaries and market activities are first reviewed by our Complaints Control Committee, comprising senior executives from across the organisation, and are allocated to responsible divisions for assessment where appropriate.

We handled 2,689 complaints during the year. A total of 1,256 cases³ were allocated for further review and 516 were referred to Hong Kong Exchanges and Clearing Limited or other financial regulators and law enforcement agencies.

General enquiries



² See Global regulatory engagement on pages 69-72.

³ One case may comprise multiple complaints.

SFC Regulatory Forum 2018

The third SFC Regulatory Forum, our biennial event, took place on 14 March 2018. The event centred on initiatives to enhance the competitiveness of Hong Kong as a capital-raising centre amidst rapid technological innovation and increasing connectivity with the Mainland and other markets.

The event kicked off with opening remarks from our Chairman, Mr Carlson Tong, who emphasised the importance of attracting a greater variety of listed companies and collaborating more closely with both local and overseas regulators.

The keynote address by Mr Paul Chan, Financial Secretary of the Government of the Hong Kong Special Administrative Region, highlighted the Government's initiatives to promote the development of financial services and enhance Hong Kong's competitiveness as an international financial centre. Mr Chan stressed that Hong Kong needs to be innovative and proactive to remain competitive and maintain its growth momentum.

Hong Kong is not only a super-connector to mainland China – we have also been playing a very important risk management role from a policy perspective.

*Au King Lun, Chief Executive Officer,
Value Partners Group Limited*



The first of four panel discussions addressed ongoing reforms to listing regulation in Hong Kong in the context of the SFC's front-loaded, real-time approach and the evolving relationship between Hong Kong and Mainland capital markets. Our Chief Executive Officer Mr Ashley Alder stressed that effective regulation and reciprocal, balanced regulatory cooperation are vital to further market integration and expand global investment flows.

In this age of advanced technology, the industry needs to move fast to provide the public with the convenience they need and a better overall experience with financial services.

*Chu Gang, Chief Operating Officer and
Chairman of Capital Markets Committee,
China International Capital Corporation Limited*





Another panel considered the opportunities and challenges facing the asset management industry in view of recent cross-border initiatives. Panellists also weighed the potential for Hong Kong to develop as the region's premiere risk management centre and derivatives hub as the city plays an increasingly important role in connecting the Mainland and the rest of the world.

Mainland China will be the largest source of new listings and capital flows for Hong Kong in the years to come and the key strategy to drive this is to raise corporate governance standards in Hong Kong.

Yin Ke, Chief Executive Officer, CITIC Securities International Company Limited

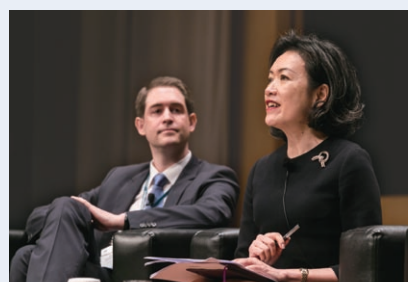
In the third panel, speakers discussed the role of regulation in changing corporate behaviour and the need for changes in listing regulation to deal with the most pressing problems, particularly shell manufacturing and backdoor listings, as well as the role of independent non-executive directors.

The last panel addressed our recent efforts to ensure intermediaries' compliance (eg, senior management responsibilities and accountability) and deter corporate fraud and market misconduct. The discussions also covered how we are keeping up with the pace of technological change in the financial services industry.

Around 900 leaders from the financial industry, listed companies, professional services firms and industry associations attended the full-day event. Videos of the proceedings and a summary of discussions were posted on the SFC website.

We need to make sure that valuations fairly reflect the value of the underlying assets and that there are protections for minority shareholders and all shareholders are treated equally.

Manuel Schlabbers, Chief Executive Officer, Accudo Capital Limited



Stakeholder communication

We launched a new system which provides a one-stop platform for storing and processing information about the complaints we receive. With the new system, we can more easily access information, compile statistics, generate management reports and track the progress of complaints.

To increase public understanding of Hong Kong's financial regulatory framework and our regulatory role, we received visitors from local and overseas institutions and our senior executives delivered key messages in media interviews. We issued 138 press releases to inform the public of the latest regulatory actions and other SFC news.

We published our *Annual Report 2016-17* and three quarterly reports to help stakeholders understand our work. Our reporting efforts were recognised

with a Gold prize in the Hong Kong Management Association's Best Annual Reports Awards 2017, and a Gold award, public sector category, in the Hong Kong Institute of Certified Public Accountants' 2017 Best Corporate Governance Awards.

The public can easily obtain up-to-date information about our work and regulations on our corporate website. This year we made enhancements to facilitate access to information. To provide easier access to licensing information, we published a comprehensive *Licensing Handbook* on our website and made webpages more user-friendly. We also enhanced our homepage and other sections to improve web accessibility for users with visual or hearing disabilities.

Handling complaints and enquiries with aplomb

We strive to responsibly and professionally address complaints and enquiries regarding the markets. Our efforts were recognised during the year when Sam Chiu, Manager, External Relations, Corporate Affairs, received The Ombudsman's Awards 2017 for Officers of Public Organisations for his outstanding work in this area.

Chiu, who handles public complaints and enquiries on a daily basis, says he always tries his best to help investors understand our rules and regulations. Putting himself in their shoes helps him better understand where they are coming from.

The work can be challenging in some cases where we cannot provide certain details of our work due to secrecy provisions in the law. Nonetheless, he adds, quality complaints are a valuable channel for us to learn about market misconduct and regulate the markets more effectively.

One of the most memorable cases Chiu handled during his seven years at the SFC began with a call he received about a broker failing to return client securities.

This led to immediate regulatory action including a restriction notice on the broker to preserve its clients' assets.

In receiving his award, Chiu credited the support of his supervisors and team members for helping him excel in his role.



When the public contacts us with complaints and enquiries, we have the responsibility to help them understand the markets we regulate.

Sam Chiu

Complaints against intermediaries and market activities

	2017/18	2016/17	2015/16
Conduct of licensees	357	411	338
Conduct of registered institutions	22	39	34
Listed companies and disclosure of interests	779	739	631
Market misconduct ^a	322	221	265
Product disclosure	12	8	9
Unlicensed activities	141	116	128
Breach of offers of investments	48	141	21
Boiler rooms and suspicious websites	319	330	310
Scams and frauds ^b	186	132	100
Other financial activities not regulated by SFC ^c	503	185	220
Total	2,689	2,322	2,056

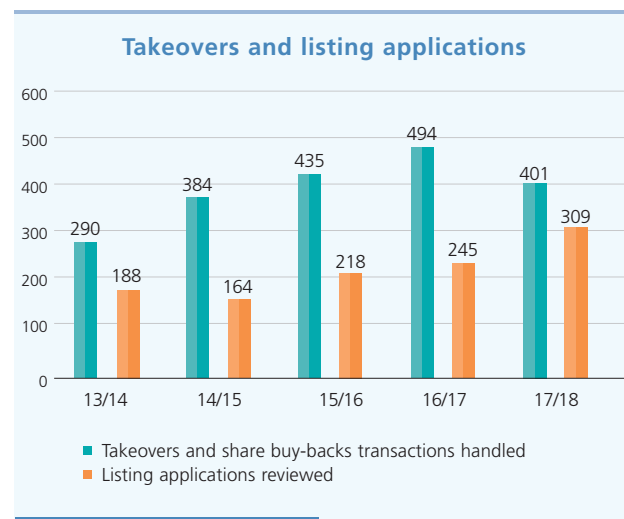
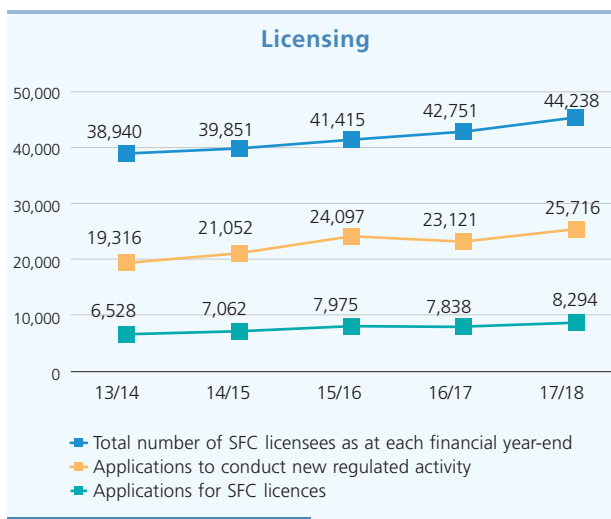
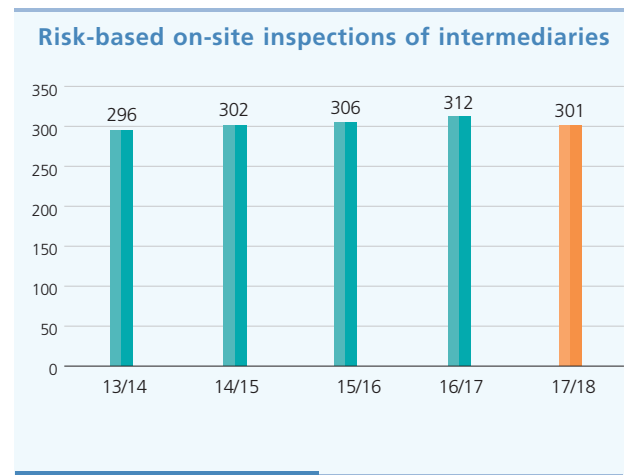
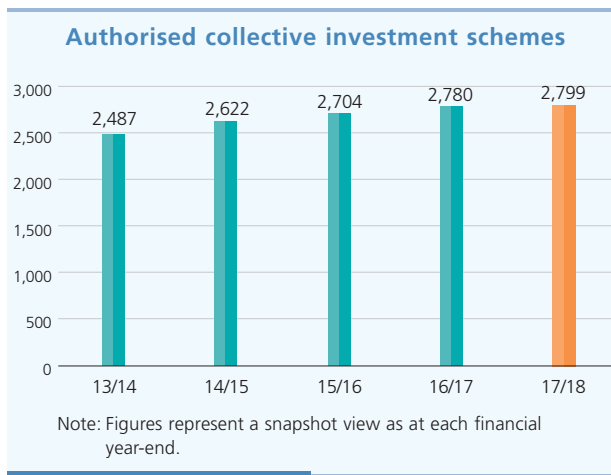
^a Primarily, alleged market manipulation and insider dealing.

