

SECURITIES AND

FUTURES

COMMISSION

ANNUAL REPORT

96/97

**CONFIDENCE IN THE MARKETS**



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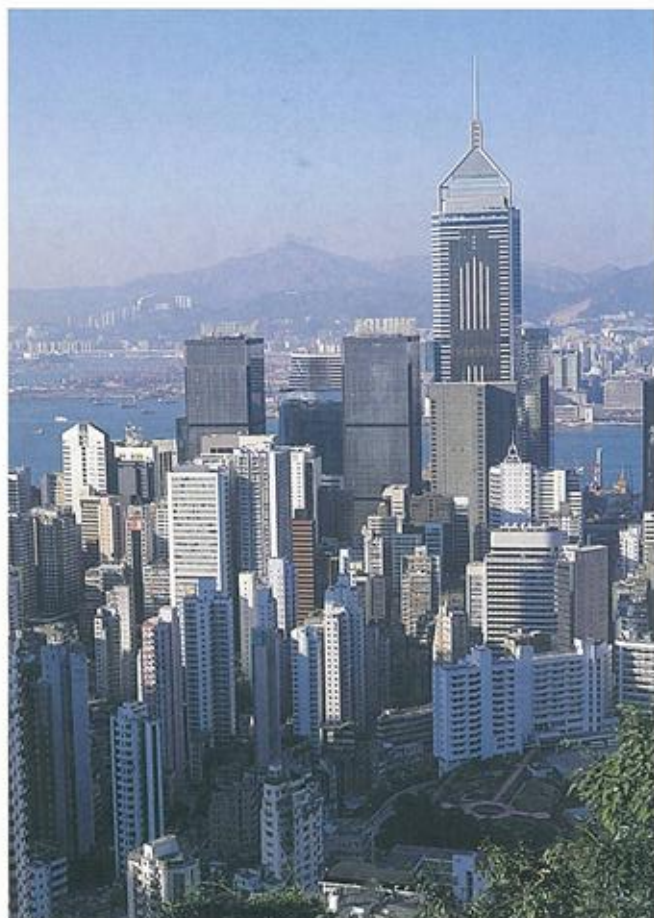
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## Mission Statement



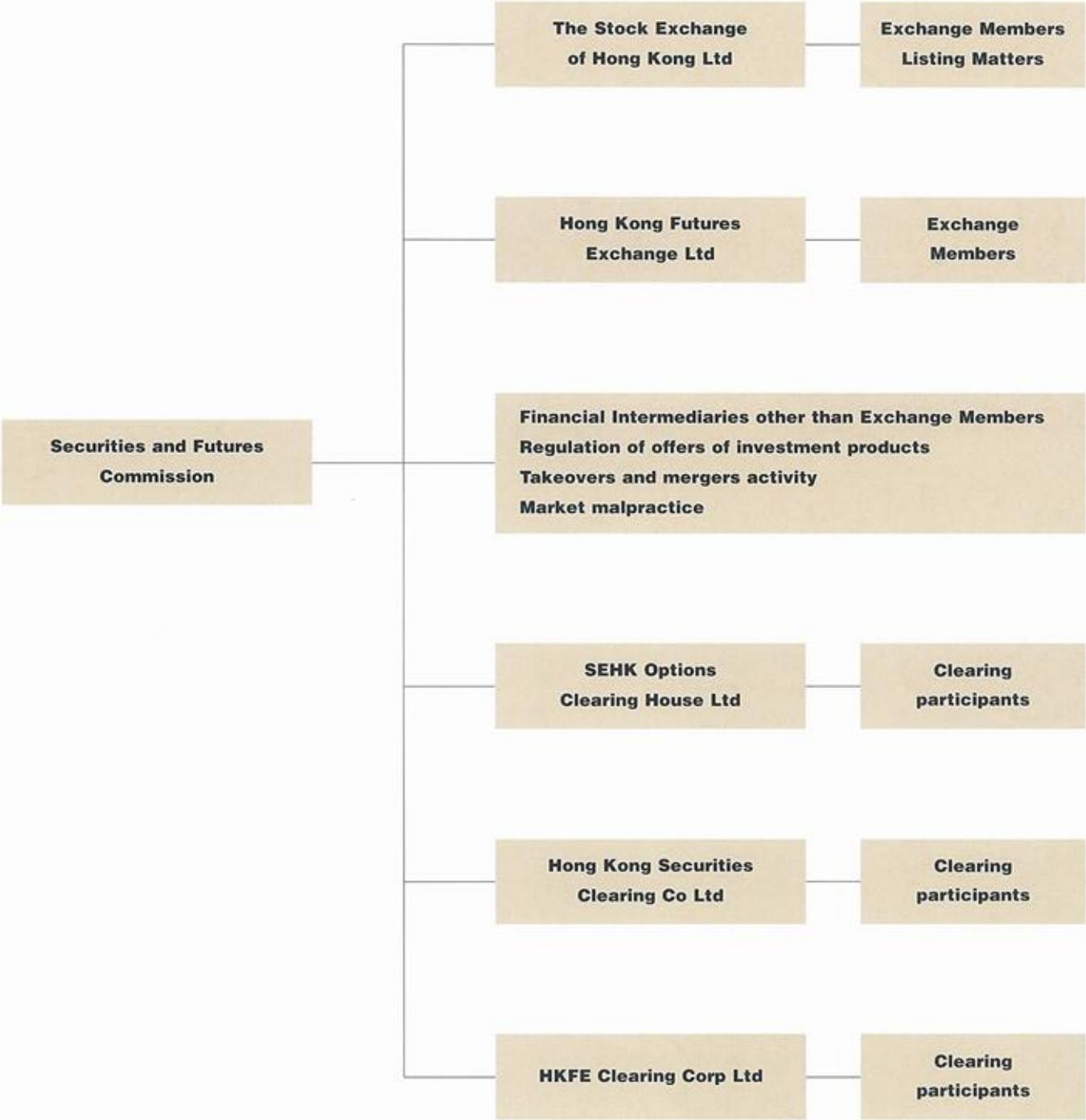
- *To promote user confidence in the efficiency and fairness of Hong Kong's securities and futures markets so as to support their continuing development, especially in relation to capital formation for the China region;*
- *To strike an appropriate balance between measures that maintain market integrity, measures that provide protection for investors, and measures that encourage market development and innovation;*
- *To effectively supervise the activities of the Exchanges, their Clearing Houses and market participants while facilitating sound business initiatives;*
- *To act firmly and fairly, while being adaptable, responsive and accessible to market participants and the investing public; and*
- *To consult on material changes to the regulatory environment and strive to ensure that full account is taken of Hong Kong's environment while paying due regard to international standards.*

## Corporate Strategic Objectives

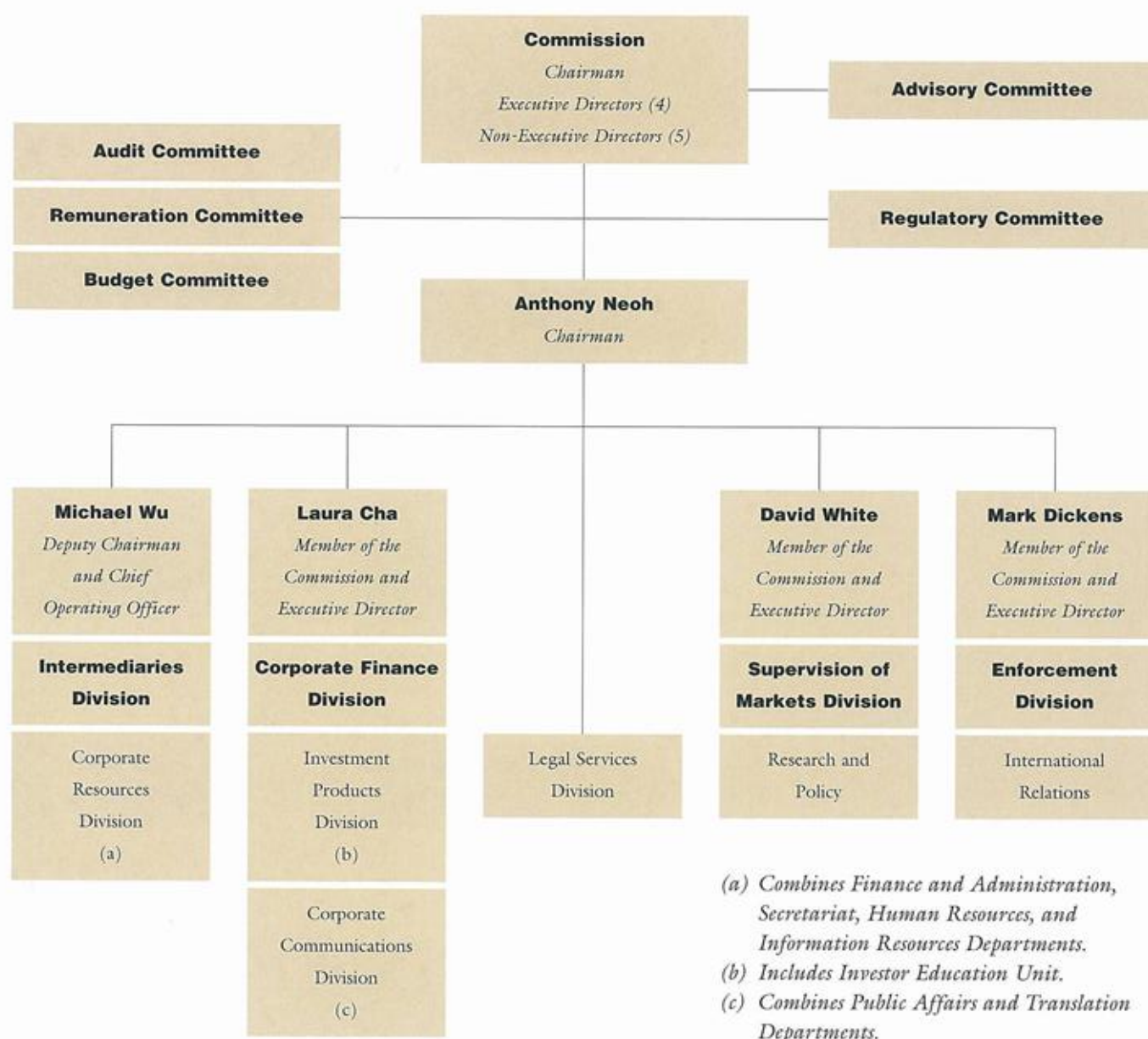
- To take all reasonable steps to ensure that Hong Kong markets are fair, efficient, competitive and informed;
- To develop and implement fair, concise and clear legislation, rules, regulations, guidelines and procedures;
- To provide expeditious, flexible and responsive services;
- To encourage the development of securities and futures markets in Hong Kong and the increased use of such markets by investors in Hong Kong and elsewhere;
- To ensure that Hong Kong's regulatory regime is structured and operated in a cost-effective and constructive manner;
- To encourage responsible and effective self-regulation by the Exchanges, the Clearing Houses, and other appropriate market bodies;
- To ensure the existence of effective risk management measures which are designed and operated in accordance with internationally recognised standards;
- To enhance the quality of our financial markets and to ensure that the expertise and skills of Hong Kong's intermediaries are consistent with both current and future market needs, and to accomplish this through the encouragement and facilitation of a comprehensive industry training programme;
- To maintain and enhance effective compliance and enforcement programmes, supported by adequate statutory powers;
- To enhance communication channels with market participants and to use these effectively;
- To develop and maintain mutually supportive relationships with the Government and other regulatory bodies in Hong Kong and overseas;
- To maintain a thorough understanding of and close rapport with the markets and to facilitate their development through (among other things) the introduction of new products, methodologies, systems and technology;
- To maintain contingency plans to deal with potential market disruptions;
- To promote proper understanding of and support for the SFC's role and objectives among SFC stakeholders; and
- To ensure SFC staff possess market knowledge and professional capabilities of consistently high quality to ensure an effective regulatory environment.



**Current Regulatory Structure**



## Organisation Chart



## Calendar of Significant Events

- 16 April 1996** Consultation Paper issued on a Draft of a Composite Securities and Futures Bill.
- 15 May 1996** Launch of SFC Web site on the Internet.
- 30-31 May 1996** SFC, Hong Kong Monetary Authority, Stock Exchange of Hong Kong and Hong Kong Futures Exchange hold joint seminar "Hong Kong: Towards a New Financial Era" in Beijing.
- 27 August 1996** New educational brochures published for retail investors.
- 28 August 1996** Consultation Paper issued on Review of Leveraged Foreign Exchange Trading Regulatory System.
- 29 August 1996** SFC and Investment Management Regulatory Organisation (IMRO) take joint disciplinary action against Jardine Fleming Investment Management and certain related companies for breaches of IMRO rules and SFC Code of Conduct.
- 18 September 1996** Memorandum of Understanding (MOU) on Mutual Assistance and Exchange of Information with Securities Commission of New Zealand.
- 18 September 1996** MOU on Mutual Assistance and Exchange of Information with Comision Nacional del Mercado de Valores of Spain.
- 19 September 1996** Anthony Neoh, QC, Chairman of the SFC, appointed Chairman of the Technical Committee of the International Organisation of Securities Commissions.
- 6 October 1996** Eight-part television series on the basics of "wise investing" premieres on TVB Jade and ATV Home.
- 24 October 1997** United States Securities and Exchange Commission Chairman Arthur Levitt visits SFC for discussions with Anthony Neoh.
- 28 November 1996** Consultation Paper issued on Management, Supervision and Internal Control Guidelines.
- 6 December 1996** Consultation Paper issued on Proposed Revisions to Draft Composite Securities and Futures Bill.
- 9 December 1996** Declaration of Cooperation on Investment Management with Luxembourg Monetary Institute.
- 16 January 1997** MOU with Monetary Authority of Singapore.
- 5 February 1997** Consultation Paper issued on Report of SFC Working Group on Automated Trading Systems.
- 24 February 1997** "Invest Wisely", a six-part television series on investor education, premieres on TVB Jade.
- 26 February 1997** MOU with Ontario Securities Commission.
- 7 March 1997** Consultation Paper issued on Review of the Financial Resources Rules.





### TOWARDS THE ERA OF THE SAR

*As this Annual Report is published, we will be very close to the time when China resumes the exercise of its sovereignty over Hong Kong. This historic occasion marks the beginning of a new era in the governance of Hong Kong. It has not therefore been a matter of surprise to me, since I took up my duties as Chairman of this Commission, that the one most frequent question that has been put to me by my regulatory colleagues elsewhere, by the constant stream of visitors to the Commission, and by the many people I come across in my overseas speaking engagements, has been whether the Hong Kong markets will continue to operate as before. My usual instant reply would be on these lines:*



“Why, of course, what makes you think that our markets will operate differently?” This invariably excites a torrent of comments and further questions, all of which belie one commonly shared perception, or as time will demonstrate, a common misconception. This perception is often stated in these terms: that given the best will in the world, the shadow cast by China will be so large that Hong Kong is likely to find itself hard pressed to regulate its markets with the high degree of autonomy that the Basic Law guarantees.

### **China building a market oriented financial infrastructure**

For persons who look at China from afar, that is an understandable perception. China has, after all, really committed itself to a market economy for less than twenty years. The capital markets in the mainland have had less than seven years of history. There is, by developed market standards, too thin a layer of regulation and the legal system still lacks predictability in resolving the many problems which all capital markets raise. The economy in the mainland is a giant and fast developing economy. There is no doubt that China will wield great economic power. What has not often been noticed, however, is that China has in recent years made definite inroads in building a market oriented financial infrastructure by reforming its banking and monetary system, by building up a viable securities regulatory structure both centrally and in the provinces, and by enacting relevant laws. In this process, China has absorbed a considerable body of proven ideas of financial regulation and market organisation. The value of Hong Kong as a conduit of ideas and the example of Hong Kong as a well regulated market cannot possibly have been overlooked by China.

### **Continuing interchange of ideas**

As is well known, there is a continuing interchange of ideas between Hong Kong and mainland financial regulators, exchange officials and market participants. The two Memoranda of Regulatory Co-operation signed between this Commission and the China Securities Regulatory Commission (CSRC) in 1993 and 1995 respectively, have proven their worth time and time again, as is shown by the improving awareness on the part of H-share companies of the need to cultivate good investor relations, by the improving standard of disclosure made by these companies, by the increasing number of H-share companies raising capital in Hong Kong and listing in our Stock Exchange, and by the help afforded to this Commission in a number of important investigations. In the past four years, the CSRC and the Commission have developed a partnership which has worked to the mutual benefit of our respective markets.

### **A quiet symbiosis**

What has also not been noticed is the quiet symbiosis that has long been a central feature in the developing economic relationship between the mainland of China and Hong Kong. Hong Kong has been the main direct investor in China since the beginning of the move towards a market economy. Hong Kong is also China's largest trading partner and its principal forum for raising capital for its state owned enterprises.

### **The fundamentals that make Hong Kong what it is**

The nature of symbiosis is that all parties in the process prosper. It is unnecessary to relate the figures which attest to the dramatic success of both economies in the past twenty years. Hong Kong's success in this symbiotic process lies in the simple fact that it is considered by domestic and international investors and market participants alike to be a good place to do business. While a good place to do business may mean a different set of things to different sets of businessmen, there are certain fundamentals which all businessmen require in a good business environment. The first is a system of government which is stable and ensures that rights and freedoms are equally protected for all, and where disputes are resolved with a high degree of predictability and with reasonable despatch. A close second is a set of economic and regulatory policies which do not impede the free internal and external flow of capital and ensure that markets will be allowed to thrive in a manner which is perceived to be fair, orderly and efficient. The third is a sufficient pool of talent and the availability of hard infrastructure such as internal and external communications, buildings, schools, hospitals and other social facilities,

and preferably, a hinterland for expansion. The fourth is the availability of market structures which give maximum assistance to capital formation.

There is obvious room for argument as to whether this list is exhaustive but there can be no argument that this is a list of requirements which all businessmen would want any good business environment to possess. An economy is only armed with these qualities over time and as these qualities are built up, business begets more business. Hong Kong undeniably possesses these qualities and, in abundance, as the growth of our markets have borne witness and as the appellation, Leading International Financial Centre of Asia, becomes increasingly applied to Hong Kong. The value of cultivating these qualities cannot be lost on any rational government, least of all the Government of China which has seen the country benefit from them.

### **Maintaining Hong Kong as an International Financial Centre**

The Basic Law of the Special Administrative Region of Hong Kong, drafted over a period of five years, with wide public consultation in Hong Kong, and passed by the National People's Congress in April 1990, in fact enshrined within the body of its 160 Articles specific provisions aimed at the preservation of the qualities which make Hong Kong what it is today. In particular, Article 109 states: "The Government of the Special Administrative Region shall provide an appropriate economic and legal environment for the maintenance of the status of Hong Kong as an international financial centre". While this represents recognition by China of the value of Hong Kong's many qualities, it also shows that China fully realises that it is up to the Government and the people of the SAR to maintain and develop them. That is why the duty imposed by Article 109 is expressed as a continuing one.

There is clearly no room for complacency for any international financial centre, least of all Hong Kong where there is no constraint whatsoever in the free flow of capital or trade. In a world where markets are no longer confined by geographic boundaries, the markets of Hong Kong are by definition world markets and by circumstance, subject to every competitive challenge that exists in the world today and in the future. That is why the Commission has committed itself to the three-pronged strategy set out in our 1996/1999 Corporate Plan. Our work programme since last year has been devoted to the following three strategic directions:

- Competitive Markets and Competitive Regulation.
- Development of the China Dimension.
- Development of Market Integrity.

### **Ensuring effective use of resources**

At the same time, we made special effort to ensure that the resources available to us are used to best effect. One of the central features of this year's work has been that with the modest increase of only 14 posts (which were only gradually filled during the year), we were able to achieve, by re-engineering our work processes and by working longer hours, a vast (almost 100%) improvement in output. In addition, we met our performance pledges to the full.

### **Growing intermediary population**

In the area of licensing, the year saw an increase in the total registrant population of 6.5%. As at the end of the year, the registrant population stood at 17,154 and we dealt with 4,940 applications for registration. As part of our information technology strategy, the project to enable electronic submission and imaging with full Chinese character input and display capability began and is expected to be completed by the last quarter of 1997. With the increase in the registrant population, we began to pioneer the use of risk-based supervision techniques resulting in our being able to conduct, with only minor increase in staffing resources, 323 routine inspections this year compared to the 157 we were able to conduct the previous year. In addition, we were able to conduct 30 special inspections.



### **Increasing Corporate Finance activity**

As the turnover in our Stock Exchange increased, so did mergers and acquisition activities. Our Corporate Finance Division considered a total of 612 applications compared with 338 in the previous year, some of great complexity and always necessitating rapid response.

### **Growing Fund Management Industry**

The fund management industry continues to grow strongly. As at the end of the year, the total number of authorised funds stood at 1,356, an increase of 11.2% over the previous year. We estimate that Hong Kong has some 195 fund management companies and certainly has the most international representation anywhere in Asia. We also expect that the industry will continue to grow strongly with the advent of the Mandatory Provident Fund and as the fund management industry grows both in the Mainland of China and Taiwan.

### **A competitive regulatory system**

Recognising that our markets have to remain competitive, we completed, in the course of the year, a review of the Leveraged Foreign Exchange Trading Regulatory System and consulted the market. At the time of writing, we also completed a review of the Financial Resources Rules and the Reporting System for OTC Derivatives Activities and market consultation was in progress. The objective of these exercises is to ensure that Hong Kong has a regulatory system which is international in outlook and application so that international market participants will themselves be equally confident in the Hong Kong markets as they are of any other major market in the world.

To ensure that our listed Derivative Warrants continue with added momentum, we approved major changes to the listing rules after an extensive review and market consultation. These new rules require additional attention to be paid to on-going risk management and disclosures. With a total of 296 derivative warrants listed during the year, Hong Kong has become one of the largest derivative warrant markets in the world.

We continued to work on greater transparency and higher efficiency in the markets, working in conjunction with the Stock Exchange and the Hong Kong Monetary Authority. Projects completed in this area include the amendment of the listing rules arising from the HKMA guidelines for further financial disclosure by banks, and projects underway include a comprehensive review of the mechanism for global offering of securities, a review of the Securities (Disclosure of Interests) Ordinance, a further review of the Stock Exchange's Code of Best Practice by directors, and a project for the simplification of prospectuses and announcements by listed companies. In the fund management area, two major initiatives on insurance-linked products came to fruition: the imposition of a cooling-off period of 21 days and the requirement for disclosure of surrender values.

The many rule changes in the Exchanges and clearing houses that we have considered in the past year attest to the seriousness with which our markets attend to the question of competitiveness. We should, however, be particularly mindful to the changes that technology can bring. With this in mind, we published and endorsed the Report of the Working Group on Automated Trading Systems. This Report sets out the potential changes in the horizon and the regulatory responses to these changes.

Any modern regulatory regime for the financial markets must give full recognition to the fact that there is always a community of interest between regulators and market practitioners in ensuring that there is confidence in the markets so that they may grow in size and sophistication. In keeping with this sentiment, the Commission embarked upon two major projects during the year. The first involved the publication of the Draft Securities and Futures Bill and the conduct of subsequent extensive public consultation. Altogether over 1,000 persons attended various seminars organised by the Commission and the Commission received written comments from some fifty persons and institutions. The result of the public consultation, together with the Commission's Response, was presented to the Government. At the time of writing, the Government has provided the Commission with a preliminary response but indicated that it was not possible to introduce a Bill in this legislative session. The Commission is nonetheless grateful to the Government for the efforts they have made in

studying the Bill and hopes that the Bill, which vastly improves the efficiency with which the law can be found and introduces much needed modernisation to laws made 23 years ago, will be introduced as soon as is practicable.

The other project is the consultation paper on Guidelines for Internal Control. Good internal control in the end means good business as a number of high profile international cases, such as Barings and Sumitomo, have shown. The Commission's many seminars attracted a very considerable number of practitioners. At the time of writing, the finalised Internal Control Guidelines, taking full account of the many helpful public comments, are ready for publication.

### **Internationalisation of our markets**

Last year saw yet a further increase in overseas capitalised firms setting up in Hong Kong. This further internationalisation of our markets has necessitated joint effort among regulators. During the year, we conducted joint inspections with the SEC of the United States and with IMRO and the SFA of the United Kingdom. Our bilateral relations with the regulators have thus also become important. During the year, we signed a further four Memoranda of Understanding with other regulators bringing the total number of such agreements to 24. In addition, we have 12 informal exchange of information agreements with other regulators.

With the globalisation of the markets there is obvious need for the Commission to take an active part in the formulation of international thinking on regulation. Accordingly, the Commission continued to commit itself fully to participation in the work of the International Organisation of Securities Commissions (IOSCO). During the year, I was elected to serve a two year term as Chairman of the Technical Committee of IOSCO. This Committee is responsible for formulating the regulatory thinking which spans the 16 most developed markets of the world. I am honoured to have been the first Chairman of an Asian Commission to serve as the Committee's chairman.

### **Investor Education**

Confidence in the markets require knowledgeable investors. This year saw the first flowering of our Investor Education Programme in which the public and the media have participated with enthusiasm. The six-part, half-hour-per-episode television series, produced in conjunction with Radio Television Hong Kong, was among the most highly rated public television programmes of the period when they were aired. We will continue to keep up the momentum in this area.

### **Developing the China Dimension**

Our work in developing the China dimension continues to focus on consolidating and improving our position as the principal market for capital formation by China outside of the mainland. Of the original 38 Chinese companies approved by the State Council for overseas listing, 29 have now done so and of these, 27 have chosen to list in Hong Kong. In December 1996, a further 38 companies were chosen by the State Council to list overseas. It is expected that following past experience a major proportion will list in Hong Kong. H-share companies have also begun to issue convertible bonds reflecting the increasing maturity of our debt market. In addition to H-share companies, there are some 46 Hong Kong-domiciled listed companies which are either directly or indirectly controlled by the Chinese Government. Hong Kong now, therefore, not only holds the position of being the principal market for raising capital but also represents the most liquid secondary market for listed shares in companies controlled by the Chinese Government outside of the mainland.

The number of mainland capitalised intermediaries have also increased and at the end of the year stood at 28, while at the time of writing, this number has increased to 42. Also during the year, the People's Bank and the CSRC continued to make progress in their draft regulations for fund management and sent fact-finding missions to study our experience in the regulation of the fund management industry. In addition to co-ordinating closely with the CSRC in the exercise of our respective functions, we also worked closely with other financial regulators, in particular the People's Bank and the State Administration for Foreign Exchange



to ensure that the mainland-capitalised intermediaries are able to continue to comply with both Hong Kong and mainland regulatory requirements.

At the same time, we felt it important to bring the Hong Kong financial markets and their regulatory ethos to the attention of the management of Chinese enterprises and of Government officials involved in the management of the economy. One major event was the "Hong Kong: Towards a New Financial Era" seminar in Beijing jointly organised by the Commission, the Hong Kong Monetary Authority, and the Hong Kong Stock and Futures Exchanges. In addition, we participated actively in seminars in China for prospective listing candidates.

### **Developing market integrity**

Market integrity is the cornerstone of confidence in our markets. As I have stressed in last year's annual report, market integrity can only be maintained by a culture of observance of the rules shared by all. We apply this philosophy at every level of our work. During each of the 350 inspections conducted by the Intermediaries Supervision Department last year, we took the opportunity to assist and counsel management in compliance. We believe that the counselling provided during these inspections has assisted the firms visited to provide a higher standard of service to their clients.

### **A remedial approach to enforcement**

Our Enforcement Division handled a total of 376 cases and completed 207 of them. In all cases, our basic approach has been remedial. In the Jardine Fleming case covered in this year's report, for example, we sought firstly to ensure that the investors concerned were compensated (and they were, by \$150 million), secondly to ensure that the firm was able in future to prevent a recurrence of the breach by mandating immediate improvements in procedures (and the Company complied) and an externally conducted compliance audit (which is now being conducted), and thirdly to ensure that those responsible for the breach were visited with appropriate penalties (and they were as severe as any that we have applied to other intermediaries involved in similar breaches).

While our approach has been remedial, we are determined to bring all breaches we can discover to book. We have thus been working closely with the Exchanges to improve our surveillance and detection ability. This is an area where we are still continuing to apply new techniques in information technology. An example of the inroads we have made in the use of technology may be found in our first successful prosecution of a case involving a breach of the Protection of Investors Ordinance through the Internet as a result of our Internet surveillance. Surveillance has also paid dividends in improved detection of insider trading and market manipulation cases. This year saw the completion of three insider trading cases before the Insider Dealing Tribunal. Four cases are being heard at the time of writing.

Another area where we are determined to protect investors lies in our civil cases. In the Canwell case, we obtained full restitution for all the margin clients of the failed Leveraged Forex Trader. We shall continue to pursue the Mandarin Resources case through the High Court until the minority shareholders are adequately compensated.

### **Confidence in the markets**

As we enter the era of the SAR, we can note with some pride the fact that our markets are vital and currently enjoy the confidence of both international and domestic investors. However, there is no room for complacency. The constitutional arrangements in the era of the SAR, far from impeding us, in fact provide us with the institutional building blocks to continue to develop Hong Kong's status as an international financial centre. More than ever before, we hold our future in our own hands.

Anthony Neoh, QC, JP  
*Chairman*

## Directors of the Commission

### Executive Directors

ANTHONY FRANCIS NEOH, QC, JP *Chairman*

Queen's Counsel, 1990; Member, Hospital Authority, 1990 - 1995; Vice-Chairman, Council of the Chinese University of Hong Kong, 1995; Formerly, Member of the Council, Hong Kong Stock Exchange, 1991 - 1994; Practice at the Hong Kong Bar, 1979 - 1995 and California Bar, 1984 - 1995; Administrative Officer, Hong Kong Government 1969 - 1979.

MICHAEL WU WAI CHUNG, JP *Deputy Chairman and Chief Operating Officer*

Formerly Executive Director, SFC, 1992 - 1994 (Intermediaries); Senior Director of Licensing and Supervision of Markets, SFC, 1989 - 1992; Administrative Officer, Hong Kong Government, 1982 - 1989; Trade Officer, Hong Kong Government, 1972 - 1982.

LAURA M CHA, JP *Executive Director (Corporate Finance)*

Council Member, Hong Kong University of Science and Technology; Formerly Senior Director of Corporate Finance, SFC, 1991 - 1994; Attorney, Coudert Brothers, Hong Kong, 1985 - 1990; Pillsbury, Madison and Sutro, San Francisco, 1982 - 1984.

DAVID J WHITE, JP *Executive Director (Supervision of Markets)*

Formerly Director, Derivatives and Market Development, Australian Stock Exchange, 1992 - 1995; Executive Director, Operations, County Natwest Investment Management Limited (London), 1990 - 1992; Group Finance and Operations Director, County Natwest Australia Limited; 1986 - 1990; Director and Group General Manager, Dominguez Barry Samuel Montagu (Sydney), 1983 - 1986; General Manager, Citicorp Australia Group, 1977 - 1983.

MARK DICKENS, *Executive Director (Enforcement) (from 1 January 1997)*

Formerly, Senior Director of Corporate Finance, 1991-1996; various senior positions with Australian National Companies and Securities Commission, including General Counsel and Senior Director, Market Supervision, 1980-1991.

GERARD J McMAHON, JP *Executive Director (Enforcement) (to 31 December 1996)*

Barrister; Formerly Chief Counsel, SFC, 1989 - 1992; Senior Assistant Crown Solicitor (Commercial), Attorney General's Chambers, Hong Kong 1986 - 1989.



*Executive Directors (from left to right): Gerard McMahon  
Michael Wu, Mark Dickens, Anthony Neoh, David White and  
Laura Cha*



**Non-Executive  
Directors**

RODERICK E D CHALMERS

Chartered Accountant; Managing Partner, Coopers & Lybrand Hong Kong.

RONNIE C CHAN

Chairman, Hang Lung Development Group; Director, Morningside/Springfield Group; Non-Executive Director of several publicly listed companies, including Standard Chartered PLC and Enron; Vice President, Real Estate Developers Association of Hong Kong; Chairman, Asia Society - Hong Kong Centre; Council Member, Hong Kong University of Science and Technology; Chairman, HK-US Economic Cooperation Committee.

THE HON VINCENT CHENG HOI CHUEN, OBE, JP

Executive Director, Hongkong and Shanghai Banking Corporation; Managing Director, Hang Seng Bank Limited; Member, Executive Council; Hong Kong Affairs Adviser to the PRC; Chairman, Mandatory Provident Fund Advisory Board; Member, Economic Advisory Committee; Member, Industry and Technology Development Council.

HENRY H L FAN

Managing Director, CITIC Pacific Limited; Deputy Chairman, Cathay Pacific Airways Limited; Director, Hong Kong Telecommunications Limited and China Light & Power Company Limited; Member, Services Promotion Strategy Group; Member, Advisory Committee on Corruption; Member, Standing Committee on Company Law Reform; Member, University Grants Committee and the Council of the City University of Hong Kong.

ROBERT G KOTEWALL, QC

Queen's Counsel, 1989; Chairman, Occupational Retirement Schemes Appeal Board; Member, Standing Committee on Company Law Reform; Member, Subcommittee on Civil Evidence of Law Reform Commission; Member, Fight Crime Committee; Member, Supreme Court Rules Committee; Member, Appeal Board on Public Meetings and Processions; Member, Witness Protections Appeal Board; Member, Banking Advisory Committee; Member, Medical Council.



*Non-Executive Directors (from left to right): Ronnie Chan, Robert Kotewall, Roderick Chalmers, Henry Fan and Vincent Cheng*

### FUNCTIONS

*1.1 Under the Ordinances administered by the SFC, securities, futures and leveraged foreign exchange intermediaries are required to register with or be licensed by the SFC before they can carry on business in Hong Kong. These requirements enable market participants generally, and investors in particular, to have confidence that the people and organisations with which they deal are fair, efficient, honest and financially sound.*

*1.2 The Ordinances also impose ongoing requirements on registered/licensed*

*intermediaries, including maintenance of adequate capital, proper books and records, segregation and safe custody of client assets, and submission of annual returns and accounts to the SFC.*

*1.3 The Intermediaries*

*Division is responsible for ensuring that registered/licensed intermediaries meet the initial and ongoing requirements under the Ordinances. The Licensing Department administers the registration/licensing requirements, while the Intermediaries Supervision Department supervises compliance with the provisions of the relevant Ordinances.*



**Michael Wu** is Deputy Chairman, Chief Operating Officer and Executive Director responsible for the Intermediaries Division, which comprises the Licensing and Supervision of Intermediaries Departments. He is also responsible for the Corporate Resources Division.



## Licensing Department

1.4 In order to obtain or maintain a registration with the SFC, a person must satisfy the SFC that he is a "fit and proper" person.

1.5 In assessing whether a person is fit and proper, the SFC is required to take into account :

- his financial status;
- his educational or other qualifications and experience relevant to the nature of the functions he intends to perform;
- his ability to perform such functions efficiently, honestly and fairly; and
- his reputation, character, financial integrity and reliability.

1.6 In the case of a limited company seeking a

registration or licence, the fit and proper test will be applied to all its directors, substantial shareholders and related persons.

## Applications for Registration under the Securities Ordinance and Commodities Trading Ordinance

1.7 A total of 4,940 applications for registration were received by the SFC during the year. Together with those carried forward from the preceding year, a total of 4,359 approvals were granted, 34 applications were refused and 321 applications were withdrawn. A detailed breakdown by category of these data is at Table 1.

Table 1  
**Application for Registration**  
for the period 1 April 1996 to 31 March 1997

Securities Dealers	Individual	Corporation	Partnership	Dealing Director	Representative	Total	
Applications received	0	58	0	322	1,965	2,345	(1,929)
Applications granted	0	41	0	250	1,741	2,032	(1,932)
refused	0	1	0	9	9	19	(3)
withdrawn	0	6	0	52	72	130	(111)
Securities Investment Advisers	Individual	Corporation	Partnership	Investment Adviser Director	Representative	Total	
Applications received	3	75	1	311	1,000	1,390	(1,348)
Applications granted	0	60	0	274	921	1,255	(1,330)
refused	0	1	0	4	2	7	(3)
withdrawn	0	14	0	53	34	101	(99)
Commodity Dealers	Individual	Corporation	Firm	Accredited Dealer	Representative	Total	
Applications received	0	16	0	107	901	1,024	(1,247)
Applications granted	0	11	0	85	819	915	(1,263)
refused	0	0	0	2	4	6	(3)
withdrawn	0	4	0	21	43	68	(132)
Commodity Trading Advisers	Individual	Corporation	Firm	Accredited Adviser	Representative	Total	
Applications received	1	27	0	60	93	181	(160)
Applications granted	0	23	0	52	82	157	(168)
refused	0	1	0	1	0	2	(1)
withdrawn	0	2	0	9	11	22	(34)

Note: 31 March 1996 data in brackets

Intermediaries registered under the Securities Ordinance (SO) and Commodities Trading Ordinance (CTO)

1.8 As at 31 March 1997, a total of 17,154 intermediaries were registered with the SFC. A detailed breakdown by category is in Table 2.