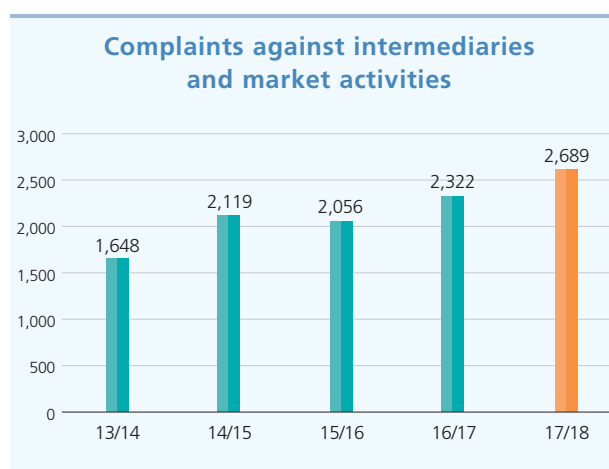
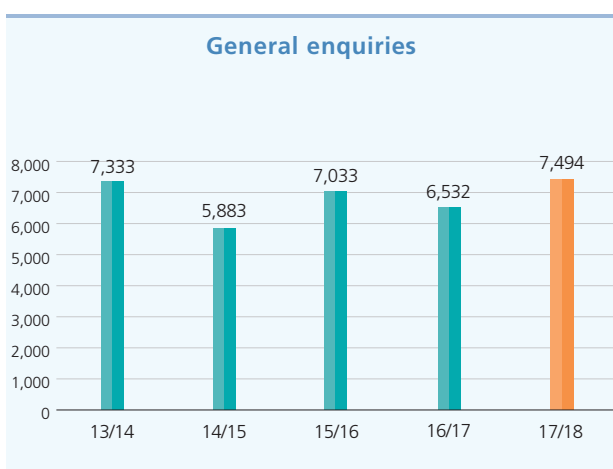
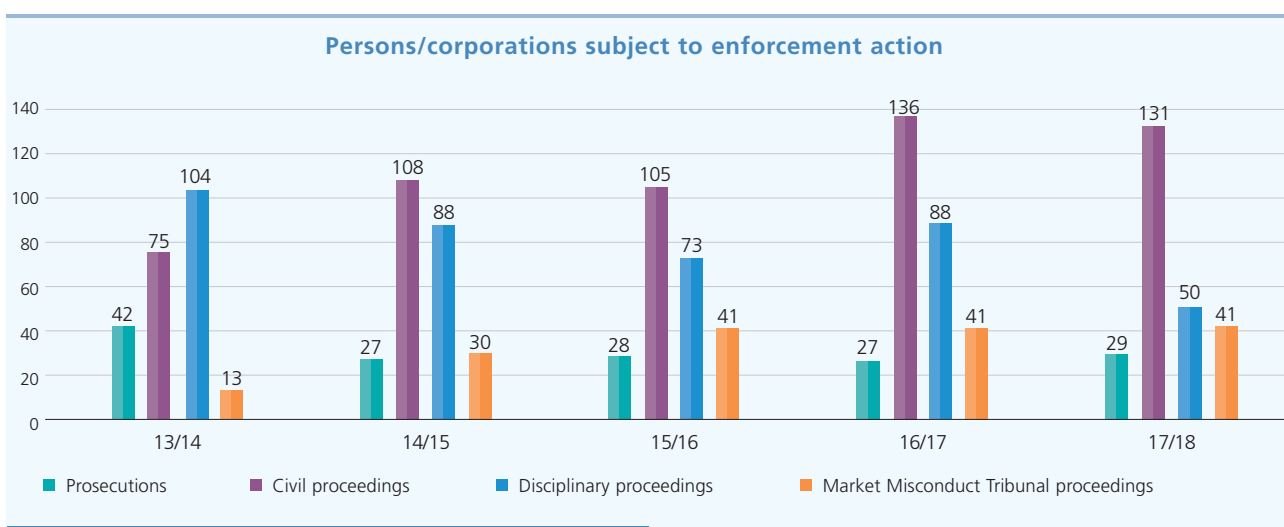
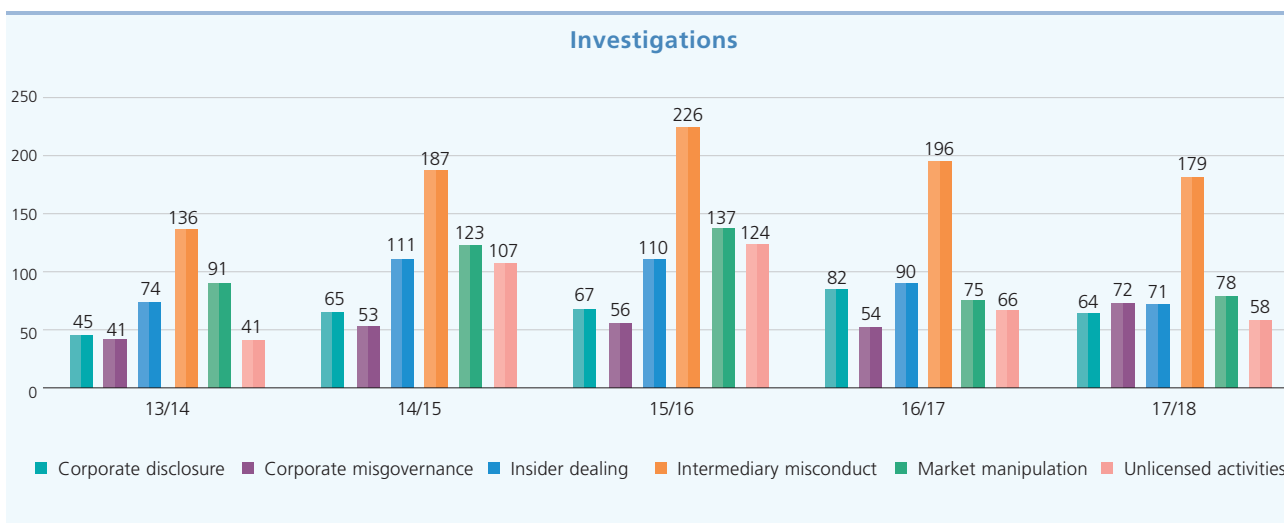
^b Such as identity fraud and impersonation.

^c For example, bullion trading, banking complaints.

SFC activity data

These charts are intended to show at a glance some top-line data on our activities. See Breakdown of SFC activity data on pages 163-169 for more details.





Corporate Social Responsibility

Our corporate social responsibility initiatives focus on supporting sustainable markets, caring for the community, protecting the environment and promoting staff wellness.

As a socially responsible organisation, we strive to incorporate corporate social responsibility (CSR) principles into our daily operational decisions and practices.

Governance

Our CSR efforts are coordinated by a dedicated committee which reports directly to the SFC's Executive Committee. The CSR Committee is chaired by the Chief Financial Officer and Senior Director of Corporate Affairs, and includes members from different units across the organisation.

The Committee is responsible for:

- formulating and developing our CSR vision, principles, framework and policies;
- organising and promoting CSR activities; and
- setting objectives, targets and key performance indicators to measure the effectiveness of our CSR efforts.

The CSR Committee has three working groups. Each is charged with planning and implementing initiatives under a specific theme.

Corporate Social Responsibility

	Focus	2017/18	2018/19
Commission Volunteers Group 	Community	Reach out, help out, volunteer	Extend, expand
Green Working Group 	Environment	Environmental sustainability is our responsibility	Green in SFC, counts on you and me
Wellness Group 	People	Good health is your wealth	Being healthy, being well

We explain our CSR goals, principles and activities on our corporate website and intranet, and circulate a quarterly e-newsletter to update staff about the outcomes of our CSR initiatives. The newsletter is also a platform for participants to share first-hand accounts of our CSR activities and for all staff to provide feedback.

Our CSR efforts were recognised by the Hong Kong Council of Social Service which named us a “Caring Organisation” for the twelfth consecutive year.



Walking abandoned dogs



English practice with students

Corporate Social Responsibility

Marketplace support

As a statutory body, we consider the impact of our regulatory work on Hong Kong's financial markets. We adopt measures to enhance industry-wide operational efficiency, minimise resource consumption and reduce paperwork for both the SFC and industry participants.

Raising industry-wide operational efficiency

In February 2018, we adopted a revamped process for applications for approval of post-authorisation changes and for authorisation of revised offering documents for funds¹. The revamped process provides timely notification of post-authorisation changes to investors and allows more efficient use of our resources.

We implemented a mandatory online submission initiative in 2017 which requires individual applicants and licensees to submit applications, notifications and annual returns via the SFC Online Portal. This enables us to handle an increasing number of applications and makes the licensing process more efficient.

To reduce the industry's compliance burden and paper consumption, we ceased to issue printed licences² to individuals in 2015. Details of licensed individuals are now only available on our online Public Register of Licensed Persons and Registered Institutions.

An online system to streamline the submission and posting of Rule 22³ dealing disclosures under the Code on Takeovers and Mergers has been in operation since 2014.

The Mixed Media Offer process, another measure to reduce paper consumption, allows listed applicants and listed companies to distribute paper application forms for public offers where an online prospectus is available.

Promoting professional competence

We have continuous professional training (CPT) requirements⁴ in place to enhance the competence of licensees. This year, our senior executives delivered 55 hours of CPT-eligible training to licensees.

We funded the Hong Kong Securities and Investment Institute's Advanced Learning Platform, an online portal launched in September 2017 enabling market practitioners to access learning resources at their convenience. We also provide funding to the Financial Reporting Council which aims to uphold the quality of listed companies' financial reporting, as well as to the Financial Dispute Resolution Centre to provide an effective, cost-efficient channel for financial institutions and their customers to resolve monetary disputes.



Christmas charity sale



Baking cookies with Fu Hong Society members



Making ornaments with Po Leung Kuk members

¹ See Investment products on pages 47-50.

² We continue to issue printed licences for licensed corporations and certificates of registration for registered institutions, and these must be exhibited prominently at their places of business.

³ Rule 22 of the Code on Takeovers and Mergers requires parties to an offer and their respective associates to disclose dealings in relevant securities of the offeree company and the offeror (in the case of a securities exchange offer) conducted for themselves or on behalf of discretionary clients during an offer period.

⁴ Under the SFC's Guidelines on Continuous Professional Training, licensees are required to complete a minimum of five CPT hours per calendar year for each type of regulated activity.

Community

We provide staff with volunteering and engagement opportunities to make a positive impact on the community. We offer volunteering leave to encourage staff participation in community service.

This year, 134 staff spent a total of 458 hours volunteering. Our staff engaged with different members of the community, including minorities, the single elderly, the intellectually challenged and the underprivileged.

Our staff also support community services through donations and fundraising events. This year, we raised a total of \$104,509 through the Standard Chartered Marathon, a Christmas charity sale and four Community Chest events: Love Teeth Day, Dress Casual Day, Skip Lunch Day and Green Day.

Donating used items to charities allows us to give back to the community and reduce wastage. This year, we

donated used computers, printers and servers to Caritas Hong Kong's computer refurbishment project which prolongs the lifecycle of computers and accessories and reduces landfill.

We partnered with Po Leung Kuk to make Christmas gifts with its members who are physically or intellectually challenged. We also engaged three other social enterprises, namely the Fu Hong Society, Hong Kong Down Syndrome Association and Hong Kong Society for Rehabilitation, to sell items made by their members at our in-house Christmas charity sale. We received orders worth more than \$8,100 and additional donations of over \$2,300 to these four charities.

As a participant in the ENGAGE programme organised by Community Business, we offered a two-week work placement opportunity to disadvantaged secondary students to raise their career aspirations.

Message from Chairman and CEO

Strategic Priorities

Mission and Mandates

Corporate Governance

Our People

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The joy of sharing

At Christmas 2017, our Chairman Mr Carlson Tong took part in the Carol Singing Festival to raise money for the Child Development Matching Fund, a charity which supports underprivileged youth. The Financial Secretary Mr Paul Chan, leaders from the financial sector and other guest singers also joined the children's choir to "sing for our next generation".



Director of Enforcement Denise Ip bakes for charity sale



Chairman Mr Carlson Tong joins Child Development Matching Fund's Carol Singing Festival

Cooking for charity

For the past three years, our staff have looked forward to our in-house Christmas charity sale where they could sample treats prepared by expert baker Denise Ip, Director of Enforcement, whose motto is "love to cook, cook for love". Denise creates her own recipes for delicacies ranging from mini panettone to organic chocolate truffles and also designs festive packaging to reflect the spirit of the season. Because her creations always sell out fast, this year colleagues were invited to place orders in advance to avoid disappointment.

Corporate Social Responsibility

Volunteering events

Month	Activity	Purpose	Outcome
Apr 2017	Retail store visit with underprivileged students	To interact and practise English with underprivileged children	19 volunteers visited the flagship store of an audio-visual retail chain with 60 primary school students who spent the day practising English and learning about retail operations.
May 2017	Care for animals series 1: Abandoned rabbits	To raise awareness about abandoned rabbits' welfare	18 volunteers helped to feed abandoned rabbits and clean their cages, raising \$2,420 for the Hong Kong Rabbit Society.
Aug 2017	Baking cookies with the mildly visually impaired	To interact with the mildly visually impaired	20 volunteers spent quality time baking chocolate and butter cookies with Fu Hong Society members.
Sep 2017	Mid-Autumn series 1: Hot meal distribution to the homeless	To raise awareness about poverty	19 volunteers joined Sunshine Action to visit rough sleepers in Nam Cheong and Sham Shui Po and distribute meal packages to the needy.
Oct 2017	Mid-Autumn series 2: Elderly home visit and rice delivery	To connect with the elderly community	18 volunteers visited and delivered rice bags to the elderly during Mid-Autumn Festival.
Nov 2017	Care for animals series 2: Abandoned cats and dogs	To raise awareness about abandoned pets' welfare	14 volunteers visited cat kennels and walked abandoned dogs, raising \$2,650 for the Society for Abandoned Animals.
Dec 2017	Christmas gift-making with the physically and mentally impaired	To interact with and raise funds for the physically and mentally impaired	15 volunteers made tissue boxes and Christmas ornaments with Po Leung Kuk members.
Feb 2018	Chinese New Year activities with underprivileged children	To interact and practise English with underprivileged children	60 primary school students enjoyed a fun cooking experience with volunteers.