1.9 Table 3 shows the number of institutions declared to be exempt dealers and exempt investment advisers by the SFC. During the year, 2 applications for declaration as exempt dealer and 2 applications for declaration as exempt investment adviser were received by the SFC. Three institutions were declared to be exempt dealers and 1 exempt investment adviser application was withdrawn. Five exempt dealer and 1 exempt investment adviser declarations were revoked.

### Applications for licence under the Leveraged Foreign Exchange Trading Ordinance (LFETO)

1.10 During the year, the SFC received 1 trader and 286 representative applications. Three trader licences and 601 representative licences were granted, and 1 representative application was refused. One trader application and 476 representative applications were withdrawn. A detailed breakdown by category is in Table 5.

1.11 During the year, the SFC also completed the processing of the remaining 2 applications from the batch of 45 submitted by then existing traders, including Emperor International Exchange (Hong Kong) Company Limited, the largest trader in Hong Kong.

Table 2  
Number of Registered Securities and Commodities Intermediaries  
as at 31 March 1997

	Securities			Commodities			Grand Total	
	SEHK Members	Total		HKFE Members	Total			
Dealers, comprising	1,355	1,850	(1,830)	398	475	(462)	2,325	(2,292)
Individuals	142	153		-	-			
Corporations	349	524		126	155			
Partnerships	3	3		0	0			
Directors	861	1,170		272	320			
Dealer's Representatives	5,650	7,369	(6,781)	2,597	2,952	(2,777)	10,321	(9,558)
Advisers, comprising		1,648	(1,632)		292	(275)	1,940	(1,907)
Individuals		30			4			
Corporations		589			119			
Partnerships		1			1			
Directors		1,028			168			
Adviser's Representatives		2,405	(2,230)		163	(125)	2,568	(2,355)
		13,272	(12,473)		3,882	(3,639)	17,154	(16,112)

Note: 31 March 1996 data in brackets.

Table 3  
Number of Exempt Dealers and Exempt Investment Advisers  
as at 31 March 1997

Exempt Dealers, comprising	225	(227)
Licensed Banks	99	
Restricted Licence Banks	25	
Deposit-taking Companies	32	
Unit Trust Managers	20	
Trustee Companies	12	
Others	37	
Exempt Investment Advisers	46	(47)

Note: 31 March 1996 data in brackets

Table 4  
Number of Licensed Leveraged Foreign Exchange Traders  
and Representatives  
as at 31 March 1997

Trader		
Discretionary A/C	12	(15)
Non-Discretionary A/C	7	(12)
Introducing Agent	3	(5)
Trader's Representative		
Responsible Director	52	(74)
Representative	1,267	(1,366)
Introducing Agent	30	(47)
Grand Total	1,371	(1,519)

Note: 31 March 1996 data in brackets

1.12 The licence to Emperor International Exchange was granted on 29 January 1997 on the basis of a range of measures adopted, and a number of undertakings provided by the company. These include a revamp of its organisational and management structure thereby ensuring operational independence, strengthening its internal control and compliance regime, and engaging an independent firm of auditors to conduct semi-annual focused compliance audits for a period of two years. These measures and undertakings are the most onerous in the history of the SFC.

1.13 As at 31 March 1997, the total number of licensed traders and representatives were 22 and 1,349 respectively. A detailed breakdown by category is in Table 4.

1.14 During the year, the SFC received notifications from 3 corporations that they met the criteria for exemption from licensing as leveraged foreign exchange traders. As at

31 March 1997, there were 36 corporations falling within the qualifying class under the Exemption Rules.

## Trends

1.15 As indicated in Tables 1 and 2, the number of applications for registration under the Securities Ordinance and Commodities Trading Ordinance received by the SFC during the year has increased by 256 to 4,940 and the size of the registrant population has grown by approximately 6.5% over the preceding year. While the number of applications received from business entities has declined by 18.5%, the number of applications for registration as representatives has increased by about 9.5%. This is a continuation of the trend, which began a few years ago, of

Table 5

### Application for Licence

for the period 1 April 1996 to 31 March 1997

Leveraged Foreign Exchange Traders	Trader Discretionary A/C	Trader Non-Discretionary A/C	Trader Introducing Agent	Trader's Representatives	Introducing Agent's Representatives	Total	
Applications received	0	0	1	257	29	287	(1,006)
Applications granted	2	0	1	580	21	604	(1,328)
refused	0	0	0	1	0	1	(5)
withdrawn	1	0	0	470	6	477	(728)

Note: 31 March 1996 data in brackets

Figure 1

### Total Registrants - Securities and Commodities 1989 - 1997 (as at 31 March)

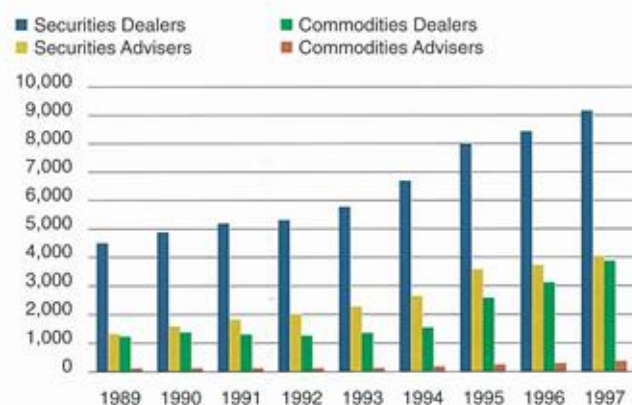
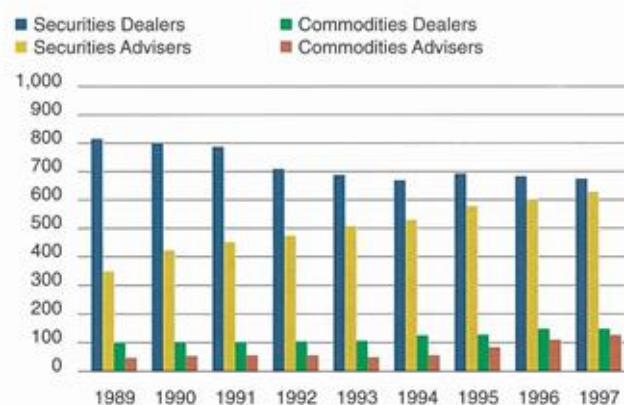


Figure 2

### Number of Dealing and Advising Business 1989 - 1997 (as at 31 March)





business entities further consolidating their operations in Hong Kong. A comparison of the number of accredited individuals per registered business entity provides a clearer picture. The ratio of 9.3 : 1 as at 31 March 1996 has increased to 9.9 : 1 as at 31 March 1997.

1.16 The trend cited above is more obvious in the securities industry, where further consolidation and convergence were seen. Sole proprietorship businesses (whose population has dropped from 178 as at 31 March 1996 to 153 as at 31 March 1997) were increasingly being incorporated or acquired by larger firms. The number of registered persons per securities dealing firm increased from 13 per firm to 14 per firm on a year-end basis.

1.17 The year has also seen increasing participation in Hong Kong by intermediaries from within Asia, especially the People's Republic of China and South East Asia (see Table 6). Apart from reflecting the importance of Hong Kong as a premier regional financial centre, this trend is also indicative of the continuing development of the region as an economic powerhouse and the importance of financial services as a component of this development.

1.18 Following world-wide trends, the leveraged foreign exchange industry continued to undergo a contraction. As indicated in Table 4, the population of both traders and trader's representatives declined significantly over the preceding year, with the number of licensed traders declined from 32 to 22 and that of representatives from 1,487 to 1,349.

1.19 Several factors have contributed to the decline in this industry, including:

- the impact of regulation, particularly the minimum margin requirements, the prohibition of credit for margin deposits, and the ban against cold calling/hawking etc., which has prevented the product from being marketed to persons who could not afford the risks involved, e.g. housewives, the young and the elderly;
- migration of the lower end of the business to Macau;
- the ban imposed by the People's Republic of China authorities on financial futures, including leveraged forex, which has deprived the industry of a significant number of big-ticket clients; and
- increased competition from Authorised Institutions, particularly the large retail banks which have entered the retail end of the market in a big way since the introduction of the LFETO.

## Monitoring

1.20 In addition to the initial vetting of intermediaries at the entrance level, the Licensing Department also monitors the continuing fitness and properness of its registered and licensed persons. This function includes the maintenance and updating of a database on its registrant/licencee population. To this end, the Department commenced a

Table 6  
Foreign-Capitalised Dealers

Jurisdiction	Securities						Commodities					
	1992	1993	1994	1995	1996	1997	1992	1993	1994	1995	1996	1997
Australia	5	7	6	5	5	3	0	0	0	0	0	0
Bermuda	1	3	7	6	0	0	0	1	2	2	0	0
British Virgin Islands	0	1	5	8	0	0	0	0	1	1	0	0
Canada	7	6	7	7	10	7	1	1	1	1	1	1
Cayman Islands	1	2	2	2	0	0	2	1	1	1	0	0
France	8	7	7	7	6	10	1	2	4	4	4	4
Germany	1	1	1	1	4	4	0	1	1	1	1	1
Indonesia	3	3	4	4	1	7	2	2	2	2	0	2
Japan	42	40	38	39	39	37	7	8	9	10	16	16
Korea	0	0	1	4	7	10	0	0	0	0	0	0
Malaysia	1	1	1	3	8	13	0	0	0	0	1	4
PRC	0	0	8	11	19	22	0	0	3	3	6	6
Singapore	11	11	11	15	14	16	2	3	4	5	4	5
Switzerland	6	6	5	6	8	7	0	1	1	1	3	3
Taipei	1	4	7	11	16	19	2	2	1	0	0	2
Thailand	2	3	4	4	3	6	0	0	0	0	0	1
The Netherlands	1	1	3	4	8	7	1	1	1	1	2	3
UK	23	22	27	29	29	33	9	9	8	8	10	10
USA	21	23	24	29	30	35	11	11	12	12	19	19
Others	11	9	10	11	7	7	0	1	1	1	1	1
Total	145	150	178	206	214	243	38	44	52	53	68	78

Note 1: Figures quoted are as at 31 March of the year concerned.

Note 2: Figures as at 31 March 1996 and 31 March 1997 have been adjusted to exclude dealers controlled by overseas incorporated companies which are controlled by Hong Kong residents.



survey in January 1997 on the business activities of registered firms. Although the responses from the survey are being collated and analysed, it is anticipated that the information obtained from the survey will give the SFC a more thorough understanding of the range of business activities undertaken by market intermediaries and facilitate the formulation of appropriate regulatory policies.

## Disciplinary Action

1.21 In order to safeguard the interests of investors and to promote and maintain the integrity of registered persons and the market, the SFC devoted substantial effort during the past year to the monitoring of the continuing fitness and properness of registered intermediaries. This effort carried out by both the Enforcement Division and Licensing Department led to formal inquiries being conducted into 173 cases, of which 124 resulted in some form of disciplinary action.

1.22 This year's inquiries centered mainly on issues such as short-selling, rat trading, misappropriation of clients' assets, unregistered activities, failure to implement adequate internal controls and failure to act in the best interest of the integrity of the market.

1.23 As a result, 2 registrants surrendered their registrations for a certain period of time and the SFC revoked 13 registrations, suspended 62 registrations, reprimanded 49 registrants and issued 27 warnings to registrants for various forms of misconduct during the past year. As at 31 March 1997, 6 revocations and 6 suspensions were the subject of appeal to the Securities and Futures Appeals Panel, the decisions of which are still pending.

1.24 Apart from the above inquiries and disciplinary action taken directly by the Department, a total of 52 cases concerning misconduct by members of the two Exchanges were referred to the respective Exchanges for action.

1.25 Some particular cases of interests are detailed below. Other cases are set out in the section of the annual report relating to the Enforcement Division.

## Some Particular Cases Of Interest

### Mr Lai Kim Leong

1.26 On 24 April 1996, the SFC suspended the registration of Mr Lai Kim Leong, dealing director of JCG Securities Limited, for five years. Lai was found to have misled the SFC during its investigation into insider dealing activities involving the shares of Public International Investments Limited (PIIL) and to have misled the Insider

Dealing Tribunal appointed by the Financial Secretary to investigate the matter when he testified before it. In addition, Lai was found to have withheld material information regarding his holdings in PIIL and JCG Holdings Limited.

### Mr Yuen Moon Chung

1.27 On 7 June 1996, the SFC suspended the registration of Mr Yuen Moon Chung for 18 months. Yuen, whilst acting as a securities dealer's representative of G K Goh Securities (HK) Limited, misled the SFC during its investigation into insider dealing activities involving shares of PIIL. Yuen was also found to have assisted others in providing misleading information to the SFC.

### Crosby Capital Markets (Asia) Limited

1.28 Crosby Capital Markets (Asia) Limited, a registered securities dealer, was publicly reprimanded by the SFC on 27 September 1996 following an inquiry into the placement of approximately 191 million shares in Giordano International Limited arranged by Crosby on behalf of Mr Jimmy Lai Chee Ying on 27 February 1996. The inquiry revealed that Crosby had accepted and executed a mandate to place Lai's shares on the same day as an announcement by Giordano stating, among other things, that "there was currently no definite proposal for such placing" and that Lai had not sought nor obtained Crosby's consent for a disposal of his shares.

1.29 The SFC was of the view that a person reading the announcement would reasonably infer that Lai would not, at least not on the very same day of the announcement, dispose of his shares in Giordano. The SFC, therefore, concluded that Crosby, in proceeding with the placement without taking steps to inform the market and/or to correct the perception created by that announcement, had failed in its duty to act in the best interest of the integrity of the market, and in so doing, had prejudiced the interests of members of the investing public.

## Administration

1.30 As part of its effort to enhance efficiency and cater for an increasing workload caused by the growth in the intermediaries population, the Department began rebuilding its computer system during the year. The project, expected to be completed by the last quarter of 1997, has been designed to support electronic submission and imaging, and most importantly, full Chinese character input and display capabilities.

1.31 The SFC's pilot Common Anniversary Date scheme for registrants' annual submissions, initiated in mid-1995, has completed one annual operating cycle smoothly. The scheme, which enabled registered firms to adopt a uniform anniversary date for all their registrants to aggregate all annual fees payable into one payment, and to submit annual returns in bulk, has been well received by the 21 participating firms. In view of the positive response, the SFC has decided to extend this programme, on an optional basis, to all registered/licensed firms, including licensed leveraged foreign exchange traders.

1.32 In preparation for this across-the-board extension, the necessary technical arrangements, including amendments to the Leveraged Foreign Exchange Trading (Annual Returns) Rules and the Securities and Futures Commission (Annual Returns) Rules, have been completed. Furthermore, 5 seminar sessions were organised in March 1997 to brief interested firms on the mechanics of the programme. More than 250 compliance staff from 200 firms attended the seminars. By 31 March 1997, a total of 437 business entities, in addition to the pilot scheme participants, had joined the programme.

### Intermediaries Supervision Department

1.33 The Intermediaries Supervision Department is responsible for the financial regulation of registered intermediaries and the supervision of their business conduct. Registered intermediaries are supervised mainly through on-site inspections and off-site reviews of a wide range of financial and other returns.

1.34 In recognition of the role of the Exchanges as front-line regulators of their members, the SFC limits routine inspections of Exchange members to about 5% of the Exchange membership each year. Dealers who are not Exchange members, and other registered intermediaries, are normally covered by a three-year cycle of visits.

### Inspections

1.35 In view of the growth in the number of registered intermediaries and the increasing complexity and diversity of their activities, the Department has introduced a programme to enable it to prioritise its visit cycle. Moreover, it has re-focused its monitoring programme and supervisory strategy, placing more reliance on risk-based inspection techniques. New analytical tools, such as on-site analysis using laptop computers, were also introduced.

1.36 The Department has also streamlined the inspection programme, including revised inspection planning checklists

and information questionnaires, to help focus on key issues to enhance the effectiveness and quality of site visits. In addition, inspection staff undertake a thorough analysis of target firms prior to an inspection to prepare themselves for the visit. These efforts have improved the effectiveness of the inspection programme, shortened the average length of visits and consequently increased the inspection coverage of registered intermediaries. They have also enabled the SFC to take more speedy regulatory action when required.

1.37 Alongside this change of strategy was the introduction of a computerised inspection results tracking system. The system allows instant access to the latest inspection progress and findings to enable prompt and proactive regulatory actions to be taken if circumstances dictate.

1.38 In addition, the Department has made greater use of outside resources to assist in compliance monitoring of registered intermediaries. Where significant inadequacies in the internal control systems are identified in the course of an inspection visit, the Department will require the intermediary to commission an independent compliance review by an external firm of professionals to detail the failures and to recommend improvements to processes and procedures. During the year, seven securities dealers and one investment adviser complied with such independent compliance review requests.

1.39 A breakdown of inspections undertaken for the year is as follows:

Figure 3

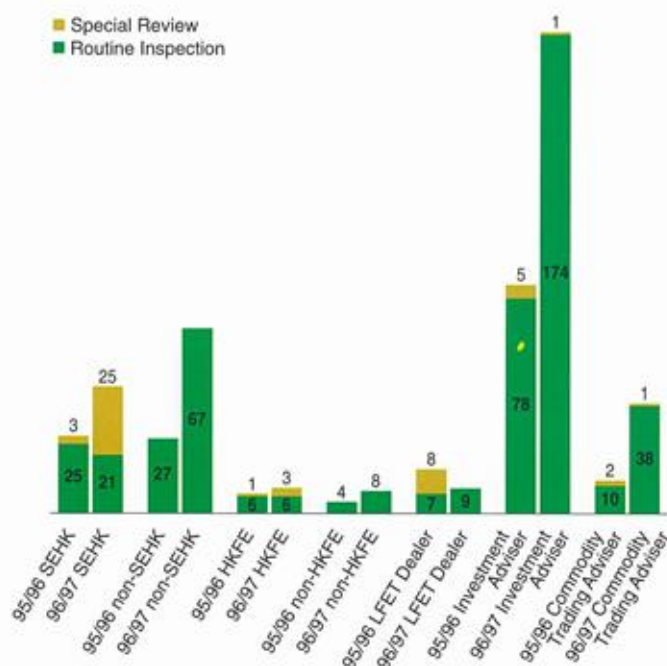
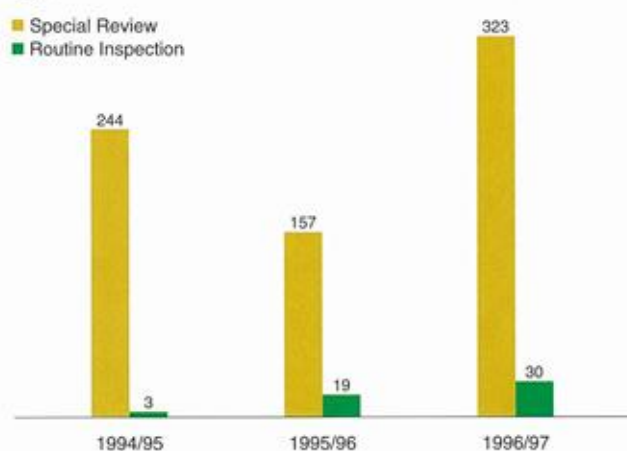




Figure 4



1.40 As a result of the above actions, routine inspection visits increased by 105% compared to 1995/96 as figure 4 illustrates.

1.41 The major types of rule breaches and non-compliance noticed during the course of inspections are as outlined in tables 7 and 8.

1.42 Although these tables suggest that the number of breaches noted during routine inspections have increased during the year, the Department does not regard this as a cause for concern or a reflection of a decline in the ethics

Table 8

**Breaches by Advisers noted during Routine Inspections**

Ordinances, Code of Conduct Unit Trust Code *	Investment Adviser	Commodity Trading Adviser
Failure to comply with the Financial Resources Rules	11	2
Unregistered dealing & registration of reps	31	1
Failure to maintain proper books	7	0
Failure to make filing / notification	15	0
Breach of Code of Conduct	172	4
Failure to make adequate disclosure in annual returns	2	1
Breach of licensing condition	3	0
Breach of Unit Trust Code	7	0
<b>Total</b>	<b>248</b>	<b>8</b>

Note : \*A single inspection may reveal breaches of more than one provision.

and professional standards of the registered intermediaries visited. The Department believes this to be a result of the more focused inspection programme and the increase in inspection activity during the year. The experience of the Department is that the majority of registered intermediaries visited conduct their operations with a high level of professionalism and integrity, ensuring that clients are treated fairly.

Table 7

**Breaches by Dealers noted during Routine Inspections**

Ordinances, Code of Conduct Unit Trust Code *	SEHK Member	Non-SEHK Member Dealer	HKFE Member	Non-HKFE Member Dealer	LFE Trader
Failure to comply with the Financial Resources Rules	10	33	0	0	7
Failure to safekeep clients' securities	11	7	1	0	0
Failure to maintain proper books	13	9	1	1	5
Failure to safekeep clients' money	3	10	2	1	4
Registration of reps & unregistered dealing	5	9	1	1	2
Breach of requirements of contract notes	7	5	1	1	2
Failure to make filing/notification	3	5	2	1	2
Breach of Code of Conduct	68	121	15	7	22
Breach of trading rules & dealing practices	8	0	0	0	1
Breach of margin requirement	0	1	3	0	4
Breach of Code of Business Guideline	0	0	0	0	7
Breach of Unit Trust Code	0	4	0	0	0
Short selling of securities	2	0	0	0	0
Breach of Core Operational & Financial Risk Management Controls for OTC Derivatives of Registered Persons	1	0	0	0	0
Breach of licensing condition	0	1	0	0	1
<b>Total</b>	<b>131</b>	<b>205</b>	<b>26</b>	<b>12</b>	<b>57</b>

Note : \*A single inspection may reveal breaches of more than one provision.



## Significant Market Integrity Activities

1.43 A sample of the cases which the Department dealt with during the year is described in the following sections.

### Frankwell Commodities Limited

1.44 The Department, together with the Hong Kong Futures Exchange, jointly conducted an on-site inspection visit on Frankwell. The inspection noted, among other things, that the company failed to meet the Financial Resources Rules and that the two major shareholders, whilst unregistered, were closely involved in the management of Frankwell's business, making all major decisions.

1.45 In light of the findings, Frankwell's dealing directors and major shareholders were publicly reprimanded. Frankwell subsequently ceased business and requested the SFC to revoke its registration (see paragraphs 3.17 - 3.19).

### Canwell Forex International Limited

1.46 An inspection by the Department in late 1995 into Canwell's operations uncovered strong evidence to suggest that Canwell did not possess the necessary regulatory capital. The company appeared to have arranged a series of short-term loans to cover the requisite capital whenever it had to produce evidence of the possession of such capital to the SFC. It also appeared to have falsified its monthly financial returns to the SFC to disguise the fact. An analysis of the actual accounts of the company indicated that it did not have sufficient assets to repay all client deposits.

1.47 In view of the findings, the SFC issued a restriction notice to freeze the assets of the company and successfully applied to the High Court under section 13 of the LFETO for the appointment of an administrator to Canwell to protect the interests of its clients. The administrator was further appointed as Receiver *ad litem* by the Court, on 17 January 1996, to represent Canwell against a legal claim made by a third party for the return from the administrator of \$32 million, its primary assets at the time.

1.48 On 3 October 1996, a settlement agreement, approved by the Court, was reached between the administrator, the SFC and the third party which provided, among other things, for a sum of \$6.6 million to repay all of Canwell's clients who traded with it after the commencement of the LFETO. The amount also covered the costs of the SFC and the administrator/receiver *ad litem*.

1.49 The licences of Canwell and its supervisory director were subsequently revoked. Further pursuit of the case rests with the Commercial Crime Bureau of the Hong Kong Police.

1.50 A review of the licensing and monitoring process was undertaken following discovery of the case to identify ways and means to uncover similar irregularities at an early stage.

All the recommendations from the review have since been implemented.

### Wei Xin Securities Limited

1.51 Wei Xin, a member of the Stock Exchange of Hong Kong Limited (SEHK), voluntarily ceased trading on 26 March 1996 in the face of serious financial problems. Thereafter, the SEHK suspended the membership of Wei Xin while the Hong Kong Securities Clearing Corporation Limited declared it a defaulter.

1.52 In order to protect the interests of investors while the liabilities of Wei Xin and an accurate evaluation of its clients positions were established, the SFC issued a restriction notice to Wei Xin on 16 April 1996 prohibiting it from carrying on business and dealing with its assets without the prior approval of the SFC. The action was taken under sections 39 and 40 of the Securities and Futures Commission Ordinance (SFCO). The restriction notice was withdrawn on 27 May 1996 when external administrators were appointed by the Supreme Court upon the application by a client of Wei Xin. The client also presented a winding up petition against Wei Xin.

1.53 At the winding up hearing, on 3 July 1996, the Supreme Court ordered that Wei Xin be wound up and the Official Receiver be appointed as provisional liquidator to handle the affairs of Wei Xin. The external administrators were later appointed by the Official Receiver to act as Special Managers to deal with claims against securities held by Wei Xin.

1.54 It is understood that substantially all clients' securities, including the proceeds from the sale of expiring warrants, have since been returned to clients.

### Cheung Cheong Woon trading as Cheong Woon Securities Company (CWS)

1.55 Mr Cheung Cheong Woon, a sole proprietor trading as CWS, reported to the SEHK and the Commercial Crime Bureau, on 10 May 1996, that he had disposed of clients' securities without their consent since 1991 and that his liabilities exceeded his assets by at least \$10 million. CWS's membership was suspended by the SEHK on the same day.

1.56 Based on information provided by the SEHK, the SFC issued a restriction notice, on 20 May 1996, prohibiting Cheung from dealing with his personal assets and the assets of CWS without the prior approval of the SFC. In order to ensure all investors' claims could be dealt with in an orderly manner, the SFC presented a petition to appoint the Official Receiver as the trustee in bankruptcy to deal with Cheung's financial affairs. The order was duly granted by the Supreme Court of Hong Kong.

1.57 On 26 July 1996, Cheung pleaded guilty to ten charges of theft and was sentenced to two years imprisonment.

#### Lai Kwok Kuen, Daniel trading as C.K. Securities Company

1.58 An inspection by the SEHK on C.K. Securities Company indicated that the company was unable to settle its indebtedness to clients and that stocks it held in the Hong Kong Securities Clearing Corporation Ltd were insufficient to meet its obligations to its clients. At the request of the SEHK, the SFC issued a restriction notice on 15 October 1996, pursuant to section 40 of the SFCO, to prohibit Lai from disposing of his assets without the SFC's prior written consent.

1.59 To safeguard the interests of investors, the SFC made an application to the High Court under section 144 of the Securities Ordinance (SO) for the appointment of administrators to C.K. Securities Company. The administrators were duly appointed on 13 November 1996. The administrators received over \$1 million from the closure of various bank accounts under the name of C. K. Securities Company and Lai Kwok Kuen. In addition, warrants with a short life span were sold for over \$94,000 and substantially all securities, with the exception of those of clients whom the administrators were unable to contact, were returned to identifiable owners.

1.60 The case remains unresolved as the SFC has no power to close down a sole proprietor in the absence of an act of bankruptcy falling within the definition of the Bankruptcy Ordinance.

### Waivers and Modifications

1.61 To provide relief for dealers and leveraged foreign exchange traders in unduly burdensome situations, the SFC has powers, under sections 29 and 55A of the SFCO and section 69 of the LFETO, to waive or modify certain requirements of the SO and the LFETO in respect of the safe custody of clients securities, segregation of clients' money and in particular the requirements of Financial Resources Rules.

1.62 Waivers or modification applications handled by the Department during the year were as follows:

Table 9

#### Waiver or Modification Applications

	Received/ carried forward	Granted	Rejected/ Withdrawn	Outstanding as at 31.3.97
S29 of SFCO	17	11	1	5
S55A of SFCO	9	9	0	0
S69 of LFETO	3	2	0	1
Recognition of counterparties under s2 of LFETO				
new	22	13	5	4
renewal	4	4	0	0
Subordinated loan				
new	39	26	5	8
repayment	14	11	0	3
extension	11	9	0	2
Total	119	85	11	23

### Policy and Review of Rules

1.63 During the year, the Department was involved in the following policy initiatives and review of subsidiary legislation.

#### Review of the Leveraged Foreign Exchange Trading Regulatory System

1.64 At the time the LFETO was introduced in September 1994, the SFC undertook to review the regulatory framework in light of experience gained during its initial phase of implementation. The SFC commenced a review of the regulatory framework in March 1996 and issued a consultation paper in August 1996 proposing a number of changes to the regulatory framework. Eighteen written submissions were received.

1.65 The comments were carefully considered by the SFC and a report concerning the consultation on the review was issued in April 1997. The report concluded that it remains appropriate to proceed with the proposed changes but that amendments are required to some recommendations to take account of points raised during the consultation exercise.

#### Review of the Financial Resources Rules

1.66 In order to ensure that the rules keep pace with changes in the market place and that no undue regulatory burden is imposed on registrants, a review of the Financial Resources Rules (FRRs) was conducted by the SFC during the year.



Although the review focused on the FRRs as applicable to securities and futures intermediaries, the FRRs for leveraged foreign exchange traders were also considered and consequential changes proposed. As a result of the review, a consultation paper was issued in March 1997 inviting comments on the review findings and the proposed changes.

#### Survey on the Over-the-counter (OTC) Derivatives Activities by Registered Firms

1.67 In 1995, the SFC conducted a survey on the OTC derivatives activities of registered persons. The survey was directed mainly at identifying firms which carried derivatives activities on their books and at establishing the nature and effectiveness of their risk management systems. The results indicated that only about 30 mainly large, internationally active securities firms, out of a total population of about 1,500 registered firms in Hong Kong, were engaged in OTC derivatives activities. The majority were engaged primarily in an agency role, and in the management of the derivatives positions of overseas affiliated companies.

1.68 As the first survey was of a qualitative and general nature, the SFC conducted a second survey, of the OTC derivatives activities of a selected group of registered persons, to collect quantitative information on the extent and nature of their involvement in this market, including proprietary derivative trading activities of affiliated companies managed by them. Twenty-four registered firms indicated their involvement in OTC derivatives activities as of 31 December 1995.

1.69 The results of the surveys indicate that for many large, internationally active firms, management of affiliates' derivatives positions constituted the major, if not the only, part of their derivatives activities. In addition, these firms had generally put in place the necessary risk management systems to assist them in conducting their derivatives activities prudently.

1.70 A report on the two surveys was published in April 1997. The report recommends a reporting requirement on the fact of involvement in OTC derivatives activities by a registered firm or its affiliates. Specific reporting requirements on the level of activities would be agreed with the firm on receipt of such a report. This new requirement will be introduced in the context of the review of the FRRs (see above).

#### Collaboration With Foreign Regulators

1.71 During the year, joint inspections were conducted with overseas regulators on intermediaries who are registered with both the SFC and the overseas regulatory bodies.

1.72 The Department believes joint inspections are an effective way for regulators to learn from each other, share experience, identify any overlaps of regulatory coverage and develop relationships for more effective supervision.

1.73 In June 1996 and March 1997, the Department conducted joint inspections with staff of the Securities and Exchange Commission of the United States of America on several investment advisers/fund managers for which both regulatory bodies have responsibility.

1.74 The Department also conducted joint inspection visits on fund managers with staff of the Investment Management Regulatory Organisation Ltd of the United Kingdom.

1.75 In October 1996, the Department visited several securities dealers jointly with staff from the Risk Assessment Group of the Securities and Futures Authority of the United Kingdom. The objective of the joint visits was to understand and assess the risk management systems of those globally active entities which conduct extensive derivatives activities in Hong Kong, the United Kingdom and other major financial centres.



### FUNCTIONS

2.1 *The Corporate Finance Division consists of the Listing Policy and Market Development Department, the Takeovers and Mergers Department and the Investment Products Division.*

2.2 *Among other regulatory functions, the Corporate Finance Division:*

- *administers the Takeovers and Mergers Code and Share Repurchases Code to ensure there is full and timely disclosure of relevant information affecting the value of securities of public companies;*
- *ensures there is fair and equal treatment of public shareholders;*
- *maintains and improves investor protection standards by developing fair, clear rules for listed companies, and promoting the development of good and sound business practices;*
- *oversees the performance of the Stock Exchange of Hong Kong (SEHK) of its listing-related functions and responsibilities;*
- *reviews and recommends changes to the Listing Rules;*



**Laura M Cha** is Executive Director responsible for the Corporate Finance Division, which comprises the Listing Policy and Market Development Department, the Takeovers and Mergers Department and the Investment Products Division. She is also responsible for the Corporate Communications Division.

- facilitates the development of effective and efficient capital markets in both equity and debt issues; and
- facilitates the development of Hong Kong as the preferred overseas market for the listing and trading of securities of PRC enterprises.

## **Listing Policy and Market Development Department**

### **China Initiatives**

2.3 Eight PRC state enterprises listed their H-shares in Hong Kong during the year, raising approximately HK\$13.91 billion from the market. Twenty-nine of the first 38 companies authorised by the PRC State Council to list outside the PRC have done so to date; and 27 of these 29 have chosen to list in Hong Kong. The State Council authorised a further 38 companies in December 1996 for overseas listing and it is expected a majority of these companies will also choose to list in Hong Kong.

2.4 During the year, two Hong Kong-listed H-share companies have issued convertible bonds amounting to a total value of US\$300 million.

2.5 During the year, the Division held ongoing discussions with the China Securities Regulatory Commission (CSRC) on the listing and regulation of companies controlled by PRC interests in Hong Kong. These discussions were in addition to the regular quarterly meetings under the Memorandum of Regulatory Cooperation.

2.6 In May 1996, the SFC, together with the SEHK, the Hong Kong Monetary Authority (HKMA), Hong Kong Futures Exchange (HKFE) and the China Securities Regulatory Commission (CSRC) jointly organised a seminar in Beijing to promote the financial markets of Hong Kong to PRC government officials and senior executives of PRC companies. The SFC also participated in a seminar organised by the CSRC to further their understanding of Hong Kong's role as an international financial centre.

### **Derivative Warrants**

2.7 In July 1996, the SFC approved major changes to the SEHK Listing Rules governing the listing of derivative warrants. This was the result of the joint effort of the SFC and the SEHK, developed through an extensive review of the previous rules and a market consultation exercise, with a view to further developing the derivative warrant market in Hong Kong.

2.8 The new rules, together with other existing requirements, were consolidated into a new chapter 15A of the Listing Rules. The new rules impose stringent ongoing disclosure requirements on issuers covering information

relating to their financial statements and risk management systems. Criteria governing the issue of basket warrants were relaxed to accommodate comments from the market that the former rules were too restrictive. The new rules also encourage the listing of derivative warrants based on regional stocks.

2.9 Since the introduction of the new rules, the derivative warrant market in Hong Kong has experienced substantial growth. There was a marked increase in the number of derivative warrant issuers approved by the SEHK, from 16 a year ago to 22 as at the end of March 1997. As at 31 March 1997, there was a total of 296 (1996: 109) outstanding issues of derivative warrants listed on the SEHK, representing HK\$31,686 million (1996: HK\$11,249 million) in market capitalisation and approximately 0.92% of the total market capitalisation on the SEHK. The product type of derivative warrants has also diversified. There were 247 derivative warrants based on a single underlying share, 47 derivative warrants based on a basket of shares, and 2 derivative warrants based on non-equity financial instruments, such as a stock index or gold prices. Whilst the vast majority of the derivative warrants are call warrants, 4 put warrants were issued during the year.