Contributions

	2017/18	2016/17	2015/16
Number of staff participating in volunteering activities	134	110	137
Total volunteering hours	458	471	548
Funds raised for community causes	\$104,509	\$70,648	\$186,789
Corporate sponsorships for community causes [^]	\$13,000	\$9,000	\$18,000

[^] Including donations in lieu of corporate gifts made in the names of guest speakers invited to our in-house training seminars.

Environment

We are committed to managing and reducing our impact on the environment and raising green awareness amongst staff and stakeholders. We encourage staff to reduce, reuse, repair and recycle through our internal protocol, *A guide to working "Green" at the SFC*.

We adopt a number of green practices in our workplace to encourage the smarter use of resources including:

- sharing meeting materials on tablet computers;
- using internal electronic processes for training course enrollments, conference room bookings, expense claims, overseas travel records, pay slips, leave applications, appraisals and paperless diaries to save time and paper;
- adjusting indoor lighting after office hours using auto timers;
- reducing electricity usage at our data centres;
- providing recycling bins for newspapers;
- sorting cans and bottles for recycling;
- replacing paper holiday greeting cards with e-cards; and
- recycling used red packets in support of Greener Action's campaign.



Mid-Autumn series: Elderly home visit and rice delivery



Cooking class with students

Corporate Social Responsibility

We extend our green efforts beyond the workplace by supporting the World Wide Fund for Nature's global warming prevention and environmental conservation causes.

- No Shark Fins Policy: We have in place an organisation-wide policy pledging not to serve sharks' fins at any SFC event.
- Earth Hour 2018: We took part in this annual energy conservation event for the eighth year. In addition to encouraging staff to switch off lights for one hour, this year we also made a pledge as a corporate supporter.



Visit to Go Green Organic Farm

We engaged our staff in a number of initiatives to raise their environmental awareness throughout the year. To promote an eco-friendly lifestyle, we organised a handmade soap workshop where colleagues learnt how to make natural, bio-degradable soap. We arranged outdoor activities for our colleagues to explore Hong Kong's natural ecosystem, including an eco-tour to Mai Po guided by the World Wide Fund and a visit to Go Green Organic Farm to learn about biodiversity and environmental stewardship.

Consumption and recycling

	2017/18	2016/17	2015/16
Consumption			
Paper (pieces/head)	9,563	10,857	11,831
Electricity (kWh)	4,018,442	4,770,712	4,078,591
Recycling			
Paper (kg)	37,815	30,852	26,048
Toner and printer ink cartridges	1,106	1,130	1,008



Eco-tour to Mai Po

Workplace

The wellbeing of our staff is vital to us. In the past year, we organised activities to enhance health awareness and encourage healthier lifestyles including:

- Mental Health Month to raise awareness and promote open dialogue about mental health;
- a Pilates session to introduce physical exercise techniques;
- free on-site influenza vaccinations and health screening with individual consultations;
- lunchbox recipes to encourage healthier diets; and
- a health talk to illustrate the benefits of physical exercise.



Pilates class



Handmade organic soap workshop

Workplace mental health

We promote wellbeing in the workplace through our support for mental health initiatives. As a founding member of City Mental Health Alliance Hong Kong (CMHA HK) and a member of its Advisory Committee, we help strengthen the mental health awareness both of our staff and of the business community at large. Launched in 2017, CMHA HK is the Hong Kong chapter of London’s City Mental Health Alliance which aims to build a supportive working environment where mental health issues can be openly discussed.

Our Chief Executive Officer (CEO) Mr Ashley Alder discussed mental health in the workplace at the Hong Kong Mental Health Conference 2017, a three-day event held in November.

In October 2017, our CSR Wellness Group invited staff to participate in CMHA HK’s mental health survey to collect data for use in planning training and other events for the financial industry. In March 2018, the group organised Mental Health Month with talks, workshops and newsletters on various mental health topics for our staff.



Mr Alder, CEO, addresses the Hong Kong Mental Health Conference 2017



A staff talk on “Stress Management: Occupational Stress and Mental Health”

CSR activity calendar

April – June 2017

- Community Chest Green Day
- Handmade organic soap workshop
- **Beach clean-up**
- Retail store visit with underprivileged students
- Care for animals series 1: Abandoned rabbits
- Healthy lunchbox recipes



July – September 2017

- Organic farm visit
- Baking cookies with the mildly visually impaired
- **Mid-Autumn series 1: Distributing hot meals to the homeless**
- Health screening
- Pilates class
- Blood donation day

October – December 2017

- Community Chest Dress Casual Day
- Nutrition bar day
- Health talk
- Mid-Autumn series 2: Elderly home visit and rice delivery
- Community Chest Love Teeth Day
- **Care for animals series 2: Abandoned cats and dogs**
- Christmas series 1: Gift-making with the physically and mentally impaired
- Christmas series 2: Christmas charity sale



January – March 2018

- Red packet recycling
- Massage day
- Mental Health Month
- Chinese New Year series: Cooking class with underprivileged students
- **Eco-tour to Mai Po**

Corporate Developments

Building an efficient organisation driven by an effective and engaged workforce is crucial for us to carry out our regulatory work.

We strive to build a high-performing, effective and engaged workforce while ensuring our resources are used appropriately. We periodically upgrade our information technology infrastructure and adopt a centralised approach to data analysis.

People

Professional development

At the SFC, people development incorporates our core values – “professional”, “proactive” and “people count”. Enhancing the professional capabilities of our staff and equipping them with the right knowledge and skills is important for us to operate effectively.

During the year, we undertook a thorough review of our talent and performance management practices to foster a merit-based approach to performance evaluation, career development and reward management.

A new programme was launched during the year to equip our senior management with the knowledge and tools to lead strategically. We continued our Leading with Effectiveness and Professionalism (LEAP) programme which supports employee growth and helps build effective teams. By the end of the year, 81% of our people managers had completed the programme.

Our Chief Executive Officer (CEO) communicated important organisational matters, discussed regulatory initiatives and addressed staff questions at regular CEO sharing sessions. Other senior management shared new regulatory developments with staff at Commission Connection Series events.

A cross-divisional exchange programme helps staff broaden their work experience through short-term internal secondments and we organise briefing sessions to increase staff awareness of available resources for career development.

Corporate Developments

Professional staff were offered annual secondment opportunities to the Financial Services Development Council, Financial Services and Treasury Bureau as well as the China Securities Regulatory Commission (CSRC). We signed a Memorandum of Understanding with the CSRC in March 2018 to facilitate personnel exchanges. We also arranged visits to regulatory counterparts in Shenzhen and Shanghai and workshops on Mainland capital markets-related themes.

We offer training based on identified learning and development needs. This year, we invited local and overseas regulators and industry professionals to present and discuss topics including financial products, regulatory changes and market developments on the Mainland and overseas. Two new e-modules on regulatory and legal topics were added to complement our training courses.

During the year, each employee spent an average of 31 hours on structured learning courses, including workshops, seminars and training programmes. Invitations to some of these programmes were extended to fellow regulators such as the Hong Kong Monetary Authority and Insurance Authority.

We recruited six graduate trainees in the ninth annual intake for our Graduate Trainee Programme and placed 44 summer and winter interns in various divisions.



To acknowledge and reward outstanding performance and encourage our staff to strive for continuous development, we recognised one individual and 13 teams in our annual Employee Awards for 2017.

For the twelfth consecutive year, the SFC was named a “Caring Organisation” for our encouragement and support of employee volunteering and for providing family-friendly work arrangements.¹ We also received the “Employees Retraining Board Manpower Developer” award for the fifth time for advocating the importance of learning and development.

Training and e-learning

	2017/18	2016/17	2015/16
Percentage of employees who participated in internal training [^]	89%	95%	95%
Average hours of internal training per employee [^]	31	31	34.2
Number of employees who undertook e-learning	185	198	175

[^] Including lectures, workshops and seminars.

¹ See Corporate Social Responsibility on pages 82-90.

Quality workplace

As an equal opportunity employer and an employer of choice, we provide a safe, quality work environment and promote good employment practices and a sense of belonging.

Our staff have opportunities to mingle by participating in inter-organisational, cross-divisional activities such as dragon boat races as well as in basketball and badminton tournaments with fellow regulators.

Our Women’s Network² organised seminars for all staff on topics including developing self-awareness and building executive presence. It also supported “Ring the Bell for Gender Equality” in celebration of International Women’s Day.

We provide an appropriate and friendly environment for post-natal employees where practicable.



Information technology

We have begun centralising all electronic data submissions in a single online portal to make the process more user-friendly for the industry. Our information technology infrastructure was upgraded³ and our network security was strengthened against malware and ransomware threats. A new version of our intranet was launched to improve collaboration and efficiency. We also enhanced our search functions to improve access to information.

To meet rising demand for reference materials, we broadened access to online information resources and organised 20 training sessions during the year. We expanded our collection of specialised financial and legal research databases, including regulatory intelligence and market data. As of end-March 2018, we subscribed to 88 electronic databases.

Administration

We regularly review our corporate resources, including space requirements, to ensure that our operational needs are met. To keep our workplaces well-equipped and occupationally safe, we carried out office repair and maintenance work.

Access controls safeguard against unauthorised entry to our office premises. Access rights are properly assigned and closely managed. A business resumption plan addressing readily identifiable risks, including technical problems, fires, natural disasters and other emergencies, is in place.

Communications

We emphasise active communications with the industry as well as the public through multiple channels, including the SFC Regulatory Forum, senior executives’ speaking engagements, seminars and workshops, consultation and consultation conclusions papers, industry circulars, industry-related publications, annual and quarterly reports and press releases. Our constantly updated corporate website (www.sfc.hk) provides timely and easily accessible public information.

Our press office’s proactive engagement with the media enhances the transparency of our operations and promotes public understanding of our regulatory actions and policies.

² The SFC Women’s Network aims to enhance professional development and inspire women for leadership roles.
³ Our IT Quality Management System was upgraded to ISO 9001:2015 to enhance the quality of service delivery.

Corporate Developments



Legal support

Our in-house legal team performs a full range of services to support our work. It prepares and conducts criminal cases and manages civil litigation and Market Misconduct Tribunal cases initiated by the SFC, and defends judicial reviews and other cases brought against the SFC.

In our day-to-day work, it provides advice and guidance on legislative drafting work and regulatory matters such as licensing, takeovers, enforcement investigations and compliance with disclosure requirements, as well as on administrative affairs including employment and procurement contracts.

As collaboration between regulators becomes more important, our in-house legal team maintains regular contact with the legal affairs department of the CSRC and conducts joint training with them on an annual basis. The second joint SFC-CSRC legal seminar took place in Xiamen in December 2017.

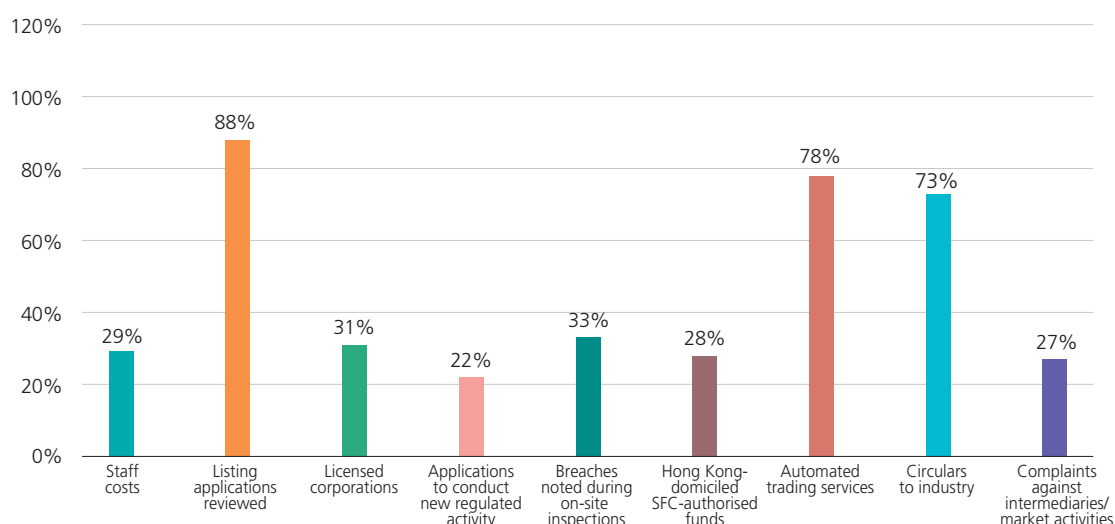
Breakdown of staff

	As at 31.3.2018		As at 31.3.2017		As at 31.3.2016		As at 31.3.2015	
	Actual	Budget	Actual	Budget	Actual	Budget	Actual	Budget
Professional	701	759	677	729	651	698	608	666
Support	186	185	190	188	190	195	185	186
Total	887	944	867	917	841	893	793	852

Employee statistics

	As at 31.3.2018	As at 31.3.2017	As at 31.3.2016
Male	289	283	278
Female	598	584	563
Average years of service	8	7.7	7.2
Female staff at Senior Manager grade or above	61%	59%	59%

Three-year change in staff costs, regulatory activities and market statistics (2014/15-2017/18)



Finance Funding

We are operationally independent of the Government and are funded mainly by transaction levies and fees from market participants. The current levy rate is 0.0027% for securities transactions, which is significantly less than the initial rate of 0.0125% when the transaction levy mechanism was set up in 1989. We have not revised our fees and charges since 1994. Additionally, we have offered waivers for annual licensing fees five times since 2009. The current waiver is in effect for one year beginning 1 April 2018.