### **Financial Disclosure by Banks**

2.10 As the result of the joint efforts with the HKMA and SEHK, the SFC approved further enhancements to financial disclosure rules under the Listing Rules for banks listed on the SEHK. These rules reflect the requirements contained in the HKMA's Best Practice Guide and require banks to include in their financial statements cash flow statements which were previously exempt by the Companies Ordinance, information relating to their market risk exposures and additional segmental information relating to their significant classes of business. Disclosure requirements for listed banks as set out in the Listing Rules have been increased each year since 1994 and are recognised as the most rigorous regime in South East Asia.

### **Review of the Listing Functions of the SEHK**

2.11 Pursuant to the terms of the 1991 Memorandum of Understanding (MOU) between the SFC and the SEHK that devolved to the SEHK sole responsibility for the day-to-day administration of listing-related matters, the Division completed in February 1997 the third post-devolution review of the listing functions of the SEHK. The review covered the period from 1 January 1995 to 30 June 1996 and involved the examination of a number of operational areas of the Listing Division, including the prospectus vetting function, as well as the review of a number of selected cases.



2.12 The SFC will continue to perform reviews, at eighteen month intervals, on the operations of the SEHK in order to discharge its oversight functions on the SEHK under the MOU.

#### **Mechanism for Global Offering of Securities**

2.13 The SFC, together with the SEHK, conducted during the second half of 1996 interviews with market practitioners and listed issuers with regard to the offering mechanism used in the distribution of securities in global offerings. The purpose of the interviews was to review the implementation by the market of the Joint Policy Statements on offer mechanism made by the SFC and the SEHK in November 1994, with a view to refining the current practice and ensuring that the objectives of the policy statements were met. The SFC anticipates conducting a public consultation exercise with the SEHK before issuing further guidance in this area.

#### **Statutory Protection for Auditors**

2.14 The SFC assisted the Government in drafting a bill to protect auditors of listed companies from liabilities arising from reporting to the SFC and the SEHK reasonable suspicion of misfeasance by the companies and their officers. The SFC is of the view that such legislation would encourage auditors to report suspected misfeasance to the authorities in circumstances where they might be reluctant to do so for fear of possible legal proceedings by their clients alleging defamation or breach of duty to maintain client confidentiality. The bill has been presented to the Legislative Council and awaits consideration by a bills committee.

#### **Securities (Disclosure of Interests) Ordinance (SDIO)**

2.15 Whilst work is still continuing on the rationalisation of securities legislation, the proposed public consultation on the amendment of the SDIO and related legislation drafting work has been postponed. The Division intends to consult the public on proposed revisions to the SDIO as soon as work on the draft Composite Securities and Futures Bill is completed.

#### **Corporate Governance**

2.16 The subject of corporate governance has continued to attract public attention in Hong Kong. An SEHK Corporate Governance Working Party, which included an SFC representative, is expected to report to the Listing Committee in the second quarter of 1997 on possible changes to the SEHK's Code of Best Practice.

#### **Mandarin Resources Corporation Limited**

2.17 On 25 June 1996, following consultation with the Financial Secretary, the SFC filed with the Supreme Court of Hong Kong a petition against Mandarin Resources Corporation Limited (MRC) and the Honourable Mr Chim Pui Chung, its controlling shareholder. The petition seeks a number of remedies, including redress for the minority shareholders of MRC arising from the manner in which the affairs of MRC are alleged to have been conducted. The petition was based on an investigation conducted by the Division. It is anticipated that the case will be set down for hearing by the end of 1997.

#### **Simplification of prospectuses and announcements by listed companies**

2.18 In view of the increasingly complex language used in announcements, circulars and prospectuses issued by listed companies, in March 1997 the SFC formed a working group with market practitioners and the SEHK to consider and promote the use of plain and clear language in public documents issued by listed companies. The working group will also review the quality and format of information in a prospectus in order to make it easier for the investing public to discern the relevant information. It is anticipated that the working party will complete its review and issue recommendations by the end of 1997.

### **Takeovers and Mergers Department**

#### **Administration of the Takeovers Code and Share Repurchases Code**

2.19 During the year, there were 31 general offers under the Takeovers Code and 114 waivers of general offer requirements and confirmations of no offer requirement (e.g. placing and top-up), 6 privatisation proposals and 457 other waivers, consents and confirmations given by the Department. Statistics on cases handled by the Takeovers Panel and the Takeovers Executive are at Table 1. These show a very considerable increase in the number of cases handled by the Department. In addition, the year saw many large and complex transactions, some of which are discussed below.

#### **TVE (Holdings) Limited**

2.20 On 14 February 1996, South China Morning Post (Holdings) Limited announced a voluntary conditional share offer for all the shares of TVE (Holdings) Limited. Shortly after the offer document was dispatched, Shaw Brothers issued a counter-bid for TVE, offering to buy all the shares of TVE in cash. The SCMP offer was not considered to be fair and reasonable by the independent financial adviser of



TVE. SCMP then increased its offer by adding a cash alternative, after which Shaw Brothers withdrew its offer with the consent of the Takeovers Executive. TVE was eventually privatised by SCMP under the compulsory acquisition provisions of the Companies Ordinance. This case is noteworthy as one of the very few hostile takeovers which have taken place in the Hong Kong market in recent years.

#### Consolidated Electric Power Asia Limited

2.21 In October 1996, Hopewell Holdings Limited agreed to the takeover of Consolidated Electric Power Asia Limited (CEPA), its power generation subsidiary, by the Southern Group in the United States. This was the second largest takeover to date of a Hong Kong listed company in terms of the monetary value of the consideration received by shareholders. Under a Scheme of Arrangement, shareholders of CEPA were offered either cash or a combination of cash and new CEPA shares. This resulted in CEPA becoming an 80% subsidiary of the Southern Group and its withdrawal of listing from the SEHK. Upon completion of the Scheme of Arrangement in early 1997, control of CEPA was passed to Southern. Hopewell, the former controlling shareholder of CEPA, retained a substantial interest in CEPA. The Takeovers Code provisions regarding a privatisation by way of scheme of arrangement did not apply in this case as Hopewell effectively sold its control of CEPA to a third party purchaser on terms made equally available to other CEPA shareholders under the scheme.

#### Cheung Kong Group Reorganisation

2.22 The Cheung Kong Group announced in early January 1997 a proposed reorganisation involving a general offer by Hutchison Whampoa Ltd for Hong Kong Electric Holdings Ltd, followed by a realignment of two companies by way of intra-group transfers. The resulting group structure is a vertical one with Cheung Kong (Holdings) Ltd owning just below 50% of Hutchison Whampoa, and Hutchison Whampoa controlling Cheung Kong Infrastructure Holdings Ltd which in turn holds Hong Kong Electric. Hutchison Whampoa's takeover of Hong Kong Electric exceeded Southern's offer for CEPA in total monetary value. Of the various steps of the reorganisation which have implications under the Takeovers Code, the Takeovers Executive was satisfied (i) that any general offer obligation resulting from the intra-group transfers of the interest in Cheung Kong Infrastructure from Cheung Kong to Hutchison and that in Hong Kong Electric from

Hutchison to Cheung Kong Infrastructure could be waived on the basis that Cheung Kong remained in ultimate control over each of the group companies; and (ii) that the consolidation of control by Cheung Kong over Hutchison Whampoa was effected within the creeper restriction applicable for the relevant 12-month period under the Takeovers Code.

#### Some Decisions by the Takeovers Panel

##### *Privatisation of Asean Resources Holdings Limited*

2.23 The Panel met on 3 May 1996 to review a ruling made by the Takeovers Executive in relation to a proposed privatisation of Asean Resources Holdings Ltd by Huey Tai International Ltd. The ruling related to the inclusion of a warrant-for-warrant alternative in the proposed offer structure.

2.24 Huey Tai owned 68.1% interest in Asean and proposed to privatise it by way of a scheme of arrangement through the offer of one cent or one new Huey Tai warrant for one Asean warrant. This offer (the warrant-for-warrant offer) was higher than the "see-through price" (i.e. the offer price for Asean shares less the exercise price of Asean warrants) of the Asean warrant. The issue for the Panel was whether the proposed offer was in compliance with the "equality of treatment" principle and Rule 13 of the Takeovers Code.

2.25 The Panel ruled that the "see-through price" formula provided under the Note to Rule 13 of the Code is only a minimum requirement for the protection of warrantholders. The Takeovers Executive or the Panel may permit an offer higher than the "see-through price". However, a higher offer would not be considered appropriate if it were to be considered part of a special deal to provide an incentive to persons who also hold shares or other securities of the offeree company to accept the offer. Regarding the interpretation of "equality of treatment" under Rule 13.1, the Panel takes the view that this should mean equality of treatment within a class of security holders as opposed to equality of treatment between different classes of securities.

##### *Application of Rule 31.1(a)(i) of the Code*

2.26 The Panel met on 1 March 1997 to consider a referral by the Takeovers Executive in connection with the application of Rule 31.1(a)(i) of the Code in relation to The Kwong Sang Hong International Ltd, a listed company which was owned more than 50% by Peregrine International Holdings Ltd. Peregrine announced in December 1996 a proposal to privatise Kwong Sang Hong by way of a scheme

of arrangement. Implementation of the scheme is, therefore, subject to approval by a majority in number representing 90% in value of those shares that are voted at a duly convened general meeting by shareholders other than Peregrine and persons acting in concert with it (the "independent shareholders").

2.27 Peregrine was concerned that the scheme would not be approved by the necessary number of independent shareholders during the general meeting which was required to be held as a court meeting. Prior to the court meeting, Peregrine applied to the Takeovers Executive under Rule 31.1(a)(i) for consent to make a voluntary general offer for all the shares of Kwong Sang Hong if the privatisation proposal was not approved by the independent shareholders during the court meeting. The consideration offered to shareholders under the proposed voluntary offer would be the same as the consideration offered under the privatisation proposal. The voluntary general offer would be an unconditional offer. The Takeovers Executive did not consider it appropriate to give the requested consent and referred the matter to the Panel.

2.28 The Panel was asked to consider whether consent could be granted to Peregrine under Rule 31.1(a)(i) to make an unconditional voluntary general offer for all the shares of Kwong Sang Hong not already owned by Peregrine and its subsidiaries if the privatisation did not obtain the necessary approval by independent shareholders.

2.29 The Panel ruled that the proposed voluntary offer is contrary to the disciplines which the Code generally seeks to impose on offerors and, in particular, to the requirement of Rule 31 which does not permit an offeror to make a new

offer for the same company within the twelve-month period following the date on which an offer has lapsed. Under Note 1 to Rule 31, the consent of the Takeovers Executive is not normally given when the offeror is a substantial shareholder of the offeree company, as is the case with Kwong Sang Hong and Peregrine. After considering the representations made by the Takeovers Executive, Peregrine, and its adviser, the Panel supported the Takeovers Executive's decision not to exercise its discretion to permit Peregrine to extend a voluntary offer for Kwong Sang Hong immediately following the failure of the privatisation proposal in respect of Kwong Sang Hong.

### Suspension of trading

2.30 Under the Securities (Stock Exchange Listing) Rules the SFC may direct the SEHK to suspend all dealings in specified securities if it appears to the SFC that materially false, incomplete or misleading information has been included in a prospectus, circular, or equivalent document or in any written announcement, statement or circular issued by or on behalf of a listed company. The SFC may also direct suspension where it appears to be in the interest of maintaining an orderly and fair market, in the interest of the investing public or in the public interest. These powers were formally invoked only once during the year as the Division was able to encourage listed companies under certain circumstances to amend announcements, to provide further information in a public announcement, or to request voluntary suspension in the trading of shares until the relevant announcements could be made.

Table 1

**Code on Takeovers and Mergers & Code on Share Repurchases**  
Statistics of Cases during the 12-month periods  
ended 31 March 1997 and 31 March 1996

	1 Apr 96 to 31 Mar 97	1 Apr 95 to 31 Mar 96
General Offers under Takeovers Code	31	24
General Offers under Share Repurchases Code	0	3
Privatisations	5	6
Waiver applications of General Offer Requirement	114	65
Other waiver applications under Takeovers Code	116	81
Waivers applications under Share Repurchase Code	1	6
Withdrawal of Offer	2	1
Applications for exemption under Securities (Disclosure of Interests) Ordinance	337	140
Withdrawal of Privatisation	1	0
Cases dealt with by the Panel by way of Meeting / Hearing / Circulation:		
Referral by the Executive	1	0
Reviews of Executive rulings by Panel	2	3
Disciplinary Proceedings	0	2
Panel Meeting Days	2	7



## Investment Products Division

### Functions

2.31 The Investment Products Division has regulatory responsibility for investment products, which include unit trusts, mutual funds, investment-linked assurance schemes, pooled retirement funds and immigration-linked investment schemes as well as other forms of investment arrangements. These products require authorisation by the SFC before they can be marketed to the public in Hong Kong. The Division vets applications for authorisation of investment products and related advertising material and monitors ongoing compliance with the requirements. In addition, it administers the prospectus-vetting provisions of the Companies Ordinance, vetting prospectuses for issues not listed on the SEHK.

2.32 To assist its work, the Division has developed and administers three Codes: the Code on Unit Trusts and Mutual Funds, the Code on Investment-linked Assurance and Pooled Retirement Funds, and the Code on Immigration-linked Investment Schemes. The Division also develops guidelines and policies on other types of investment products and matters affecting the investment management industry generally.

2.33 The Division administers the applicable provisions of the Protection of Investors Ordinance (PIO). It monitors the print media for offers to the public to invest, making enquiries into misleading advertising that falls within the remit of the PIO and working with the Enforcement Division in relation to enforcement action.

2.34 The Investment Products Division has also recently taken on responsibility for investor education, including the public enquiry and complaints function previously handled by the Enforcement Division.

## Unit Trusts and Mutual Funds

### Regulation of Investment Management

2.35 Following the Jardine Fleming (JF) disciplinary case in August 1996 (see paragraphs 3.14 - 3.16), and the temporary suspension of Morgan Grenfell's funds in the UK and Dublin in September 1996, many questions were raised by the media and the public about the regulation of investment management. Although no regulatory system can guarantee to prevent misconduct or malpractice, regulators are very aware of the ongoing need to take all reasonable steps to safeguard the interests of investors and to ensure that transactions take place in a fair market.

2.36 In November 1996, the SFC issued a consultation paper on Management, Supervision and Internal Control Guidelines, which outlines detailed compliance procedures for all intermediaries, including fund managers. In addition, the Division has been working with the Hong Kong Investment Funds Association (HKIFA) on the development of "best practice" guidance to supplement the existing rules and codes. The HKIFA has prepared a detailed guideline on the restrictions for personal account dealing by fund managers, to supplement the existing requirements for client priority and avoidance of conflicts of interest. Fund management companies themselves, moreover, are demonstrating increasing compliance awareness, which will be reinforced by SFC inspections.

### Statistics

2.37 Strong growth in the fund industry continued over the period. Despite the deauthorisation of 52 funds, 164 funds were authorised during the period, bringing the total number of authorised funds to 1,356 as at 31 March 1997 (See Figure 1), compared to a total of 1219 as at 31 March

Figure 1  
**Authorisations vs De-Authorisations**  
Unit Trusts & Mutual Funds, April 1996 - March 1997

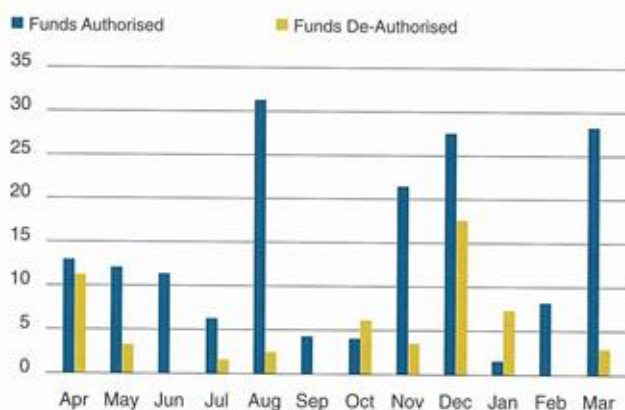
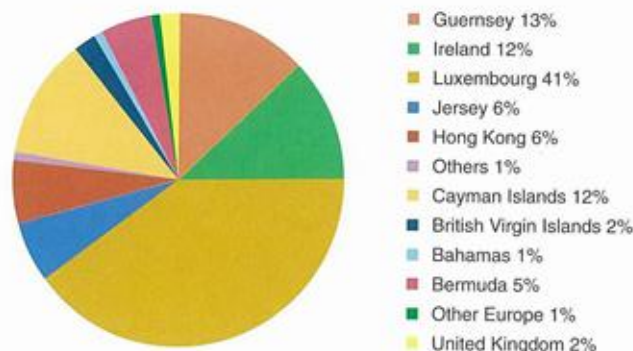


Figure 2  
**Authorised Unit Trusts & Mutual Funds By Jurisdiction**





1996. This represents an increase of 11.2% and the highest level yet achieved for authorised funds in Hong Kong. Of the 1,356 authorised funds, 972 were sub-funds of umbrella funds, representing a 12.8% increase over the last year (See Table 2)

2.38 The number of applications continued to increase steadily. In particular, equity funds investing in the Asian region continued to be a market favourite (See Table 3).

2.39 Despite the entrance of a number of new management groups, mostly from overseas, restructuring and amalgamation of some existing fund management groups has caused the number of fund management groups to remain fairly steady. As at 31 March 1997, the number of fund management groups authorised to market their funds in Hong Kong totaled 90 compared to 87 at the end of March 1996. However, this does not include the total number of fund management companies in Hong Kong, which is estimated at 195. This number is a subset of the population of licensed Securities Investment Advisers, and a more detailed database will be established with the assistance of the Licensing Department in the coming year.

2.40 Authorised funds in Hong Kong continue to be predominantly international in origin. (See Figure 2). Although Hong Kong authorised funds are domiciled in 20 jurisdictions, some 55% of authorised funds are managed or advised by Hong Kong domiciled fund managers, with the remaining majority being managed or advised in places such as the UK and the United States. (See Figure 3)

2.41 The average authorisation time for standard funds remained at about three weeks. Overall, the Division has continued to maintain its efficiency in processing new applications (see Performance Pledges).