As a publicly-funded organisation, we follow a disciplined approach in drawing up our budget. We appoint external investment managers to manage our reserves according to investment guidelines approved by the Financial Secretary. This year, the annual review of our internal controls conducted by an independent external firm covered banking and investment procedures, information technology security, financial reporting and staff benefits. It led to subsequent revisions to our policies and procedures⁴.

Income

Total income for the year was \$2,015 million, up 48% from \$1,363 million a year ago. Due to higher securities market turnover, our levy income increased by 52% to \$1,549 million in the current year. Our income from fees and charges increased by 8%, from \$143 million last year to \$154 million this year, mainly attributable to the receipt of more licensing application fees and takeovers and mergers document fees. We recorded higher net investment income as a result of the performance of our equity fund investments.

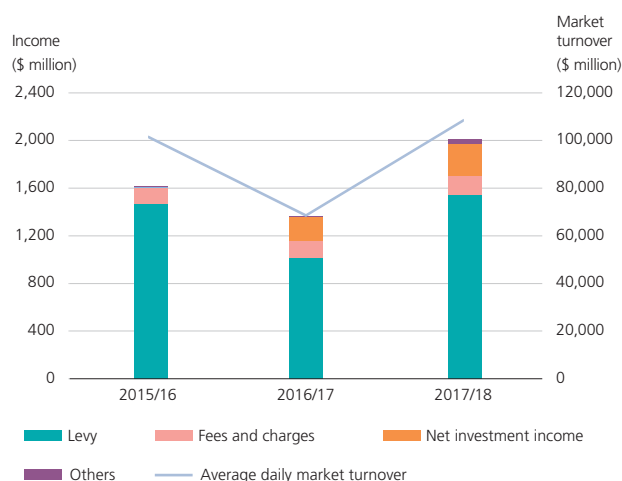
Income breakdown

	2017/18	2016/17	2015/16
Levies	76.9%	74.6%	90.8%
Fees and charges	7.6%	10.5%	8.1%
Net investment income	13.5%	14.4%	0.6%
Others	2%	0.5%	0.5%

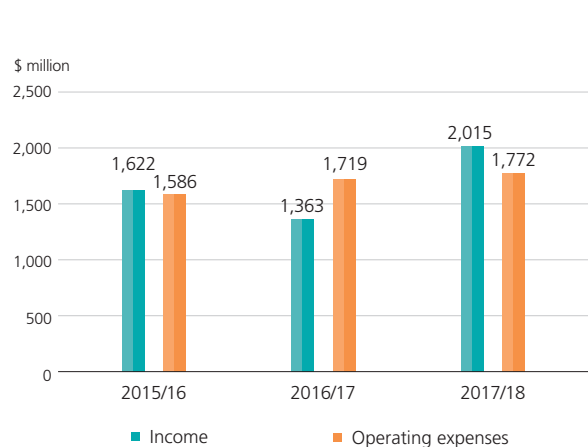
⁴ See Corporate Governance on pages 12-31.

Corporate Developments

Income vs market turnover (2015/16-2017/18)



Income and operating expenses (2015/16-2017/18)



Expenditure

The costs of our operations were \$1,772 million, \$181 million below our original budget of \$1,953 million. Over the past three years, our staff costs increased 29% while our regulatory work increased in both volume and complexity (see chart on page 95).

The ratio of average expenses to income for the past three years was 102%. In the same period, the average increase in expenses and income was 7% and 16% respectively.

Owing to the increase in income, we recorded a surplus of \$243 million for the year, compared to a deficit of \$356 million last year. As of 31 March 2018, our reserves stood at \$7.2 billion, of which \$3 billion was set aside for possible future acquisition of office premises.

Expenditure breakdown

	2017/18	2016/17	2015/16
Staff costs	72.4%	69.9%	69.3%
Premises and related expenses	14.2%	15.1%	15.6%
Other expenses	11.7%	12.3%	11.9%
Depreciation	1.7%	2.7%	3.2%

Finances

	2017/18	2016/17	2015/16	2014/15
Income (\$ million)	2,015	1,363	1,622	1,381
Expenses including depreciation (\$ million)	1,772	1,719	1,586	1,457
Surplus/(Deficit) (\$ million)	243	(356)	36	(76)

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 129, which comprise:

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

Our opinion

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

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (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.

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

- Transition as auditor
- Valuation and classification of investments

Transition as auditor

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

How our audit addressed the Key Audit Matter

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

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

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

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

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

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

Valuation and classification of investments

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

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

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

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

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

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

How our audit addressed the Key Audit Matter

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

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

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

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

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

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

Other information

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

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

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

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

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

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

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

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

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

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with Section 16(3) of the Securities and Futures Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAAs 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 HKSAAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

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

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

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

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

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

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

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

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

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 1 June 2018

Consolidated Statement of Profit or Loss and Other Comprehensive Income

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

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

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

Consolidated Statement of Financial Position

At 31 March 2018 (Expressed in Hong Kong dollars)

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

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

Carlson Tong
Chairman

Ashley Alder
Chief Executive Officer

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

Statement of Financial Position

At 31 March 2018 (Expressed in Hong Kong dollars)

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

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

Carlson Tong
Chairman

Ashley Alder
Chief Executive Officer

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

Consolidated Statement of Changes in Equity

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

	Initial funding by Government \$'000	Reserve for property acquisition \$'000	Accumulated surplus \$'000	Total \$'000
Balance at 1 April 2016	42,840	–	7,234,700	7,277,540
Transfer to reserve for property acquisition	–	3,000,000	(3,000,000)	–
Loss and total comprehensive income for the year	–	–	(355,640)	(355,640)
Balance at 31 March 2017 and 1 April 2017	42,840	3,000,000	3,879,060	6,921,900
Surplus and total comprehensive income for the year	–	–	242,864	242,864
Balance at 31 March 2018	42,840	3,000,000	4,121,924	7,164,764

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

Consolidated Cash Flow Statement

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

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

Analysis of the balance of cash and cash equivalents

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

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

Notes to the Consolidated Financial Statements

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

1. Status and principal activities

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

2. Income

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

- (a) levies collected by The Stock Exchange of Hong Kong Limited (SEHK) and Hong Kong Futures Exchange Limited (HKFE) on transactions recorded on the Exchanges at rates specified by the Chief Executive in Council.
- (b) fees and charges in relation to its functions and services according to the provision of subsidiary legislation.

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

3. Significant accounting policies

(a) Statement of compliance

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

The HKICPA has issued certain new and revised HKFRSs that are first effective or available for early adoption for the current accounting period

of the Group. Note 3(q) provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these financial statements.

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

(b) Basis of preparation

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

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

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

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

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

Notes to the Consolidated Financial Statements

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

3. Significant accounting policies (cont'd)

(c) Basis of consolidation

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

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

(d) Recognition of income

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

(i) Levies

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

(ii) Fees and charges

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

(iii) Interest income

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

(iv) Revaluation gain/loss

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

(e) Operating leases

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

(f) Employee benefits

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

(g) Fixed assets and depreciation

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

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

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

Notes to the Consolidated Financial Statements

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

3. Significant accounting policies (cont'd)

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

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

(h) Financial instruments

(i) Initial recognition

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

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

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

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

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

(ii) Fair value measurement principles

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

(iii) Derecognition

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

(iv) Offsetting

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

Notes to the Consolidated Financial Statements

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

3. Significant accounting policies (cont'd)

(i) Related parties

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

- (a) A person, or a close member of that person's family, is related to the Group if that person:
 - (i) has control or joint control over the Group;
 - (ii) has significant influence over the Group; or
 - (iii) is a member of the key management personnel of the Group.
- (b) An entity is related to the Group if any of the following conditions applies:
 - (i) the entity and the Group are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
 - (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
 - (iii) Both entities are joint ventures of the same third party.
 - (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
 - (v) The entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group.
 - (vi) The entity is controlled or jointly controlled by a person identified in (a).

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

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

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

(j) Translation of foreign currencies

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

(k) Debtors and other receivables

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

Notes to the Consolidated Financial Statements

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

3. Significant accounting policies (cont'd)

(l) Cash and cash equivalents

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

(m) Creditors and accrued charges

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

(n) Investment in subsidiaries

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

(o) Impairment

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

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

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

Notes to the Consolidated Financial Statements

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

3. Significant accounting policies (cont'd)

(p) Provisions and contingent liabilities

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

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

(q) Changes in accounting policies

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

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

4. Taxation

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

Notes to the Consolidated Financial Statements

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

5. Investment income

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

6. Other income

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

7. Staff costs and directors' emoluments

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

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

Notes to the Consolidated Financial Statements

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

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

Directors' emoluments included in the above comprised:

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

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

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

³ Retired having completed his appointment period of six years.

Notes to the Consolidated Financial Statements

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

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

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

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

Their emoluments are within the following bands:

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

Employee benefits

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

Notes to the Consolidated Financial Statements

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

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

Employee benefits (cont'd)

(a) ORSO Scheme

(i) General grade staff

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

(ii) Executive staff

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

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

(b) MPF Scheme

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

8. Other expenses

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

Notes to the Consolidated Financial Statements

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

9. Held-to-maturity debt securities

The Group and the SFC

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

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

Notes to the Consolidated Financial Statements

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

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

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

The pooled funds comprise mainly listed equity securities.

Notes to the Consolidated Financial Statements

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

11. Fixed assets

(a) The Group

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

Notes to the Consolidated Financial Statements

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

11. Fixed assets (Cont'd)

(b) The SFC

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

Notes to the Consolidated Financial Statements

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

12. Bank deposits and cash at bank

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

Reconciliation with the consolidated statement of financial position

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

13. Investments in subsidiaries

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

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

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

As at 31 March 2018, the investments in subsidiaries, which are stated at cost less any impairment losses, amounted to \$0.2 (2017: \$0.2). The balance is too small to appear on the statement of financial position which is expressed in thousands of dollars.

14. Creditors and accrued charges

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

15. Non-current liabilities

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

16. Debtors, deposits and prepayments

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

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

17. Initial funding by Government

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

Notes to the Consolidated Financial Statements

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

18. Capital commitments

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

19. Commitment to pay rents for offices

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

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

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

Notes to the Consolidated Financial Statements

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

20. Related party transactions

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

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

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

(b) Remuneration of key management personnel

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

21. Financial risk management and fair values

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

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

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

Notes to the Consolidated Financial Statements

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

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

(a) Credit risk

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

(b) Interest rate risk

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

Notes to the Consolidated Financial Statements

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

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

(b) Interest rate risk (Cont'd)

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

(c) Exchange rate risk

The Group's investment guidelines for our investment portfolio only allow investments in assets denominated in Hong Kong dollars, US dollars and renminbi. Exposure in renminbi should not exceed 5% of the investment portfolio. As the majority of the financial assets are denominated in either US dollars or Hong Kong dollars which are closely pegged, the Group was not exposed to significant foreign exchange risk at the end of the reporting period.