## Unlisted Company Prospectuses

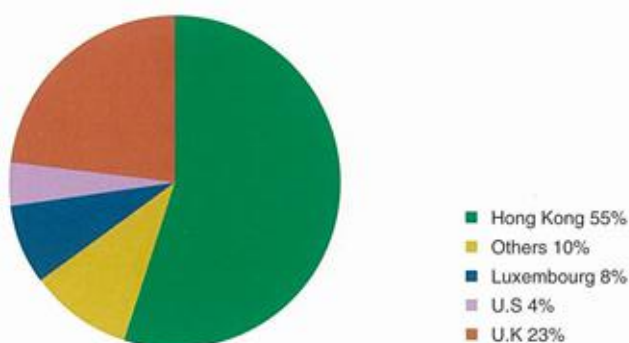
2.42 Apart from the authorisation of 74 mutual fund prospectuses, the majority of the applications for authorisation for registration of unlisted company prospectuses were Eurobond issues, most of which were medium term note programmes. There was one public share offer and four B-share rights issues during the period.

## Other Investment Products

### Investment-linked Assurance and Pooled Retirement Funds

2.43 Two major initiatives came to fruition during the past year in relation to investment-linked assurance schemes. The first was the introduction of the cooling-off period

Figure 3  
Domicile of fund managers



\* Data excludes sub-funds of umbrella funds

Table 2  
Origin / Net asset value of authorised funds  
as at 31 March 1997

	Umbrella Number	Sub-funds Number	Single Funds Number	Total			
				Number	%	NAV* (US\$ Million)	%
Hong Kong	2	2	73	77	6	2,993.5	3
Jersey	7	74	1	82	6	2,932.8	3
Luxembourg	42	488	23	553	41	27,477.0	28
Ireland	25	124	11	160	12	8,931.0	9
Guernsey	11	155	12	178	13	5,194.1	5
United Kingdom	0	0	28	28	2	7,496.0	8
Other Europe	0	0	9	9	1	5,543.3	6
Bermuda	6	41	20	67	5	1,596.4	2
Bahamas	1	6	1	8	1	578.2	1
British Virgin Islands	1	9	15	25	2	1,917.2	2
Cayman Islands	17	71	70	158	12	3,555.7	4
Others	1	2	8	11	1	29,378.9	30
<b>No. of Authorised Funds</b>	<b>113</b>	<b>972</b>	<b>271</b>	<b>1356</b>	<b>100</b>	<b>97,594.1</b>	<b>100</b>

\* Net Asset Value as at 31/12/96: based on information available (excluding "umbrella funds")

Table 3  
**Authorised Mutual Funds and Unit Trusts**  
 as at 31 March 1997

	Total		NAV*	
	Number	%	(US\$ Million)	%
Bond	190	15	10,403.9	11
Equity	713	57	71,186.1	73
Diversified	75	6	7,469.0	8
Money Market	186	15	5,887.2	6
UPMF	24	2	515.1	1
Warrant	16	1	279.3	0
Other specialized #	39	3	1,853.5	2
	<b>1243</b>	<b>100</b>	<b>97,594.1</b>	<b>100</b>
Umbrella structures	113			
No. of Authorised Funds	<b>1356</b>			

\* Net Asset Value as at 31 Dec 96; based on information available.

# includes: Futures & Options funds; Guaranteed funds & Leveraged funds.

which came into effect on 1 July 1996. Buyers of long-term life policies, including investment-linked assurance schemes, are now given a maximum of 21 days to demand a full refund (less a market value adjustment, where applicable) from the insurer. The second initiative was the requirement for insurers to provide details on surrender values to prospective investors in these schemes before they sign the application form, illustrating the penalties applicable to the early years of the policy. This requirement came into effect on 1 January 1997.

2.44 These initiatives stem from an increasing number of investor complaints about these products in recent years, in particular from investors who claimed to have been misinformed about the long-term nature of the products and the penalties for early encashment. Both initiatives received the invaluable assistance of the Life Insurance Council of Hong Kong and the Insurance Authority.

2.45 In the coming year, the SFC will revamp the Code on Investment-linked Assurance and Pooled Retirement Funds in the light of recent developments in the market for both products. These include, among other things, the increasing localisation of the market for unit-linked policies, the increasing involvement of fund houses in the pooled retirement funds market and the potential impact of the Mandatory Provident Fund.

2.46 Given the increasing divergence of the two products, the SFC intends to split the Code into two and publish one code each for investment-linked assurance schemes and pooled retirement funds. This is expected to be achieved within the coming year and, when implemented, will facilitate promoters' of scheme documents as requirements will be more specific to the products under regulation.

## Statistics

2.47 The number of investment-linked assurance and pooled retirement funds whose documentation had been authorised increased to 119, of which 67 were investment-linked assurance schemes and 52 were pooled retirement funds. The number of management groups or companies increased by 5 to 41.

## Immigration-linked Investment Schemes

2.48 As in previous years, Canada continued to be the only country from which immigration-linked investment schemes originated. Activity in this area slowed considerably since the Canadian government halted the promotion of private sector managed schemes in July 1996 (except for Quebec-based schemes). At present, the market is dominated by government-administered or Quebec-based schemes. It is difficult to predict with accuracy how the market for this product will be in the coming year as, among other reasons, the Canadian government is again reviewing the situation and some changes to the Immigrant Investor Program are due to be made in June 1997. The SFC authorised the documentation of a further 6 immigration-linked investment schemes during the year, making a total of 57 authorised schemes since the introduction of the Code on Immigration-linked Investment Schemes in May 1990. As of 31 March 1997, only 12 authorisations remain current.

## Investor Education

2.49 The Investor Education Unit was established in April 1996 to implement educational initiatives to explain to the investing public the operation of the regulatory framework, the protections available within it, and the role investors should play to safeguard their own interests when investing. It also handles investor enquiries and complaints.

## Publications

2.50 New publications, in English and Chinese, designed for prospective and existing retail investors, were launched in August 1996. These booklets

discuss some of the key issues people should consider when deciding to invest. Those issues include the risks and rewards of investing, the importance of "doing your homework" when selecting an investment or





choosing a broker or financial adviser, and what the SFC can do to help investors who encounter market malpractice by intermediaries. The titles of these publications are :

- Step 1 : Your First Moves Towards Investing
- Step 2 : Choosing Your Broker or Financial Adviser
- Step 3 : The Importance of Monitoring Your Investments
- Step 4 : When to Pursue a Complaint

2.51 All the publications are available to the public free of charge at the SFC and all 16 offices of the Consumer Council. Some 35,000 brochures were distributed within three weeks of launch in August 1996.

2.52 The contents of these publications are available on the SFC's Web site on the Internet, located at <http://www.hksfc.org.hk>. At the request of both Ta Kung Pao and the Oriental Daily News, the contents of the brochures have also been published in a series of articles.

#### Media Programme

2.53 In a joint project with Ming Pao, a series of eight investor education stories appeared in the newspaper's business pages in August and September 1996. The stories illustrate common problems experienced by investors and explain how investors can safeguard their interests in similar situations. These stories can also be found on the SFC's Web site.

2.54 The SFC sponsored two television series, produced by Radio Television Hong Kong (RTHK), which aim to guide the public through the steps of wise investment. The first series, "All About Investing", comprised eight episodes of five minutes each and was aired on the TVB Jade and ATV Home channels in October 1996. The second series, "Invest Wisely", consisting of six half-hour documentaries, was aired on TVB Jade from February to April 1997.

2.55 The next phase of the investor education programme will seek to enhance the existing publication programme by developing more booklets on topics of concern, as well as to explore other media to disseminate the SFC's educational messages. In addition, the Investor Education Unit will continue to coordinate educational activities with the Exchanges and other market bodies such as the Hong Kong Investment Funds Association.

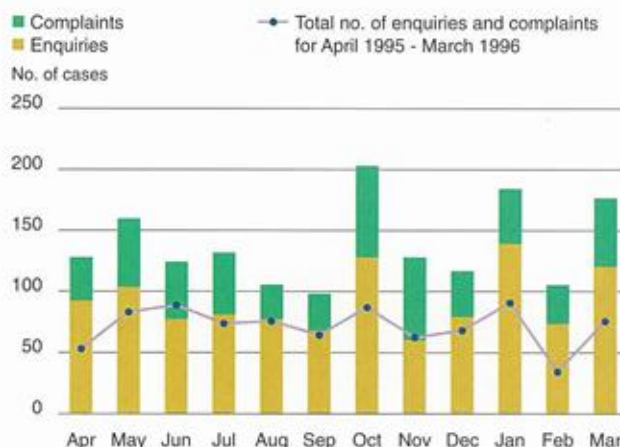
#### Investor Enquiries and Complaints

2.56 All investor enquiries and complaints are handled by the Investor Education Unit. Investors can call the SFC Hotline at 2840-9333 if they believe there has been malpractice in relation to their investments or if they want to check whether their broker is licensed or if an investment product is authorised. The Hotline operates during normal

working hours and has a tape recording system outside of working hours. Investors may also submit a written enquiry or complaint or request an appointment to discuss these matters in person.

2.57 During the year, the SFC received 1,088 enquiries and 565 complaints from the investing public. The subjects of enquiries were diverse, but it is clear that the investing public were increasingly concerned about the operation of the regulatory framework and their rights in dealing with intermediaries. The vast majority of complaints were resolved without further investigation being necessary. Legitimate complaints are passed on to relevant SFC departments for further assessment, and if necessary, to the Enforcement Division for investigation. In 19 of these cases, formal investigations were initiated (see paragraph 3.7).

Figure 4  
**Number of Investor Enquiries and Complaints**  
April 1996 - March 1997



### FUNCTIONS

3.1 *The statutory functions of the SFC which are of an enforcement nature include:*

- *ensuring compliance with laws relating to the securities and futures industries, leveraged foreign exchange trading, and investment arrangements;*
- *reporting suspected insider dealing to the Financial Secretary;*
- *suppressing illegal, dishonourable or improper practices in dealing in securities, trading in futures and leveraged foreign exchange contracts, entering into investment arrangements, and providing*

*investment advice or other financial services;*

- *inspecting the books and records of listed companies when directors and officers are suspected of impropriety in the management of a listed company's affairs; and*

*cooperating with and assisting domestic or overseas regulatory bodies concerned with securities, futures, leveraged foreign exchange trading, banking, insurance or other financial services; or with the affairs of corporations.*



**Mark Dickens** is Executive Director responsible for the Enforcement Division and for International Relations.



3.2 In performing these functions, the SFC's Enforcement Division :-

- collects evidence to:
- support prosecutions for breaches of the various laws administered by the SFC;
- institute disciplinary proceedings in respect of misconduct by licensed intermediaries;
- refer to the Stock Exchange of Hong Kong (SEHK) and the Hong Kong Futures Exchange (HKFE) apparent breaches of their rules; and
- detect impropriety by directors and officers in the management of a listed company's affairs;
- issues warnings, and advice on remedial action, for minor transgressions;
- prepares cases triable summarily for prosecution by the SFC's Legal Services Division;
- forwards to the Director of Public Prosecutions cases involving offences that appear to warrant prosecution on indictment;
- reports to the Financial Secretary circumstances which suggest that inspections under the Companies Ordinance or the Securities (Disclosure of Interests) Ordinance should be initiated;
- cooperates with and assists inspectors appointed by the Financial Secretary, the Insider Dealing Tribunal, and other regulatory and investigative authorities in Hong Kong such as the Hong Kong Monetary Authority (HKMA), the Independent Commission Against Corruption and the Royal Hong Kong Police - especially its Commercial Crime Bureau; and
- arranges, on behalf of the SFC, bilateral agreements with overseas regulatory authorities regarding mutual cooperation in the exchange of information and other assistance.

3.3 The Executive Director, Enforcement, coordinates and prioritises enforcement activity Commission-wide to ensure the range of cases investigated are well balanced, cover the full ambit of the SFC's statutory compliance responsibilities, reinforce regulatory policy objectives and demonstrate the SFC's vigilance in protecting investors.

## Surveillance

3.4 The SFC's surveillance team monitors trading on the SEHK and the HKFE, using computer analysis to identify unusual price and volume movements and, when appropriate, conducts preliminary enquiries to determine whether the movements raise suspicions of market manipulation and/or insider dealing.

3.5 The first step is to analyse trading information from the SEHK or the HKFE. If this information raises

suspensions of insider trading or market manipulation, then client details and records are obtained from brokers and, if further analysis of these records raise reasonable grounds to suspect insider dealing, market manipulation or other misconduct, an investigation is initiated.

3.6 During the year, trading records were obtained from brokers on 32 occasions. In 21 of these cases, full investigations were initiated.

## Complaints and Enquiries

3.7 Of the 1653 complaints and enquiries received during the year by the Investor Education Unit (see paragraph 2.56), the vast majority were resolved without full investigation being necessary. However, in 19 cases, formal investigations were initiated.

## Investigations - An Overview

3.8 Although the SFC is limited in its capacity to comment on investigations by the secrecy provisions of the Securities and Futures Commission Ordinance (SFCO), there are some cases where information is already in the public domain and others where general information can be given.

3.9 A total of 188 cases were carried forward as ongoing inquiries from the previous year. During the year a further 188 cases (including the 21 cases referred to in paragraph 3.6 and the 19 cases referred to in paragraph 3.7) were referred to the Division by the public, foreign regulators, law enforcement agencies in Hong Kong, the Exchanges, and from within the SFC.

3.10 Of the total of 376 cases handled, 207 have been concluded. The remaining 169 are the subject of continuing enquiries, hearings or prosecutions.

## Investigations - "Rat Trading"

3.11 During the year, action continued against registered persons involved in "rat trading", a generic term used in the local securities and futures markets to cover a wide range of malpractices by staff of brokers, in particular floor traders, trading to the disadvantage of clients. Rat trading is usually detected during routine inspections both by the SFC's Intermediaries Division and the Financial Regulation Unit of the SEHK, who then refer their findings to the Enforcement Division for investigation.



3.12 Investigations culminated in disciplinary action being taken against 58 registered persons who were involved in, or actively facilitated rat trading. These persons either had their registrations revoked or suspended for periods ranging from three months to three years. Sixteen dealers, whose lack of supervision or system inadequacies allowed rat trading to occur, were in most cases publicly reprimanded, except in the more serious of these cases when short periods of suspension were awarded.

### **Investigations - Disciplinary Cases of Particular Interest**

3.13 Disciplinary cases of particular note resulting from investigations by the Enforcement Division and which were concluded during the year are detailed in the following paragraphs:

#### **Jardine Fleming Investment Management Limited**

3.14 On 29 August 1996 the SFC publicly reprimanded Jardine Fleming Investment Management Limited (JFIM) for failures of supervision and internal controls which allowed Colin Armstrong, a former director and senior fund manager of JFIM, to preferentially allocate trades to benefit his personal account and one particular client account to the disadvantage of funds and accounts managed by JFIM. The SFC revoked all registrations for both Colin Armstrong and Robert Thomas, the former Managing Director of JFIM, who accepted responsibility for JFIM's supervisory failures.

3.15 The public reprimand of JFIM took into account its cooperation in the investigation, its voluntary payment of compensation in the amount of HK\$148.96 million to the disadvantaged funds and accounts, and the remedial action taken.

3.16 The SFC's action coincided with an announcement by the Investment Management Regulatory Organisation Limited (IMRO) that it had fined Jardine Fleming Asset Management Ltd (JFAM) (an associated company of JFIM) and three Robert Fleming group companies a total of £700,000 for failing to properly supervise JFIM's management of funds delegated to it by them. IMRO also revoked JFAM and Robert Thomas' registration with IMRO (Robert Thomas was also managing director of JFAM).

#### **Frankwell Commodities Limited**

3.17 On 3 October 1996, the SFC publicly reprimanded Frankwell, a registered commodity dealer, its two dealing directors, Mr Johnny Sum Tai Chung, and Mr Andrew Strachan, and the major shareholders of Frankwell, Mr Wilson Lai Chan Kow, and Mr Frank Shum Tai Tung. This action related to:

a) failings by Frankwell to comply with the licensing requirements for dealers under section 3 of the LFETO in that its staff introduced clients to a Macau company to trade forex on a leveraged basis when the company was not licensed as a leveraged foreign exchange trader; in that it encouraged staff to hawk futures contracts by telephone as its main way of soliciting business, contrary to section 60A of the Commodity Trading Ordinance; and to satisfy the SFC it was and would continue to be able to meet the requirements imposed by the Financial Resources Rules; and

b) the fact that Strachan and Sum, although accredited to Frankwell as dealing directors with responsibility for the day-to-day operations of Frankwell, were directors in name only. All major decisions were made by the major shareholders, Lai and Shum, who acted as shadow directors and therefore bore ultimate responsibility for Frankwell's failings.

3.18 In deciding upon the action, which was taken in consultation with the HKFE, the SFC took into account that Frankwell had ceased business on 26 September 1996 and it, as well as Sum and Strachan, had requested the SFC to revoke their registrations. They all undertook not to re-submit any application for re-registration for a period of five years. In the case of Lai and Frank Shum, they also undertook not to submit applications for registration for themselves or for any entity in which they were directors, shareholders or partners for a period of five years and then only if an independent director with responsibility for corporate compliance acceptable to the SFC has been appointed.

3.19 On 19 November 1996, Lai and Frankwell pleaded guilty at Eastern Magistracy in relation to the unlicensed forex activity of Frankwell. They were fined a total of \$50,000 and ordered to pay costs totalling \$24,000 to the SFC.

#### **Salomon Brothers Hong Kong Limited**

3.20 On 28 February 1997, the SFC publicly reprimanded Salomon for failures within its Private Investment Department (PID) during the period April 1993 to March 1994. The failings resulted in certain account executives within the PID not being promptly registered with the SFC, and certain staff of the PID, when marketing Collateralised Mortgage Obligations, not fully explaining to their clients the risks involved in holding such products. When the bond market collapsed in February 1994, several of these clients incurred considerable losses as a result of holding high risk versions of this product. The public reprimand took into account prompt remedial action taken by Salomon at its own initiative, including the compensation of clients and the closure of the PID.



## Investigations - Other Disciplinary Actions

3.21 During the year, 3 dealing directors, 3 dealer's representatives and 1 leveraged foreign exchange trader were publicly reprimanded for minor transgressions in the conduct of their business. One dealer's and 2 dealer's representatives' registrations were suspended for periods ranging from one to three months for, among other things, concealing their trading, or facilitating trading of others, by the use of nominee accounts. In addition, 3 dealer's representatives, who misappropriated clients' shares, had their registrations revoked; the activities of these representatives were also the subject of enquiry by the Royal Hong Kong Police.