(d) Market risk

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

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

Notes to the Consolidated Financial Statements

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

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

(d) Market risk (Cont'd)

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

(e) Fair value measurement

(i) Financial assets measured at fair value

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

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

Notes to the Consolidated Financial Statements

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

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

(e) Fair value measurement (Cont'd)

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

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

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

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

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

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

Notes to the Consolidated Financial Statements

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

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

(e) Fair value measurement (Cont'd)

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

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

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

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

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

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

22. Sponsored unconsolidated structured entities

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

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

Notes to the Consolidated Financial Statements

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

22. Sponsored unconsolidated structured entities (Cont'd)

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

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

23. Funding and reserve management

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

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

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

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

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

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

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

Notes to the Consolidated Financial Statements

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

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

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

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

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

Investor Compensation Fund

Report of the Investor Compensation Fund Committee

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

Establishment of the Investor Compensation Fund

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

Financial statements

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

Members of the Committee

The members of the Committee during the year ended 31 March 2018 and up to the date of this report were:

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

Interests in contracts

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

Auditor

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

By order of the Committee

Keith Lui
Chairman

1 June 2018

Independent auditor's report To the Securities and Futures Commission

Opinion

What we have audited

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

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

Our opinion

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

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (HKSAAs) 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, 1 June 2018

Statement of profit or loss and other comprehensive income

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

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

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

Investor Compensation Fund

Statement of financial position

At 31 March 2018 (Expressed in Hong Kong dollars)

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

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

Carlson Tong
Chairman of the SFC

Ashley Alder
Chief Executive Officer of the SFC

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

Statement of changes in equity

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

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

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

Investor Compensation Fund

Cash flow statement

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

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

Analysis of the balance of cash and cash equivalents

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

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

Notes to the financial statements

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

1. Purpose, limitation and principal activity

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

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

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

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

2. Money constituting the Fund

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

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

3. Significant accounting policies

(a) Statement of compliance

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

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

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

Notes to the financial statements

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

3. Significant accounting policies (cont'd)

(b) Basis of preparation

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

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

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

(c) Recognition of income

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

(d) Translation of foreign currencies

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

(e) Financial instruments

(i) Initial recognition

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

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

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

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

Notes to the financial statements

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

3. Significant accounting policies (cont'd)

(e) Financial instruments (cont'd)

(ii) Fair value measurement principles

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

(iii) Derecognition

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

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

(iv) Offsetting

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

(f) Impairment

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

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

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

(g) Cash and cash equivalents

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

Notes to the financial statements

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

3. Significant accounting policies (cont'd)

(h) Other receivables

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

(i) Provision for compensation

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

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

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

(j) Creditors and accrued charges

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

(k) Provisions and contingent liabilities

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

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

Notes to the financial statements

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

3. Significant accounting policies (cont'd)

(I) Related parties

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

- (a) A person, or a close member of that person's family, is related to the Fund if that person:
 - (i) has control or joint control over the Fund;
 - (ii) has significant influence over the Fund; or
 - (iii) is a member of the key management personnel of the Fund.
- (b) An entity is related to the Fund if any of the following conditions applies:
 - (i) The entity and the Fund are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
 - (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
 - (iii) Both entities are joint ventures of the same third party.
 - (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
 - (v) The entity is a post-employment benefit plan for the benefit of employees of either the group or an entity related to the group.

- (vi) The entity is controlled or jointly controlled by a person identified in (a).
- (vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
- (viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the Fund.

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

(m) Changes in accounting policies

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

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

4. Taxation

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

Notes to the financial statements

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

5. Net investment income

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

6. Levy from SEHK and HKFE

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

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

7. ICC expenses

The SFC formed the ICC in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the SFO. The Fund is responsible for funding the establishment and operation of the ICC. For the year ended 31 March 2018, the ICC incurred costs of \$5,729,000 for its operations (2017: \$5,574,000) which were reimbursed by the Fund.

Notes to the financial statements

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

8. Provision for compensation

	\$'000
Balance as at 1 April 2016	1,412
Add: compensation expenses during the year ended 31 March 2017	476
Less: compensation write-backs during the year ended 31 March 2017	(294)
Less: compensation paid during the year ended 31 March 2017	(1,118)
Balance as at 31 March 2017 and 1 April 2017	476
Less: compensation paid during the year ended 31 March 2018	(476)
Balance as at 31 March 2018	–

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

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

The pooled fund comprises mainly listed equity securities.

Notes to the financial statements

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

10. Deposits with banks and cash at bank

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

11. Contributions from UECF and CECF

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

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

12. Material related party transactions

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

13. Financial risk management and fair values

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

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

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

(a) Credit risk

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

Notes to the financial statements

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

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

(b) Liquidity risk

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

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

(c) Interest rate risk

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

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

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

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

(d) Foreign currency risk

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

(e) Market risk

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

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

Notes to the financial statements

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

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

(e) Market risk (cont'd)

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

(f) Fair values of financial instruments

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

- Level 1 (highest level): fair values measured using quoted prices (unadjusted) in active markets for identical financial instruments.

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

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

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

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

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

Notes to the financial statements

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

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

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

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

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

Notes to the financial statements

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

14. Contingent liabilities

As at the date of this report, in addition to the provision made as described in note 8, there are 15 claims received for which currently there is insufficient information to determine the likely level of payment. The maximum liability in respect of these claims is \$2,375,000 (2017: \$2,558,000). This is determined based on the lower of the maximum compensation limit of \$150,000 per claimant or the amount claimed.

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

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

	Effective for accounting periods beginning on or after
HKFRS 9, <i>Financial instruments</i>	1 January 2018

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

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

Unified Exchange Compensation Fund

Report of the Securities Compensation Fund Committee

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

Establishment of the Unified Exchange Compensation Fund

Part X of the repealed Securities Ordinance (Chapter 333) established the Unified Exchange Compensation Fund (the Fund). However, when the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single Investor Compensation Fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. Up to 31 March 2018, the Fund transferred \$994,718,000 to the ICF. After settlement of all claims against the Fund and its other liabilities, the Securities and Futures Commission (SFC) will eventually transfer the remaining balance of the Fund to the ICF.

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

Financial statements

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

Members of the Committee

The members of the Committee during the year ended 31 March 2018 and up to the date of this report were:

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

Interests in contracts

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

Auditor

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

By order of the Committee

Keith Lui
Chairman

28 May 2018

Unified Exchange Compensation Fund

Independent Auditor's Report To the Securities and Futures Commission

Opinion

What we have audited

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

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

Our opinion

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

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (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.

Emphasis of matter

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

Other information

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

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

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

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

Responsibilities of directors of the SFC for the financial statements

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

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

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

Auditor’s responsibilities for the audit of the financial statements

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

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

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

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

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

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 28 May 2018

Unified Exchange Compensation Fund

Statement of profit or loss and other comprehensive income

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

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

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

Statement of financial position

At 31 March 2018 (Expressed in Hong Kong dollars)

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

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

Keith Lui
Chairman

Lee Kwok Keung
Committee Member

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

Unified Exchange Compensation Fund

Statement of changes in equity

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

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

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

Cash flow statement

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

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

Analysis of the balance of cash and cash equivalents

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

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

Unified Exchange Compensation Fund

Notes to the financial statements

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

1. Purpose, limitation and principal activity

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

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

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

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

After the Securities and Futures Ordinance (SFO) and its subsidiary legislation came into effect from 1 April 2003, a new single Investor Compensation Fund (ICF) was formed to ultimately replace the Fund and the Commodity Exchange Compensation Fund. After settlement of all claims against the Fund and its other liabilities, the SFC will eventually transfer the remaining balance of the Fund into the ICF. Claims for any defaults occurring after 31 March

2003 should be made against the ICF. If the sum of money in the Fund is not sufficient to meet its liabilities, the SFC shall pay into the Fund from the ICF the appropriate sum of money according to Section 242 of the SFO.

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

2. Money constituting the Fund

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

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

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

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

Notes to the financial statements

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

3. Significant accounting policies

(a) Statement of compliance

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

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

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

(b) Basis of preparation

Under the SFO, the Fund will continue in operation until all claims against it and all its liabilities have been settled. As the Fund will eventually cease operation, we have prepared these financial statements on a non-going concern basis. We expect that the operations of the Fund will be maintained until all claims and recoveries from liquidators in relation to the broker defaults that happened on or before 31 March 2003 have been fully settled. We have not provided for potential future claims and recoveries as these cannot be reliably estimated. We have also not provided in the financial statements for all expenses expected to be incurred subsequent to the end of the reporting period and up to the date operations will cease and these are estimated to be immaterial.

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

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

(c) Recognition of income

(i) Interest income

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

(ii) Recoveries

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

(iii) Replenishments from SEHK

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

Unified Exchange Compensation Fund

Notes to the financial statements

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

3. Significant accounting policies (cont'd)

(d) Impairment

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

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

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

(e) Cash and cash equivalents

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

(f) Creditors and accrued charges

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

(g) Provisions and contingent liabilities

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

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

Notes to the financial statements

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

3. Significant accounting policies (cont'd)

(h) Related parties

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

- (a) A person, or a close member of that person's family, is related to the Fund if that person:
 - (i) has control or joint control over the Fund;
 - (ii) has significant influence over the Fund; or
 - (iii) is a member of the key management personnel of the Fund.
- (b) An entity is related to the Fund if any of the following conditions applies:
 - (i) The entity and the Fund are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
 - (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
 - (iii) Both entities are joint ventures of the same third party.
 - (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
 - (v) The entity is a post-employment benefit plan for the benefit of employees of either the group or an entity related to the group.
 - (vi) The entity is controlled or jointly controlled by a person identified in (a).

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

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

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

(i) Changes in accounting policies

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

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

4. Taxation

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

Unified Exchange Compensation Fund

Notes to the financial statements

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

5. Creditors and accrued charges

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

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

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

According to Section 104 of the repealed Securities Ordinance, SEHK contributes to the Fund in respect of each trading right at the rate of \$50,000 per trading right. In the absence of claims or other provisions as set out in Section 106 of the repealed Securities Ordinance, the SFC must refund to SEHK the deposit within six months after the trading right was relinquished. During the year, deposits of \$2,700,000 in respect of 54 new trading rights were received from SEHK and deposits of \$250,000 in respect of 5 relinquished trading rights were refunded to SEHK. As at 31 March 2018, there were 15 trading rights in total of \$750,000 that have been relinquished but not yet refunded.

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

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

7. Contingent liabilities

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

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

8. Excess transaction levy from SEHK

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

9. Additional contributions from SEHK and the SFC

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

Notes to the financial statements

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

10. Other contributions

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

11. Contributions to Investor Compensation Fund

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

12. Material related party transactions

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

13. Financial risk management

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

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

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

Unified Exchange Compensation Fund

Notes to the financial statements

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

14. Replenishments from SEHK

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

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

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

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

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

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

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

	Effective for accounting periods beginning on or after
HKFRS 9, <i>Financial instruments</i>	1 January 2018

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

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

Breakdown of SFC activity data

Table 1 Authorised unit trusts and mutual funds – by type

	As at 31.3.2018		As at 31.3.2017	
	Number	Total NAV (US\$ million)	Number	Total NAV (US\$ million)
Bond	449 (22.7%)	569,700 (33.9%)	430 (21.9%)	466,096 ¹ (33.9%)
Equity	1,030 (52.1%)	787,889 (46.9%)	1,018 (51.9%)	638,848 (46.4%)
Diversified	172 (8.7%)	180,353 (10.7%)	162 (8.3%)	137,454 (10%)
Money market	45 (2.3%)	20,905 (1.2%)	44 (2.2%)	21,014 (1.5%)
Fund of funds	116 (5.9%)	22,897 (1.4%)	113 (5.8%)	19,865 (1.4%)
Index ²	157 (7.9%)	97,637 (5.8%)	182 (9.3%)	92,069 (6.7%)
Guaranteed	3 (0.2%)	105 (0%)	3 (0.2%)	127 (0%)
Hedge	1 (0.1%)	26 (0%)	2 (0.1%)	28 (0%)
Other specialised ³	5 (0.3%)	1,061 (0.1%)	7 (0.4%)	1,288 (0.1%)
Sub-total	1,978 (100%) ⁴	1,680,573 (100%)	1,961 (100%) ⁴	1,376,789 ¹ (100%)
Umbrella structures	237		242	
Total	2,215		2,203	

¹ These figures differ from those disclosed in the *Annual Report 2016-17* due to revised figures reported after the report's issuance.

² Including leveraged and inverse products.

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

⁴ These percentages do not add up to total due to rounding.

Table 2 Authorised unit trusts and mutual funds – by origin

	As at 31.3.2018				As at 31.3.2017		
	Umbrella funds	Sub-funds	Single funds	Total	Total NAV (US\$ million)	Total	Total NAV (US\$ million)
Hong Kong	144	534	80	758 (34.2%)	158,199 (9.4%)	735 (33.4%)	131,605 (9.6%)
Luxembourg	50	991	0	1,041 (47%)	1,105,904 (65.8%)	1,009 (45.8%)	910,351 (66.1%)
Ireland	26	211	2	239 (10.8%)	232,586 (13.8%)	256 (11.6%)	173,212 ¹ (12.6%)
United Kingdom	4	38	27	69 (3.1%)	109,340 (6.5%)	64 (2.9%)	90,987 (6.6%)
Mainland China	2	2	46	50 (2.3%)	20,855 (1.2%)	49 (2.2%)	17,056 (1.2%)
Other Europe	1	2	0	3 (0.1%)	137 (0%)	3 ² (0.1%)	94 ² (0%)
Bermuda	0	0	1	1 (0%)	173 (0%)	5 (0.2%)	217 (0%)
Cayman Islands	10	27	9	46 (2.1%)	9,033 (0.5%)	74 (3.4%)	11,546 (0.8%)
Others	0	0	8	8 (0.4%)	44,346 (2.6%)	8 ² (0.4%)	41,721 ² (3.0%)
Total	237	1,805	173	2,215 (100%)	1,680,573 (100%)³	2,203 (100%)	1,376,789¹ (100%)³

¹ These figures differ from those disclosed in the *Annual Report 2016-17* due to revised figures reported after the report's issuance.

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

³ These percentages do not add up to total due to rounding.

Breakdown of SFC activity data

Table 3 Takeovers activities

	2017/18	2016/17	2015/16
Codes on Takeovers and Mergers and Share Buy-backs			
General and partial offers under Code on Takeovers and Mergers	59	73	50
Privatisations	11	13	7
Whitewash waiver applications	41	37	51
Other applications under Code on Takeovers and Mergers ¹	289	365	323
Off-market and general offer share buy-backs	1	4	1
Other applications under Code on Share Buy-backs ¹	0	2	3
Total	401	494	435
Executive Statements			
Sanctions imposed with parties' agreement ²	5	4	1
Takeovers and Mergers Panel			
Meetings for review of Codes on Takeovers and Mergers and Share Buy-backs	2	0	0
Hearings before the Panel (disciplinary and non-disciplinary)	1	2	2
Statements issued by the Panel ³	1	2	4

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

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

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

Table 4 Breaches noted during on-site inspections

	2017/18	2016/17	2015/16
Failure to comply with Securities and Futures (Financial Resources) Rules	12	13	16
Failure to safekeep client securities	38	58	41
Failure to maintain proper books and records	33	36	34
Failure to safekeep client money	59	62	45
Unlicensed dealing and other registration issues	23	13	33
Breach of licensing conditions	7	8	10
Breach of requirements of contract notes/statements of account/receipts	62	85	69
Failure to make filing/notification	2	8	6
Breach of margin requirements	5	6	5
Marketing malpractices	0	1	0
Illegal short selling of securities	0	1	1
Dealing malpractices	3	11	2
Breach of Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ¹	320	441	388
Breach of Corporate Finance Adviser Code of Conduct	8	18	9
Breach of Fund Manager Code of Conduct	93	82	56
Breach of regulation of online trading	4	8	14
Non-compliance with anti-money laundering guidelines	175	201	223
Breach of other rules and regulations of the Exchanges ²	17	14	12
Breach of other rules and regulations of the Mandatory Provident Fund Schemes Authority	0	0	3
Internal control weaknesses ³	535	598	571
Others	80	91	146
Total	1,476	1,755	1,684

¹ Commonly related to risk management, record keeping, client agreements, safeguarding of client assets and management responsibilities.

² The Stock Exchange of Hong Kong Limited and Hong Kong Futures Exchange Limited.

³ Comprise deficiencies in management review and supervision, operational controls over the handling of client accounts, segregation of duties, information management, adequacy of audit trail for internal control purposes, among other weaknesses.

Breakdown of SFC activity data

Table 5 Successful prosecutions

Unauthorised activities

Defendants	Date of conviction	Fine (\$)	Investigation costs awarded (\$)
ETRADE Securities (Hong Kong) Limited	21.9.2017	40,000	109,857
Total		57,000	255,768

Provision of false/misleading representation to the SFC

Defendants	Date of conviction	Fine (\$)	Investigation costs awarded (\$)
YAN Ching Ching	27.7.2017	15,000	9,891
Total		35,000	38,482

Short selling

Defendants	Date of conviction	Fine (\$)	Investigation costs awarded (\$)
SHIU Kin Keung, Sammy	8.6.2017	35,000	19,435
Total		51,000	30,869

Disclosure of interests

Defendants	Date of conviction	Fine (\$)	Investigation costs awarded (\$)
CHEUNG Pui Lam	28.9.2017	27,000	6,881
Triken Limited	28.9.2017	12,000	6,881
Four Seas Mercantile Holdings Limited	11.5.2017	12,000	13,371
Total		56,500	35,895

Note: Cases with fines below \$10,000 are not shown in these tables.

Table 6 Other public disciplinary actions

Name	Date of action	Conduct	Action
HUI Lam Chiu	22.5.2017	Failures to ensure compliance with anti-money laundering regulatory requirements when processing third party fund transfers	Suspended for six months
WONG Ching Man, Bernie	22.5.2017	Forged a client's signature	Banned from re-entering the industry for four months
LI Bo	13.6.2017	Failure to disclose to his employer his personal trading account and beneficial interests in his friend's securities accounts	Banned from re-entering the industry for eight months
WU Biwei	19.6.2017	Failure to ensure compliance with anti-money laundering regulatory requirements when processing third party fund transfers	Suspended for six months
FOK Chi Kin	22.6.2017	Transferred proprietary information and client data from his former employer without authorisation	Banned from re-entering the industry for eight months
CHAN Wai Ling	26.7.2017	Accepted third party instructions to conduct unauthorised trades in clients' accounts	Suspended for 12 months
XU Tao	11.10.2017	Failure to comply with regulatory requirements of the SFC's Code of Conduct ¹ in recording client order instructions	Banned from re-entering the industry for four months
NG Chau	27.12.2017	Conducted unauthorised transactions in a client's account	Banned from re-entering the industry for six months
WU Hon Cheung	9.1.2018	Failure to keep proper records of a client's order instructions	Reprimanded and fined \$50,000
CHAN Wai Nun	22.1.2018	Transferred client data from his former employer without authorisation	Banned from re-entering the industry for six months

¹ The Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission.

Note: See Enforcement on pages 59-67 for details of the most significant disciplinary actions.

Breakdown of SFC activity data

Table 7 Other enforcement actions

	2017/18	2016/17	2015/16
S179 ¹ inquiries commenced	24	27	24
S181 ² inquiries commenced (number of letters sent)	261 (8,461)	301 (8,960)	286 (7,997)
S182 ³ directions issued	274	407	507
Rule 8 directions ⁴ issued	12	4	2
Show cause letters ⁴ issued	11	3	0
Cases with search warrants executed	22	34	31
Compliance advice letters issued	277	548	453
Criminal, Civil and Market Misconduct Tribunal (MMT) proceedings			
(a) Insider dealing			
Individuals/corporations summonsed (summons laid)	4 (7)	0 (0)	1(3)
Individuals/corporations involved in ongoing civil proceedings	13	16	13
Individuals/corporations involved in ongoing MMT proceedings	0	0	2
(b) Market manipulation			
Individuals/corporations involved in ongoing MMT proceedings	3	3	16
(c) Others			
Individuals/corporations summonsed (summons laid)	10 (47)	10 (46)	20 (107)
Individuals/corporations involved in ongoing civil proceedings	84	110	87
Individuals/corporations involved in ongoing MMT proceedings	13	26	14
Disciplinary enquiry			
Notices of Proposed Disciplinary Action ⁵ issued	29	49	35
Notices of Decision ⁶ issued (including S201 ⁷ agreement)	32	56	42
SFAT hearings			
Applications to SFAT	4	1	4
Applications/hearings completed	3	4	4

¹ Section 179 of the SFO gives the SFC the power to compel the production of records and documents from persons related to a listed company in relation to fraud or other misconduct.

² Section 181 of the SFO gives the SFC the power to require information from intermediaries about trading transactions, including the identity information of the ultimate clients, the particulars and instructions relating to the transactions.

³ Section 182 of the SFO gives the SFC the power to investigate SFO offences, market misconduct, fraud, misfeasance and disciplinary misconduct.

⁴ A Rule 8 direction is issued by the SFC pursuant to Section 8 of the Securities and Futures (Stock Market Listing) Rules, directing The Stock Exchange of Hong Kong Limited (SEHK) to suspend trading in the shares of a listed company on grounds that the market is misinformed, disorderly or unfair. A show cause letter is sent by the SFC to inform a listed company that it is minded to exercise its power under the aforesaid Rules to direct SEHK to suspend trading in the shares of the company, in the absence of a satisfactory explanation.

⁵ A notice issued by the SFC to regulated persons that it proposes to exercise its disciplinary powers, on grounds that they appear to be guilty of misconduct or not fit and proper.

⁶ A notice that sets out the SFC's decision and its reasons to take disciplinary action against regulated persons.

⁷ Section 201 of the SFO gives the SFC the power to resolve disciplinary proceedings by agreement when the SFC considers it appropriate to do so in the interest of the investing public or in the public interest.

Table 8 Statistical information and financial position of the Hong Kong securities industry¹

	As at 31.12.2017	As at 31.12.2016	As at 31.12.2015
Securities dealers and securities margin financiers	1,222	1,104	1,002
Active cash clients ²	1,320,332	1,289,563	1,259,868
Active margin clients ²	337,599	267,132	241,948
Active clients	1,657,931	1,556,695	1,501,816
Balance sheet	(\$ million)	(\$ million)	(\$ million)
Cash in hand and at bank ³	515,547	446,465	429,002
Amounts receivable from margin clients ⁴	205,977	171,633	145,307
Amounts receivable from clients and other dealers arising from dealing in securities	164,226	125,471	139,869
Proprietary positions	139,502	110,756	170,125
Other assets	312,152	224,196	205,673
Total assets	1,337,404	1,078,521	1,089,976
Amounts payable to clients and other dealers arising from dealing in securities	568,641	481,339	466,208
Total borrowings from financial institutions	170,411	86,731	111,265
Short positions held for own account	62,161	33,194	61,198
Other liabilities	164,033	143,941	146,989
Total shareholders' funds	372,158	333,316	304,316
Total liabilities and shareholders' funds	1,337,404	1,078,521	1,089,976
	12 months to 31.12.2017 (\$ million)	12 months to 31.12.2016 (\$ million)	12 months to 31.12.2015 (\$ million)
Profit and loss			
Total value of transactions ⁵	73,901,390	63,495,134	84,787,467
Net securities commission income	23,079	18,739	28,656
Gross interest income	17,259	14,026	12,203
Other income ⁶	107,079	98,344	106,044
Total operating income	147,417	131,109	146,903
Total overheads and interest expense	123,878	116,978	120,499
Total operating profit	23,539	14,131	26,404
Net profit on proprietary trading	11,667	6,893	16,799
Net profit for the period	35,206	21,024	43,203

¹ Data were extracted from the monthly financial returns submitted under the Securities and Futures (Financial Resources) Rules by corporations licensed for dealing in securities or securities margin financing. Figures reported by an overseas incorporated licensed corporation that carries out its principal business activities outside Hong Kong and operates in Hong Kong as a branch office were excluded.

² Active clients are clients for whom the licensed corporation is required to prepare and deliver monthly statements of account in respect of the relevant reporting month under the Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules.

³ Cash in hand and at bank include trust monies held on behalf of clients which totalled \$286,461 million (31.12.2016: \$248,066 million).

⁴ As at 31.12.2017, the average collateral coverage was 4.1 times (as at 31.12.2016: 4 times). It represents the number of times the aggregate market value of securities collateral deposited by margin clients over the total amount of margin loan due from these clients on a given date on an industry-wide basis.

⁵ The total value of transactions includes trading in equities, bonds and other securities in Hong Kong and overseas.

⁶ Comprises fund management fee income, corporate finance income, inter-company management fee income and others.

Committees, panels and tribunal

A number of committees and panels have been set up to advise the SFC on various matters and perform other functions as set out in their terms of reference. Their responsibilities and members are listed in this section. For information on the board committees and Executive Committee, see our discussion in Corporate Governance on pages 12-31.