## Investigations - Unregistered Dealing and Related Offences

3.22 The SFC continued its enforcement action against registered dealers who employ people to act as their representatives, but who have not been registered with the SFC. In addition, the SFC continued to pay special attention to enforcing compliance with the LFETO, which

mainly involved prosecutions against individuals for holding themselves out as carrying on a business of leveraged foreign exchange trading as agents for companies, based in Macau, whilst not licensed. This action not only resulted in 22 persons being prosecuted, but also disciplinary action being taken by the SFC against 9 registered/licensed persons; all of them were issued with public reprimands. Details of prosecutions and fines can be found in Table 1.

## First Prosecution Resulting from Surveillance of the Internet

3.23 During the year, the SFC brought its first prosecution as a result of surveillance of the Internet. An individual in the United Kingdom, Mr Richard Woodhead, claiming to be an investment adviser, placed an open message on Compuserve's Hong Kong forum indicating that he could earn a 35% return for investors and inviting interested investors to contact him. A staff member from the Enforcement Division, posing as a prospective investor and replying via e-mail, learnt that the investment concept related to leveraged foreign exchange trading. When

Table 1  
Results of Prosecutions: 1 April 1996 to 31 March 1997

### Unregistered Dealing and Related Offences

Case No.	Defendant	Date of conviction	No. of summonses involved	Fine (\$)	Cost of Investigation awarded (\$)
<b>Securities Ordinance</b>					
1	New Land Promotions Ltd	13 May 96	1	40,000	21,800
	Tsoi Ping Kwan		1	40,000	21,800
2	Lee Ka Leung	28 May 96	1	15,000	9,730
	Chow Wing Yin		1	20,000	4,000
3	Chan Chee Kong	20 Aug 96	2	2,000	6,600
4	Wong Chun Tung	24 Sep 96	1	4,000	6,000
	Get Nice Investment Ltd		1	7,000	9,000
	Shum Kin Wai		1	7,000	9,000
<b>Leveraged Foreign Exchange Trading Ordinance</b>					
5	Chan Sheung Ching	4 Jun 96	1	30,000	26,319
6	Yeung Ping Kwan	25 Jun 96	1	30,000	28,960
7	Si Yeung Fai	10 Sep 96	3	60,000	28,960
8	Richard Woodhead	2 Oct 96	1	10,000*	13,695
9	Bright Capital investment Ltd	15 Oct 96	1	30,000	-
	Ho Wing Cheong, Terence		1	15,000	15,000
	Tong Suk Po		1	15,000	15,000
10	Tang Tat Yau	29 Oct 96	2	13,000	29,582
	Wong Man Tat		1	10,000	23,171
	Pok Sze Wing		3	16,000	44,575
11	Frankwell Commodities Ltd	19 Nov 96	1	25,000	12,000
	Lai Chan Kow		1	25,000	12,000
12	Cheung Kit Wai	28 Jan 97	1	50,000	19,165
	Ng Mau Chung		1	50,000	19,165
			28	514,000	375,522

\* or in default 30 days imprisonment

Woodhead arrived in Hong Kong, further contact was made and confirmation obtained in relation to his activities. He was convicted at Western Magistracy for holding himself out as carrying on a business of leveraged foreign exchange trading whilst not licensed. Woodhead was fined \$10,000 or, in default, a 30 days term of imprisonment, and ordered to pay costs of \$13,695 to the SFC.

### Misrepresentation to obtain a registration

3.24 During the year 10 persons were successfully prosecuted for providing false information in their application to be licensed or registered as representatives. Details of these prosecutions can be found at Table 2.

### Investigations - Protection of Investors Ordinance

3.25 There was a significant decrease during the year in investigations into potential breaches of the Protection of Investors Ordinance (PIO), in particular the promotion of unauthorised investment arrangements to the public. There was only one prosecution, brought on 20 August 1996, when Skysen Development Limited pleaded guilty to 15 summonses in relation to the issue of unauthorised advertisements concerning the sale of property in China. The advertisements were issued under a scheme which constituted an investment arrangement under the PIO in that investors in the development were guaranteed that the price of property they purchased would appreciate between 20 to 25% annually. The company was fined \$90,000 and ordered to pay costs of \$17,234 to the SFC.

Table 2

#### Results of Prosecutions: 1 April 1996 to 31 March 1997

##### Misrepresentation to obtain registration

Case No.	Defendant	Date of conviction	No. of summonses involved	Fine (\$)	Cost of Investigation awarded (\$)
1	Kong Man Wai	25 Jul 96	1	15,000*	15,000
2	Chan Shiu Kai	7 Aug 96	1	7,500	7,634
	Yeung King Lau		1	7,500	7,143
	Li Pun Wing		1	7,500	6,898
	Cheung Chi Wai		1	7,500	6,048
3	Tam Chui Yan	7 Aug 96	1	7,500	3,926
4	Wong Ah Shing	6 Nov 96	1	5,000	7,000
	Sam Lai Ying		1	5,000	6,000
5	Tong Tak Wai	17 Dec 96	1	5,000	-
6	Tong Chung Wai	17 Jan 97	1	10,000	3,500
			10	62,500	63,149

\* and sentenced to four months' imprisonment, suspended for two years

### Investigations - Short Selling

3.26 During the year, 57 persons were prosecuted for short selling, details of which can be found in Table 3. Short selling contravenes section 80(1) of the Securities Ordinance, which prohibits the sale of securities when the seller does not have a presently exercisable and unconditional right to sell.

3.27 Of the 57 persons prosecuted for short selling, 19 were registered persons. Six were publicly reprimanded for their short selling activities whilst the remainder were also disciplined for other activities, including rat trading. In addition, 2 registered dealers and 3 dealer's representatives were publicly reprimanded for failing to ascertain whether their clients had scrip to settle transactions and for failing to implement sufficient compliance procedures to prevent and detect short selling. These failings potentially jeopardise the settlement process.

### Investigations - Takeovers Code Matters

3.28 The Enforcement Division cooperates with the Takeovers Executive in investigating potential breaches of the Takeovers Code and in verifying information provided to the Takeovers Executive. It also carries out investigations for the Takeovers Panel. In many cases, investigations are initiated whilst takeover transactions are underway, in which case the emphasis is on securing fair treatment for shareholders rather than on imposing sanctions after breaches have occurred. The types of outcome that are sought in these cases include having a general offer made to minority shareholders when none was previously forthcoming; having an offer price increased to that required by the Takeovers Code (the highest price paid by any



member of a concert party in the preceding six months); or requiring shareholders who are not regarded as independent to abstain from voting at meetings of shareholders in relation to the takeover.

3.29 It is usually not possible to release information about cases of this nature where SFC intervention is successful except when the Takeovers Panel decides to publish its findings.

### Investigations - the Securities (Disclosure of Interests) Ordinance (SDIO)

3.30 The SFC has continued during the year to monitor compliance with the SDIO. This resulted in two prosecutions:

- On 4 September 1996, Mr Chau Shek Cheong, a non-executive director of Kin Son Electronics (Holdings) Company Limited, was successfully prosecuted for failing, in May 1995, to notify the SEHK within five days of his ceasing to be interested in 82,345,191 shares of Kin Son. He was fined \$5,000 and ordered to pay costs of \$13,303 to the SFC.
- On 12 November 1996, Mr Li Chun, the Chairman of Best Wide Group Limited, was successfully prosecuted for failing, in October 1995, to notify the SEHK within five days of his ceasing to be interested in 6,036,000 shares of Best Wide. He was fined \$21,000 and ordered to pay costs of \$34,000 to the SFC.

3.31 In addition to prosecutions, warning letters were sent to 66 persons for minor and inadvertent breaches of the Ordinance.

### Investigations - Insider Dealing

#### Yanion International Holdings Limited

3.32 An inquiry by the Insider Dealing Tribunal concluded that there was insider dealing in the shares of Yanion International Holdings Limited between 8 March 1993 and 12 May 1993 arising out of dealings in that company's shares by Danbridge Investments Limited, Golden Key Investments Limited and Langer Services Limited. The motive behind these dealings was to avoid the loss that was likely to occur after the announcement of Yanion's 1992 results, which showed a profit for the year ending 31 December 1992 of \$2.43 million, compared to over \$39 million for the year ending 31 December 1991 ("the relevant information").

3.33 The Tribunal identified five insider dealers:-

- Leung Wah Chai, the Chairman of Yanion
- Butt Ching-han, Leung's sister-in-law, an employee of

Yanion, and a director of Danbridge and Golden Key

- Danbridge, Golden Key and Langer

3.34 The Tribunal decided that Leung provided the relevant information, directly or indirectly, to Butt knowing she would make use of such information for the purpose of dealing, through the three companies, in the listed securities of Yanion, and that he counselled or procured Butt to deal in the listed securities of Yanion through the three companies knowing that she would deal in them.

3.35 The Tribunal made orders against the insider dealers to pay the following amounts:-

	Leung	Butt
a) Loss Avoided	\$1,464,180	-
b) Financial Penalty	\$1,700,000	\$300,000
c) Expenses of the Enquiry	\$3,500,000*	-
Total	\$6,664,180	\$300,000

\* estimate

3.36 The Tribunal took the view that Butt was at all times acting for and on behalf of Leung when she dealt on insider information and that the brunt of the financial penalty should be borne by Leung.

3.37 In addition to imposing financial penalties, the Tribunal issued an order prohibiting Leung and Butt, for a period of one year from 1 December 1996, from being directors of any listed company, or being involved in the management of any listed company.

#### CNPC (Hong Kong) Limited (formerly Paragon Holdings Limited)

3.38 On 13 November 1995, the Financial Secretary appointed the First Division of the Insider Dealing Tribunal to inquire into and determine whether insider dealing had taken place in relation to the listed securities of CNPC (Hong Kong) Limited during the period 3 March to 7 May 1993. The Tribunal held its substantive hearings between 25 March 1996 and 16 August 1996 and its report has yet to be published.

#### Hong Kong Parkview Group Limited (HKPV)

3.39 An inquiry by the Insider Dealing Tribunal concluded that Mr Hwang Chou Shiuan had dealt as an insider when purchasing 974,000 shares of HKPV on 13 August 1993. The Tribunal found that at the time of his dealings, Hwang had reason to believe that China International United Petroleum and Chemicals Company Limited (UNIPEC), a PRC company, would purchase by private placement 89 million HKPV shares. According to market sentiment at that time, such a substantial purchase by a PRC company, if it had been generally known, would have been interpreted as being very positive for the company. Indeed in the three days after the announcement of the

placement on 17 August 1993, the price for HKPV rose from \$3.20 to \$4.325.

3.40 The Tribunal concluded that at the time of his dealings, Hwang was a "person connected with" HKPV because he had represented HKPV in making the offer to UNIPEC in respect of the placement of HKPV shares.

3.41 The Tribunal made orders against Hwang to pay the following amounts:-

a)	Unrealised Profit	\$1,065,550
b)	Financial Penalty	\$1,065,550
c)	Expenses of the Inquiry	80% of the expenses of and incidental to the inquiry

3.42 In addition to imposing financial penalties, the Tribunal issued an order prohibiting Hwang for a period of six months from being a director of HKPV or any of its subsidiaries, or from being involved in their management.

#### Chevalier (OA) International Limited

3.43 On 14 August 1996, the Financial Secretary appointed the Second Division of the Insider Dealing Tribunal to inquire into and determine whether insider dealing had taken place in relation to the listed securities of Chevalier (OA) International Limited arising out of the dealings in the listed securities of that company by Mr Chow Yei Ching (the Chairman of the company) during the period 26 April 1993 to 5 July 1993 (inclusive). The Tribunal commenced public hearings on 10 March 1997; the hearings are continuing.

#### Hong Kong Worsteds Mills Limited

3.44 On 23 January 1997, the Financial Secretary appointed the Second Division of the Insider Dealing Tribunal to inquire into and determine whether insider dealing had taken place in relation to the listed securities of Hong Kong Worsteds Mills Limited during the period from 6 May to 16 June 1993 (inclusive). The Tribunal held a preliminary hearing on 20 March 1997 and is expected to commence substantive hearings in June 1997.

#### Other Cases

3.45 Five cases were referred during the current year resulting in the Financial Secretary appointing the Insider Dealing Tribunal to inquire into three; Hong Kong Parkview Group Limited, Chevalier (OA) International Limited and Hong Kong Worsteds Mills Limited. The Financial Secretary's decision as to whether or not to appoint the Tribunal to inquire into the remaining two cases is awaited.

### Investigations - Market Manipulation

3.46 The SFC continues to devote resources to the investigation of apparent cases of market manipulation. Most of these cases, which are highly resource intensive, are not public. There has, however, been one exception during the year, details of which are provided in the following paragraphs.

#### Real Grant Limited

3.47 As a result of suspicions that Real Grant Limited may have been involved during the period 1 April 1995 to 22 February 1996 in the manipulation of the share prices of a number of companies listed on the SEHK, including but not limited to Dah Hwa International (Holdings) Limited; Ngai Hing Hong Company Limited; Chaifa Holdings Limited; and Wing Fai International Limited, the SFC launched an investigation under Section 33 of the SFCO.

3.48 When Notices issued under Section 33(4) of the SFCO requiring production of banking and trading records were served on Real Grant in furtherance of that investigation, the company initially challenged the SFC's authority to conduct such an investigation and then sought to limit the information it was required to produce.

3.49 This resulted in an application to the High Court under Section 33(13) of the SFCO which was concluded on 27 February 1997. Mr Justice Rogers, after considering the evidence before him, including an affirmation by the principal shareholder and director of Real Grant Limited, Mr Victor Choi Hok Wan, indicated that he viewed as "very serious" Real Grant Limited's failure to produce the documents which it was legally obliged to produce to the SFC's investigators. However, as Real Grant Limited eventually complied, he took the view that it was not a case of obstinate refusal but a culpable failure to comply. Accordingly, in addition to ordering Real Grant to pay the full costs of the SFC on an indemnity basis, he imposed a fine of \$650,000.

### Inspection of Books and Records of Listed Companies

3.50 Section 29A of the SFCO empowers the SFC to inspect a listed company's books and records if its directors and officers are suspected of impropriety in the management of a company's affairs. During the year, the power was invoked on one occasion.



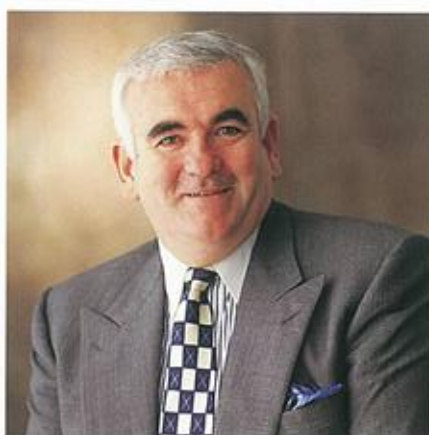
Table 3

**Results of Prosecutions: 1 April 1996 to 31 March 1997****Short selling**

Case No.	Defendant	Date of conviction	No. of summonses involved	Fine (\$)	Cost of investigation awarded (\$)
1	Ko Wing Yee	16 Apr 96	9	18,000	5,928
2	Ma Man Kuen	7 May 96	4	16,000	7,159
	Chan Wai Hung		13	48,000	10,300
3	Chu Hau Yee	7 May 96	2	8,000	9,548
4	Ho Tak Wing	4 Jun 96	8	16,000	6,900
	Lui Lok Pun		5	7,500	3,450
5	Tsun Pui Keong, Albert	18 Jun 96	41	205,000	19,128
6	Leung Hin Kwong Caine	18 Jun 96	10	25,000	12,680
	Lee Kwok Fai Wilfred		2	4,000	2,536
7	Chiang Yu Chi Diana	18 Jun 96	5	15,000	4,175
8	Chun Ping Kwong	2 Jul 96	25	125,000	53,000
	Chun Hing Mui		5	12,500	13,000
9	Lo Tak Kwan	9 Jul 96	8	20,000	12,191
	Wong Siu Wah		3	9,000	3,045
10	Hui Man Kin	16 Jul 96	3	12,000	2,300
	Lou Tung Ming		3	12,000	4,000
11	Wu Chun Hong	23 Jul 96	18	45,000	5,800
	Ng Lai Sze		12	30,000	7,600
	Yu Kwok Pui		2	5,000	7,600
	Cheung Kam Mui		8	16,000	6,100
12	Lau Chong Ho	24 Jul 96	4	8,000	-
13	Pang Yuk Chuen	26 Jul 96	9	9,000	5,000
14	Ho Chi Kwong	20 Aug 96	1	2,500	8,100
	Heung Wai Lun		26	31,200	6,100
	Chan Chee Kong Danny		7	5,600	10,000
15	Cheung Kit Fong	27 Aug 96	3	6,000	4,900
	Tong Man Yee		1	2,000	4,000
16	Chan Steven Kwok	27 Aug 96	1	28,000	6,300
17	Tse Siu Ha	8 Oct 96	7	28,000	10,895
18	Chu Yin Ming	8 Oct 96	7	14,000	8,759
	Wan Yuk Wah		6	24,000	11,382
	Chan Wing Pai		3	12,000	13,356
19	Chan Chi Wing	8 Oct 96	13	52,000	7,300
20	Ng Chi Ming	15 Oct 96	6	36,000	6,600
21	Chu Oi Ching	12 Nov 96	8	24,000	3,000
	Pang Yip Kuen		7	21,000	3,000
22	Lau Lung Shan	3 Dec 96	8	20,000	3,400
23	Tang Guo Hua	24 Dec 96	5	15,000	5,658
	Sun Lik		1	3,000	3,983
24	Cheung Kwok On	7 Jan 97	12	24,000	5,200
25	Lim Thian Hu	21 Jan 97	16	32,000	6,615
	Chong Ping		4	40,000	3,300
26	Lam Chak Chuen	18 Feb 97	14	28,000	2,661
	Fan Yuen Han		5	10,000	1,474
27	Chu King Kau	25 Feb 97	1	5,000	16,000
	Ng Sau Tung		1	3,000	2,000
	Kam Wun Fat		1	4,000	16,000
	Chan Chun Ming		2	5,000	1,900
	Tse Yung Nam		3	6,000	1,800
	Chan Hay Yin		6	12,000	1,600
	Mak Chun Kong		28	84,000	5,300
28	Wong Siu Chin	4 Mar 97	2	5,000	2,300
	Lai Kam Hung		22	33,000	3,600
	Poon Chun Keung		8	16,000	3,100
	Wai Yuk Chun		3	7,500	2,500
29	Lam Kin Chiu, Tommy	11 Mar 97	10	30,000	6,200
	Wang Hing Ting, Barry		5	20,000	7,300
			452	1,354,800	407,023

### FUNCTIONS

4.1 *The functions of the Supervision of Markets Division include, among others, the responsibility for supervising and monitoring the activities of the Exchanges and Clearing Houses; encouraging the development of the securities and futures markets in Hong Kong and the increased use of such markets by investors in Hong Kong and elsewhere; promoting and developing self-regulation by market bodies in the securities and futures industries; and overseeing and managing Hong Kong's Investor Compensation Funds.*



**David J White** is Executive Director responsible for the Supervision of Markets Division and for Research and Policy.

### CURRENT POLICY INITIATIVES

4.2 *During the past year, the Division has worked to maintain and enhance the integrity of the stock and futures markets and the Exchanges and Clearing Houses' effectiveness in providing fair, orderly, efficient and transparent marketplaces and facilities for the clearance and settlement of transactions for both domestic and international investors.*



4.3 The Division has devoted considerable resources to pursuing, in cooperation with the respective market bodies, various development initiatives. Several of the principal matters dealt with in both the areas of enhanced market integrity and market development include:

- publication for public consultation of internal control guidelines for persons registered with the SFC;
- establishment of a steering committee to set the way forward for the creation and development of a Hong Kong securities industry education institute;
- research and analysis from a market perspective into the recent growth in The Stock Exchange of Hong Kong Limited (SEHK) listed equity derivative warrant market;
- implementation of initiatives to enhance the trading and clearing operations of SEHK-listed stock options;
- further relaxation of the enhanced short selling regime on the SEHK;
- implementation of enhancements to one-day rolling currency futures contracts on the Hong Kong Futures Exchange Limited (HKFE);
- migration of trading of stock futures from open-outcry on the HKFE trading floor to the exchange's screen-based automated trading system (ATS);
- approval of a new category of membership on the HKFE, to help provide a lower cost of entry for market makers in non-equity products;
- introduction of long-dated HSI option contracts on the HKFE;
- continuation of levy holidays for SEHK stock options and HKFE one-day rolling currency futures;
- establishment of a working group to consider the use of automated trading systems; and
- participation in the SEHK's working group on new

market development, which seeks to provide local access to regional investment products.