SFC Committees

Advisory Committee

Advises the SFC on any matter of policy regarding the performance of its functions.

Chairman	
TONG Carlson, SBS, JP	
Members	
ALDER Ashley Ian, JP	KUNG Yeung Ann Yun-chi (from 1.6.2017)
Dr AU King-lun, MH	LEUNG Fung Yee Julia, SBS (from 1.6.2017)
BENNETT Prudence Ann (from 1.6.2017)	LI Brian David Man Bun, JP (to 31.5.2017)
Prof CHAN Kalok (from 15.1.2018)	LO Chi Wai (Peter LO) (to 31.5.2017)
CHAN Jeffrey Lap-tak	LUI Kei Kwong Keith (to 31.5.2017)
CHOI Fung Yee Christina (from 1.6.2017)	SHIPMAN Mark Graham
CHRISTIANSON Sun Wei	Dr TAN Yue-heng (from 1.6.2017)
DING Chen	TSANG Frederick Sui Cheong (to 31.5.2017)
DUHAMEL Vincent (to 31.10.2017)	WINTER Richard David
GRAHAM David	YIN Ke
HO Yin Tung Brian (to 31.5.2017)	
Number of meetings: 4	Average attendance rate: 70%

Academic and Accreditation Advisory Committee

Approves industry-based courses and examinations for the purpose of meeting the licensing competence requirements, endorses applications from professional bodies and tertiary institutions as recognised institutions for providing continuous professional training, advises the SFC on areas to study in the context of enhancing Hong Kong's position as an international financial centre and provides input for the development of industry-related courses and training programmes.

There were no circumstances which called for a meeting of the Committee during the year.

Chairman	
LEUNG Fung Yee Julia, SBS	
Members	
Prof CHENG Wui Wing Joseph	Prof LEUNG Siu Fai
CHOW Yuen Yee	PAN San Kong Terry
DAVIS Nigel	RONALDS Nick
Prof HOWELLS Geraint	YUEN Ho Duen Judith
KEE Nicholas Min Kwan	
Secretary	
TUNG Ka Shun Sam	
Number of meetings: 0	Average attendance rate: N/A

Committee on Real Estate Investment Trusts

Advises the SFC on general policy matters or regulatory issues that are related to the Code on Real Estate Investment Trusts (REITs), the overall market development of REITs, the property or securities market or investment management in Hong Kong or elsewhere, professional practices or guidelines that are involved in the operation of REITs, and fund investment or management in general.

During the year, the Committee met once to discuss policy issues in relation to REITs.

Chairman	
CHOI Fung Yee Christina	
Members	
BANKS Ian Robert	KWOK Lam Kwong Larry, BBS, JP
CHAN Duen Grace	LAU Chun Kong
Dr CHAN Ho Wah Terence	LO Chi Wai (Peter LO)
CHIANG Sui Fook Lilian	NG Yiu Fai (Curtis NG)
HO Edmund	WONG Chi Ming Sally
HO Yin Tung Brian	WU Thomas Jefferson, JP
Prof HUI Chi Man, MH	YEONG Wei Ming Alexandra (from 29.9.2017)
Secretary	
TSE Lok Min	
Number of meetings: 1	Average attendance rate: 80%

Disciplinary Chair Committee

Members are nominated by the Nominations Committee on the basis that they are duly experienced and legally qualified persons. Their role is to act as Chairman of the Takeovers and Mergers Panel in disciplinary proceedings under the Codes on Takeovers and Mergers and Share Buy-backs or of the Takeovers Appeal Committee on a case-by-case basis.

Members	
CHAN King Sang Edward, SC	SHIEH Wing Tai Paul, SC
JAT Sew Tong, SC, JP	WONG Yuk Lun Horace, SC, JP
LI Gladys Veronica, SC	

Fintech Advisory Group

Aims to broaden the SFC's understanding of the opportunities, risks and regulatory implications of the latest Fintech trends and developments.

During the year, the Group met twice to discuss a range of topics, such as the implication of sandboxes for start-ups, Fintech development in mainland China, blockchain technology and cryptocurrencies.

Chairperson	
LEUNG Fung Yee Julia, SBS (from 4.12.2017)	NOLENS Benedicte Etienne Noella G. (to 4.12.2017)
Ex-officio Members	
CHAN Man Cheong Rogers (to 15.8.2017)	CHIU Clara Ka Lai (from 4.12. 2017)
CHIONG Ron Sai Lung	
Members	
ADVANI Alokik Indru	LEWIS Antony
ARSLANIAN Henri-Kevork	LI Ting
BARBERIS Janos (to 28.2.2018)	MCCORMACK Urszula (from 1.3.2018)
GUZY Melissa C.	TAN Jessica (from 1.3.2018)
JOHNSTONE Syren	
Number of meetings: 2	Average attendance rate: 100%

Committees, panels and tribunal

Investor Compensation Fund Committee

Administers the Investor Compensation Fund and regulates its procedures in accordance with Part XII of the Securities and Futures Ordinance (SFO).

During the year, the Committee met once to consider the financial statements of the Fund and dealt with other administrative matters.

Chairman	
LUI Kei Kwong Keith	
Members	
ATKINSON Thomas Allan KO Teresa Yuk Yin, JP	LEE Kwok Keung Roger
Number of meetings: 1	Average attendance rate: 75%

Investor Compensation Company Limited Claims Committee

Reviews and determines investors' claims for compensation from the Investor Compensation Fund.

Chairman	
KO Teresa Yuk Yin, JP	
Members	
CHAN Lui Clara (from 8.8.2017) FUNG Wei Lung Brian LAM Sai Yuen Leo (to 7.8.2017) LO Dak Wai Alexandra, JP LUI Kei Kwong Keith	MAK Po Shuen Olivia MUKADAM Thrity Homi NG Oliver Tse Kuen TSO Pui Sze Teresa WAN Chi Yiu Andrew
Number of meetings: 1	Average attendance rate: 100%

Nominations Committee

Nominates members of the Takeovers and Mergers Panel, the Takeovers Appeal Committee and the Disciplinary Chair Committee.

Ex-officio Members	
ALDER Ashley Ian, JP (Chairman) CLARK Stephen Edward	HO Yin Tung Brian
Members	
TONG Carlson, SBS, JP	Dr WONG Ming Fung William, SC
Alternate members to CLARK Stephen Edward	
CHAN Yuk Sing Freeman KO Teresa Yuk Yin, JP LIU Chee Ming	MAGUIRE John Martin WEBB David Michael
Number of meetings: 0	Average attendance rate: N/A

Products Advisory Committee

The SFC may consult the Committee on a wide range of matters relating to the SFC Handbook for Unit Trusts and Mutual Funds, Investment-Linked Assurance Schemes and Unlisted Structured Investment Products, the SFC Code on MPF Products and the Code on Pooled Retirement Funds, overall market environment, industry practices and novel product features.

During the year, the Committee held a meeting to discuss the regulatory trends of retail fund management.

Chairman	
CHOI Fung Yee Christina	
Members	
BACCI Arthur John (to 11.9.2017)	LUO Jiabin
CHAN Duen Grace	LYU Hong (Sandra LU)
CHAN Siu Ping Chordio	Dr MALDONADO-CODINA Guillermo Eduardo (Bill MALDONADO)
Prof CHEUNG Yan Leung Stephen, BBS, JP	NORONHA Virginia (to 19.1.2018)
DASWANI Praveen Mohan (from 7.6.2017)	NOYES Keith Samuel
DING Chen	PANG Wai Sau Queenie
FUNG Ka Shing Bernard	SHIPMAN Mark Graham
HARRISON Stuart Edward (to 27.4.2017)	TSE Wai Ming (Timothy TSE)
HUI Mei Ying (Carol HUI)	TURL Graham Douglas (from 29.9.2017)
Dr HUNG Tin Yau Victor	TZATZAKIS Costa (Con TZATZAKIS)
LAW Shing Mui Alice	WONG Man Yee (Fanny WONG)
LECKIE Stuart Hamilton, OBE, JP	WONG Pui Ling Pauline
LEE Chi Kee Trevor	YANG Qiumei
LIU Yun Bonn	YEONG Wei Ming Alexandra (from 29.9.2017)
Secretary	
POON Wing Yee Loreen	
Number of meetings: 1	Average attendance rate: 77%

Public Shareholders Group

Advises on issues relating to shareholders' rights and interests.

During the year, the Group met four times and discussed many policy subjects, such as Hong Kong Exchanges and Clearing Limited's (HKEX) proposal on new board and weighted voting rights, The Stock Exchange of Hong Kong Limited's (SEHK) policies on back-door listing and the SFC's front-loaded approach to regulation for changing markets.

Chairman	
HO Yin Tung Brian	
Members	
BENNETT Prudence Ann	MA Sean
CHEN Yang Chung Roy	PARK Yoo Kyung
CHIA Chin-Ping	SCHLABBERS Manuel
HO John	van Rijn Arnout
LAU Ka Shi, BBS	WONG David (Nicolas)
LIU Hung Ho Ellis	WONG Yu Tsang Alex
LU Ting	
Number of meetings: 4	Average attendance rate: 57%

Committees, panels and tribunal

Securities Compensation Fund Committee

Administers the Unified Exchange Compensation Fund and regulates its procedures in accordance with Part X of the repealed Securities Ordinance which, under section 74 of Schedule 10 to the SFO, continues to apply to and in relation to any claim for compensation from the Fund made before 1 April 2003.

During the year, the Committee met once to consider the Fund's financial statements and to deal with other administrative matters.

Chairman	
LUI Kei Kwong Keith	
Members	
ATKINSON Thomas Allan KO Teresa Yuk Yin, JP	LEE Kwok Keung Roger MAK Po Shuen
Number of meetings: 1	Average attendance rate: 80%

SFC Dual Filing Advisory Group

Advises on treatment of cases and policy issues under the dual filing regime.

There were no circumstances which called for a meeting of the Group during the year. As there were no circumstances which called for a meeting of the Group in the last four years, the Board resolved to dissolve the Group on 22 January 2018.

Convener	
Executive Director, Corporate Finance, SFC	
Members	
CHAN Ching Chu JOHNSON Nicholas Regan LIU Kennedy Tat Yin	LUNG Hak Kau SOUTAR James Alexander WECHSLER Joshua
Number of meetings: 0	Average attendance rate: N/A

SFC (HKEC Listing) Committee

Exercises powers and functions equivalent to those of the Main Board and GEM Listing Committees of SEHK when actual or potential conflicts of interest arise between HKEX as the holding company of SEHK and the proper performance of SEHK's listing functions. In such cases, the relevant SEHK functions may be undertaken by the SFC.

There were no circumstances which called for a meeting of the Committee during the year.

Chairman	
Members present in each Committee meeting will elect a Chairman among themselves at the beginning of that meeting.	
Members	
ALDER Ashley Ian, JP ATKINSON Thomas Allan BROWN Melissa CHOI Fung Yee Christina LEE Carmelo Ka Sze, JP LEUNG Fung Yee Julia, SBS	LUI Kei Kwong Keith PHADNIS Dhananjay Shrikrishna TYE Philip Andrew YEUNG Eirene YOUNG Andrew John YU Ka Po Benita
Number of meetings: 0	Average attendance rate: N/A

SFC (HKEC Listing) Appeals Committee

Exercises powers and functions equivalent to those of SEHK's Listing Appeals Committee when actual or potential conflicts of interest arise between HKEX and the proper performance of listing functions by SEHK. In such cases, the relevant powers and functions may be exercised by the SFC.

There were no circumstances which called for a meeting of the Committee during the year.

Chairman	
Members present in each Committee meeting will elect a Chairman among themselves at the beginning of that meeting.	
Members	
AU Siu Cheung Albert, BBS	MA Xuezheng Mary
CHENG Wai Sun Edward, SBS, JP	TONG Carlson, SBS, JP
HUANG Lester, JP	Dr WONG Ming Fung William, SC
KO Teresa Yuk Yin, JP	Dr WONG Tin Yau Kelvin, JP
Number of meetings: 0	Average attendance rate: N/A

Share Registrars' Disciplinary Committee

Hears and determines disciplinary matters relating to share registrars in the first instance.

There was no circumstance which called for a meeting of the Committee during the year.

Chairman	
NORMAN David Michael	
Deputy Chairman	
KWOK Tun Ho Chester	
Members	
CHAN Henry	LO Dak Wai Alexandra
CHUI Ming Wai	TSAI Wing-chung Philip, JP
KONG YAO FAH Sew Youne (Marie-Anne KONG)	YUEN Ka Fai
LIN James C	
Number of meetings: 0	Average attendance rate: N/A

Share Registrars' Disciplinary Appeals Committee

Hears and determines appeals from Share Registrars' Disciplinary Committee. The Share Registrars' Disciplinary Appeals Committee for the hearing of each appeal case brought before it consists of members of the Share Registrars' Disciplinary Committee who did not preside or participate in the disciplinary hearing of that case.

There were no circumstances which called for a meeting of the Committee during the year.

Committees, panels and tribunal

Takeovers and Mergers Panel

Hears disciplinary matters in the first instance and reviews rulings by the Takeovers Executive¹ at the request of any party dissatisfied with such a ruling. Considers novel, important or difficult cases referred to it by the Takeovers Executive. Reviews, upon request by the SFC, the provisions of the Codes on Takeovers and Mergers and Share Buy-backs and the Rules of Procedure for hearings under the Codes and recommends appropriate amendments to the Codes and Rules of Procedure to the SFC.

During the year, the Panel met twice to discuss takeovers related policy matters. It also met once to consider non-disciplinary matters.

Chairman	
CLARK Stephen Edward	
Deputy Chairmen	
CHAN Yuk Sing Freeman KO Teresa Yuk Yin, JP LIU Chee Ming	MAGUIRE John Martin WEBB David Michael
Members	
BROWN Melissa CHAN Che Chung CHARLTON Julia Frances FU Yat Hung David IP Koon Wing Ernest LEE Kam Hung Lawrence, BBS, JP LEE Pui Ling Angelina, SBS, JP LIU Che Ning LIU Yun Bonn NORMAN David Michael NORRIS Nicholas Andrew	PARK Yoo Kyung SABINE Martin Nevil SCHWILLE Mark Andrew SHAH Asit Sudhir SOUTAR James Alexander VAS CHAU Lai Kun Judy WINTER Richard David WONG Wai Ming YU Ka Po Benita YUEN Ka Fai (Frank YUEN)
Number of policy meeting: 2	Average attendance rate: 69%
Number of non-disciplinary hearings: 1	Average attendance rate: N/A²
Number of disciplinary hearings: 0	Average attendance rate: N/A

¹ The Takeovers Executive refers to the Executive Director of the Corporate Finance Division of the SFC or his delegate.

² The Chairman will appoint not fewer than four panel members to participate in hearings, and the attendance of other members is not required.

Takeovers Appeal Committee

Reviews disciplinary rulings of the Takeovers and Mergers Panel at the request of an aggrieved party for the sole purpose of determining whether any sanction imposed by the Panel is unfair or excessive

There were no circumstances which called for a meeting of the Committee during the year.

Members	
BROWN Melissa	NORMAN David Michael
CHAN Che Chung	NORRIS Nicholas Andrew
CHAN Yuk Sing Freeman	PARK Yoo Kyung
CHARLTON Julia Frances	SABINE Martin Nevil
CLARK Stephen Edward	SCHWILLE Mark Andrew
FU Yat Hung David	SHAH Asit Sudhir
IP Koon Wing Ernest	SOUTAR James Alexander
KO Teresa Yuk Yin, JP	VAS CHAU Lai Kun Judy
LEE Kam Hung Lawrence, BBS, JP	WEBB David Michael
LEE Pui Ling Angelina, SBS, JP	WINTER Richard David
LIU Che Ning	WONG Wai Ming
LIU Chee Ming	YU Ka Po Benita
LIU Yun Bonn	YUEN Ka Fai (Frank YUEN)
MAGUIRE John Martin	
Number of meetings: 0	Average attendance rate: N/A

Independent Panels and Tribunal

Arbitration Panel under Securities and Futures (Leveraged Foreign Exchange Trading) (Arbitration) Rules

Resolves disputes in accordance with the Securities and Futures (Leveraged Foreign Exchange Trading) (Arbitration) Rules.

The panel received no new cases during the year and none were carried over from the previous year.

Chairman	
LAM Yuk Kun Lawrence	
Deputy Chairman	
LEE Pui Shan Rosita	
Members	
CHAN Kang Muk Woody (to 16.7.2017)	CHEUNG Tai Keung Jack
CHAN Siu-ping Chordio (from 17.7.2017)	LEUNG Tak-lap (from 17.7.2017)

Committees, panels and tribunal

Process Review Panel for the Securities and Futures Commission

Reviews and advises the SFC upon the adequacy of the SFC's internal procedures and operational guidelines governing the actions taken and decisions made by the SFC and its staff in the performance of its regulatory functions, including those related to the handling of complaints, licensing applications, inspection of intermediaries, product authorisation, exercise of investigation and disciplinary action, and corporate finance transactions (including the administration of Listing Rules).

Chairman	
Dr CHENG Mo Chi Moses, GBM, GBS, JP	
Members	
CHAN Kam Wing Clement	LEE Pui Shan Rosita
CHAN Lena	LEE Wai Wang Robert
DING Chen	Dr MAK Sui Choi Billy
Dr HU Zhanghong	TSANG Sui Cheong Frederick
KWOK Tun Ho Chester	YUEN Shuk-kam, Nicole
Ex-officio Members	
CHEUNG Kam-Wai, Christina, JP	TONG Carlson, SBS, JP

Securities and Futures Appeals Tribunal

Reviews a range of specified decisions made under the SFO by the SFC, the Monetary Authority or a recognised investor compensation company, and hears and determines any question or issue arising out of or in connection with any review.

Chairmen	
HARTMANN Michael John, GBS, former Non-Permanent Judge of the Court of Final Appeal	
KWOK Hing Wai Kenneth, SBS, SC, JP, former Deputy Judge of the Court of First Instance of the High Court	
TALLENTIRE Garry, former Deputy Judge of the Court of First Instance of the High Court	
Members	
CHAN Jeffrey Lap-tak	Professor LEUNG Siu-fai
CHAN Mei-bo Mabel	MAK Kwong-fai
CHAN Sze-oi Rebecca	Dr MAK Sui-choi Billy
CHEUNG Wai-sum Yvonne	MUH Yi-tong Anthony
CHEUNG Wing-han Ivy	NG Joo-yeow Gerry
CHIN Vincent	SHIH Edith
CHING Kim-wai Kerry	TSANG Chi-wai Roy
DATWANI Mohan	TSANG Kam-yin Wendy
DING Chen	TSE Wai-ming Timothy
HO Chiu-ping Dennis	WONG Hin-wing Simon
HUI Ming-ming Cindi	WONG Kwok-ching Jamee
KONG Chi-how Johnson	YUEN Miu-ling Wendy
LAI Hin-wing Henry	ZEE Helen

Glossary and abbreviations

Alternative liquidity pool (ALP)

An electronic system which allows crossing or matching of orders anonymously outside traditional exchanges without any pre-trade transparency. Also known as dark pool or alternative trading system.

Automated trading services (ATS)

Electronic facilities, outside of those provided by a recognised exchange company or clearing house, through which participants may trade, clear and settle securities, futures contracts and over-the-counter (OTC) derivatives.

Autorité des Marchés Financiers (AMF)

The authority that regulates participants and products in France's financial markets.

Boiler rooms

Frauds which may claim to be licensed and operate in a particular jurisdiction, and offer potentially worthless or false investment opportunities.

Central counterparty

Facilitates trading in derivatives and equities markets by acting as the buyer to every seller and the seller to every buyer, thereby ensuring the performance of open contracts.

China Interbank Bond Market (CIBM)

A Mainland over-the-counter market for trading debt instruments.

China Securities Regulatory Commission (CSRC)

A ministry-level agency directly under the State Council which regulates the Mainland's securities and futures markets.

Cold shoulder order

A sanction that prevents a person from accessing, directly or indirectly, the Hong Kong securities market for a stated period.

Cryptocurrency

A virtual currency which uses cryptography for security.

European Securities and Markets Authority (ESMA)

An independent authority which safeguards the stability of the financial system in the European Union by assessing risks to investors and markets, providing supervisory convergence and directly supervising credit rating agencies and trade repositories.

Exchange participant (EP)

A company with rights to trade on or through The Stock Exchange of Hong Kong Limited or Hong Kong Futures Exchange Limited.

Exchange-traded fund (ETF)

A passively managed index-tracking investment fund traded on a stock exchange.

Financial Dispute Resolution Scheme

An independent and impartial process administered by the Financial Dispute Resolution Centre whereby financial institutions in Hong Kong are required to resolve monetary disputes with their customers through mediation and arbitration.

Financial Stability Board (FSB)

An international body which promotes global financial stability through recommendations for, and the implementation and monitoring of, policy initiatives and international standards.

Financial technology (Fintech)

The application of information and communications technology to financial services, including digital payments, peer-to-peer financing, cybersecurity and data security, big data and data analytics, and distributed ledger technology.

Group of Twenty

An international forum for the governments and central bank governors from 19 of the world's major economies plus the European Union.

GEM

A stock market operated by Hong Kong Exchanges and Clearing Limited to provide fund-raising opportunities for small to mid-sized companies which may not meet the Main Board listing requirements. Formerly known as the Growth Enterprise Market.

Initial coin offering (ICO)

A fundraising mechanism whereby digital tokens or coins are offered to investors to fund a blockchain-related project.

International Organization of Securities Commissions (IOSCO)

A body of securities regulators worldwide which develops, implements and promotes adherence to internationally recognised standards for securities regulation.

Glossary and abbreviations

Investment-linked assurance scheme (ILAS)

A life insurance policy with investment elements that provides both insurance protection and investment options, usually through funds.

Leveraged and inverse products

Products structured as ETFs for public offering in Hong Kong. Leveraged products aim to deliver a daily return equivalent to a multiple of the underlying index return while inverse products aim to deliver the opposite of the daily return of the underlying index.

Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA)

A free trade agreement concluded by the Mainland and Hong Kong covering trade in goods and services as well as investment facilitation. Provisions include tariff agreements, preferential treatment for service providers, mutual recognition of professional qualifications, and enhanced cooperation in trade and investment facilities.

Mandatory provident fund (MPF)

An employment-based retirement savings scheme that requires regular mandatory contributions by employees and employers in Hong Kong.

Market Misconduct Tribunal (MMT)

An independent full-time body established under the Securities and Futures Ordinance which imposes civil sanctions against those it determines to be guilty of market misconduct.

Open-ended fund companies (OFC)

Collective investment schemes structured in corporate form with limited liability and variable share capital.

Over-the-counter derivatives (OTC derivatives)

Financial instruments that are usually traded directly between dealers and principals rather than via an exchange and whose values are derived from those of underlying assets.

Real estate investment trust (REIT)

A collective investment scheme constituted as a trust that invests primarily in real estate with the aim to provide returns to holders derived from rental income.

Regulatory technology (Regtech)

Technologies that assist regulators and firms to enhance processes for the collection, management and reporting of regulatory data, risk identification, risk weighting, surveillance and data analytics.

Rights issue

An offer to existing holders of a listed company's securities which enables them to subscribe to an additional number of securities in proportion to their existing holdings.

Securities and Futures Appeals Tribunal (SFAT)

A body established under the SFO to review specified decisions made by the SFC, the Monetary Authority or a recognised investor compensation company.

Securities and Futures Ordinance (SFO)

Together with subsidiary legislation, the law in Hong Kong relating to financial products and the securities and futures market and industry, as well as to their regulation and to other matters including the protection of investors.

Swiss Financial Market Supervisory Authority (FINMA)

The independent financial markets regulator in Switzerland.

Taiwan Financial Supervisory Commission

The authority responsible for the development, supervision, examination and regulation of the financial sector in Taiwan.

UK Financial Conduct Authority (FCA)

The conduct and prudential regulator for financial markets and financial services firms in the UK.

Undertakings for collective investment in transferable securities (UCITS)

A harmonised regulatory regime for the operation and sale of investment funds within the European Union.

Unit trust

A collective investment scheme constituted in trust form.

US Commodity Futures Trading Commission (CFTC)

The independent agency that regulates futures and options markets in the US.

US Securities and Exchange Commission (SEC)

The primary regulator of the US securities markets.

Whitewash waiver

A waiver of a party's obligation to make a mandatory offer to other shareholders of a company arising from an issue of new securities of that company.

**Contact
Information**

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