## Subject Matters

### Stock Options

4.4 During the year, the SEHK and SEHK Options Clearing House Limited (SECHK) implemented a number of initiatives to enhance the stock options trading and clearing operations. The Division recommended that the Commission approve the various initiatives and related rule changes. These include improvements to margin and collateral procedures, modifications to market makers' obligations, introduction of automatic exercise in certain circumstances, and approval of new option stocks.

4.5 The Financial Secretary indicated in his 1996 budget speech that the Government would provide stamp duty concessions for stock option market makers in relation to their hedging transactions in the underlying stock with a view to providing a stimulus to the options market and trading in the underlying stocks. To facilitate the introduction of the stamp duty concession, the Division assisted the Inland Revenue Department in drafting the Stamp Duty (Jobbing Business)(Options Market Makers) Regulation, which went into effect on 1 June 1996. The Division also recommended to the Commission that it approve related changes to the SEHK Rules. The changes prohibit an options market maker from identifying a transaction as jobbing unless it satisfies the criteria prescribed by the Collector of Stamp Revenue. The changes also impose a record-keeping requirement in relation to market-maker hedging transactions.

Figure 1  
**Stock Exchange of Hong Kong**  
**Turnover of Stock Option Contracts**  
April 1996 - March 1997

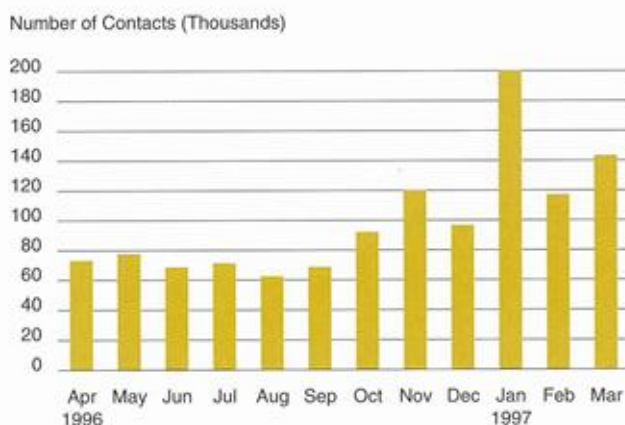
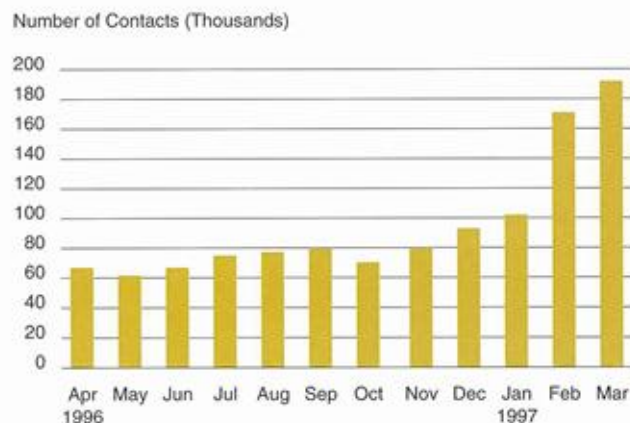


Figure 2  
**Stock Exchange of Hong Kong**  
**Average Daily Open Interest of Stock Option Contracts**  
April 1996 - March 1997



#### SEHK Working Group on New Market Development

4.6 In June 1996, the SEHK formed the Working Group on New Market Development. The Working Group comprises representatives from merchant banks, fund managers, stockbrokers, the SEHK and the SFC (represented by the Executive Director of the Division).

4.7 Thus far, the Working Group has focused on the suitability of trading regional derivative warrants, convertible bonds and depository receipts on the SEHK. During its fourth meeting, held in December 1996, members agreed to expand the existing derivative warrant market on the SEHK to include derivative warrants on regional exchanges. A list of acceptable exchanges has been established. Members also agreed to move towards the early introduction of overseas convertible bonds on the SEHK. The SEHK has invited issuers and their advisers with an interest in developing this market to present proposals for its consideration.

#### Analysis of SEHK Equity Derivative Warrant Market

4.8 The SEHK listed equity derivative warrant market has experienced marked growth in the past year. The market has essentially tripled in terms of number of listings (109 to 296) and market value (\$11,249.15 million to 31,686.04 million).

4.9 With a view to obtaining a more comprehensive understanding of this rapidly expanding market, its implications for the derivatives market and the underlying cash market, the Division has conducted a number of ad-hoc and ongoing discussions with the SEHK and market participants. A Working Group has been set up between the Division, the Corporate Finance Division and the SEHK to monitor the situation. A market database is also being maintained by the Division.

4.10 In one recent quantitative study, the Division obtained details on the positions and hedges taken by warrant issuers over a specific time period. This study has provided valuable information on market participants' risk management practices and their potential collective behaviour under different market conditions.

#### Relaxation of the Short Selling Regime

4.11 In February 1996, the Commission approved the expansion of the list of Designated Securities eligible for short selling to 113 securities, including all Hang Seng Index ("HSI") constituent stocks, the 50 largest non-HSI capitalised stocks and the balance of Hang Seng MidCap 50 Index constituent stocks that are not included in the 50 largest capitalised stocks. Also the "tick rule" was eliminated, obstacles to the reporting of short selling activities were removed and the reporting system was enhanced. A review of the revised regime was conducted by the SEHK in

October 1996 and the results were satisfactory. Reporting of short selling activities has increased, and there has been no evidence of problems with the SEHK's monitoring system.

4.12 In January 1997, the SEHK proposed additional modifications to the short selling regime. The proposals include allowing SEHK members to conduct direct business transactions with and for clients in short selling; removing the registration requirement for Short Selling members; further expanding the list of Designated Securities to include all constituent stocks of the Hang Seng China Enterprises Index, stocks with an associated derivative product and stocks which upon listing would fall within the 50 non-HSI largest capitalised stocks category; and allowing a stock which has been admitted as a Designated Security to remain on the list. After careful consideration, the Commission approved the proposals in its February 1997 meeting. The Commission, however, requested the SEHK to consult with it in setting the additional criteria for the selection of new Designated Securities, and specifically to exclude illiquid stocks and stocks believed to be the subject of misconduct.

#### SEHK Working Group on Corporate Communications

4.13 To consider ways to improve communications between listed companies and beneficial owners, the SEHK set up a Working Group with the Federation of Share Registrars, the Hong Kong Securities Clearing Company Limited (HKSCC) and the SFC. A Consultation Paper on a working model to improve communications was published in June 1996. In summary, the model provides for issuers, via their registrars, to send corporate communications directly to beneficial owners based on names and addresses supplied by brokers through HKSCC.

4.14 In October 1996, the Working Group recommended the first phase of the model be introduced in relation to the Central Clearing and Settlement System (CCASS) segregated account, with statement service and without any formal rule changes. This phase is now in operation. The HKSCC has also prepared a more detailed description of the working model to facilitate introduction of the second phase of the project. It has determined that the Brokers' Back-Office Software system used by many brokers can be modified easily to support the communications process. Work is continuing towards introduction of the second phase.

#### Overseas Linkages

4.15 During the year, the HKFE entered into a linkage agreement with the New York Mercantile Exchange (NYMEX) with a view to introducing NYMEX's petroleum and other commodities contracts to Hong Kong through HKFE members, utilising NYMEX's ACCESS electronic



trading system. The Division continues to assist in this development and has been working closely with the HKFE and SFC's US counterparts on the establishment of the linkage.

#### One-Day Rolling Currency Futures (ODRCF)

4.16 During the year, the HKFE implemented several enhancements to improve the operation of the ODRCF market and also conducted a series of seminars to improve retail investors' knowledge and awareness of the product. The year also saw the launch of the British Pound ODRCF contract, on 20 September 1996, joining the Deutsche Mark and Japanese Yen ODRCF contracts. Trading activity in ODRCF contracts surged in the first quarter of 1997. Average daily volume in 1996 was 757 contracts, as compared to February and March 1997 averages of 1,812 and 2,410 contracts respectively.

4.17 To further increase retail investors' participation in the ODRCF market, the HKFE has recently proposed to the Division to introduce a set of handling procedures for stop-loss orders. Stop-loss orders are commonly used by retail investors in banks and leveraged foreign exchange products as a protective measure against their open positions in the event of adverse market movements. The Division is discussing the proposal with the HKFE.

#### New Category of HKFE Membership - Revitalisation of Hong Kong Interbank Offered Rate (HIBOR) Futures

4.18 At its March 1997 meeting, the Commission approved proposals by the HKFE to introduce a new membership scheme, including creation of a new category of shareholding in the form of "Non-Voting Redeemable Shares". The shares are designed to provide a lower cost of

entry for market makers in relation to non-equity products, particularly debt products such as HIBOR futures. The HKFE is also planning to migrate trading in HIBOR futures to ATS and to introduce market makers to this market.

#### Long-dated Options Contracts

4.19 In 1993, the HKFE began trading in the HSI Option Contract. This market has grown steadily with average daily turnover of approximately 4,400 contracts in 1996. To further develop this market, the HKFE proposed and the Commission approved in July 1996 the introduction of long-dated HSI options. This has expanded the contract months to 8, including 12 and 24 month contracts. Long-dated options are subject to modified trading rules and a request-for-quote process.

#### Stock Futures

4.20 Stock futures contracts were launched in March 1995, with trading conducted by way of open outcry on the HKFE trading floor under an order-driven environment. Since the launch, turnover in stock futures contracts has remained low. In an effort to revitalise this market and to enhance its transparency and efficiency, the HKFE proposed, with the Division's support, to migrate the trading of these contracts to its screen-based ATS. The proposal also included the introduction of a market maker system to enhance the liquidity of this market.

4.21 At its August 1996 meeting, the Commission approved the proposal and related rule amendments. On 14 February, 1997, stock futures contracts commenced trading on the ATS. Stock futures currently approved for trading include contracts on Cheung Kong Holdings, HSBC Holdings, and Hong Kong Telecommunications.

Figure 3  
**Hong Kong Futures Exchange**  
**Turnover of One-Day Rolling Currency Futures Contracts**  
April 1996 - March 1997

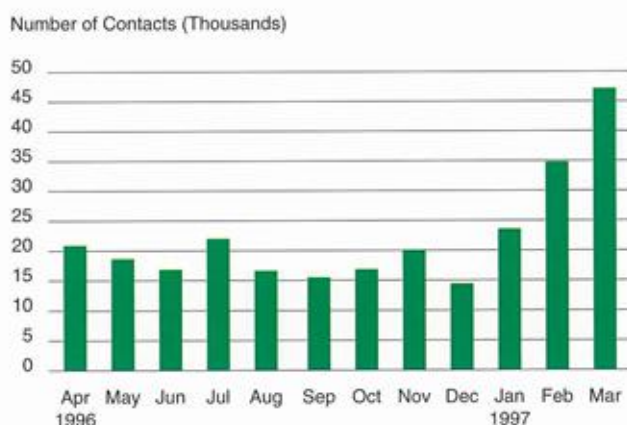
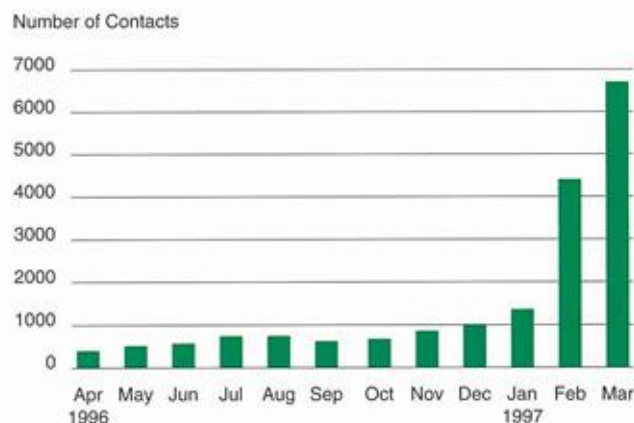


Figure 4  
**Hong Kong Futures Exchange**  
**Average Daily Open Interest of**  
**One-Day Rolling Currency Futures Contracts**  
April 1996 - March 1997





### Investor's Compensation Schemes

4.22 The Division continued to pursue recoveries of amounts previously paid out of the Compensation Funds pursuant to its subrogated rights against defaulting brokers. During the year, \$8,179.50 was recovered from a defaulting securities broker and \$2,264,093.28 was received from the SEHK as replenishment to the Unified Exchange Compensation Fund, after all relevant rights of action and other legal remedies of the SFC in relation to two defaulting stockbrokers was exhausted. Settlements with respect to commodity brokers that defaulted in 1987 resulted in the recovery of \$1,915,472.76.

4.23 During the year, no compensation payments were made out of the Commodity Exchange Compensation Fund. In regards to the Unified Exchange Compensation Fund, payments of approximately \$4 million were made to 117 claimants in relation to the defaulting broker, Bonus Securities Company, after recovery of the funds was received from the defaulting broker's Administrator.

4.24 An actuarial study undertaken by a consultant on each of the Funds was completed in October 1996. The two studies sought to evaluate the appropriate levels of the Funds under various types of compensation arrangements. The Division is now discussing the results of the study with the Exchanges and considering whether modifications should be made to the compensation arrangements. It is hoped that analysis will result in improvements to the level of coverage for individual investors.

4.25 As at 31 March 1997, the net asset value of the Unified Exchange Compensation Fund was approximately \$462.2 million and the Commodity Exchange Compensation Fund was approximately \$52.3 million.

### Internal Control Guidelines

4.26 The incidence of major losses by financial organisations due to so-called rogue traders, inadequate management or internal controls has highlighted the need for improved management and internal controls procedures. To help address this need, the Division published a consultation document on 28 November 1996 titled "Management, Supervision and Internal Control Guidelines". The purpose of the Guidelines is to provide guidance to registered intermediaries regarding the SFC's expectations in relation to internal controls. As part of the consultation exercise, a series of seminars was organised to explain the proposals and to receive direct feedback from market practitioners. Thirteen written submissions have been received and reviewed by Division staff. The consultation conclusions and final guidelines will be published in mid-1997.

### Standardisation of Education Requirements for the Securities Industry

4.27 The issue of establishing a cohesive, ongoing, educational and training process for participants in the securities industry in Hong Kong was first raised officially in a meeting of academic and professional bodies hosted by the SFC in December 1995. Participants in that meeting expressed general support for the establishment of a professional organisation whose primary function would be the promotion, through education, of high standards of professional conduct in the industry. Following that meeting, the SFC decided to undertake a study on how best to facilitate the development of industry training and accreditation policy for Hong Kong. A consultant was hired to undertake the study and met with various participants in the industry, higher education and Government. A paper was submitted to the SFC in September 1996. After considering various alternatives, the consultant recommended the establishment of an independent securities institute whose principal focus would be the development of training standards through the provision of industry courses and examinations.

4.28 Included among the principal recommendations of the consultant was the establishment of a Steering Committee made up of prominent members of the securities industry, who would set the way forward for the creation and development of the securities institute. Dr Edgar W K Cheng, Chairman of the SEHK, agreed to serve as Chairman of the Steering Committee. In addition to providing SFC representation on the Steering Committee, the Division is furnishing secretarial support. The first meeting of the initial members of the Steering Committee was held in February 1997. It was agreed in that meeting to pursue the establishment of the securities institute as an examination-based body. Overseas educational organisations will be consulted to ensure that appropriate examination standards are set. Terms of reference for the Steering Committee have been finalised, and the balance of its membership is being determined. In the near future, an industry discussion paper will be prepared.

### Levy Holidays for HKFE ODRCF & SEHK Stock Options

4.29 When ODRCF contracts were launched in November 1995, they were eligible for a six-month levy exemption arrangement, as stipulated in the Securities and Futures Commission (Levy)(Futures Contract) Order. And when the SEHK introduced stock options trading in September 1995, the Securities and Futures Commission (Levy)(Securities) Order ("the Securities Order") was amended to exempt stock options from the levy. The SFC has observed that for both markets the level of trading has



fluctuated, and that trading volume has not reached its potential.

4.30 In order to maintain an environment that is conducive to further market development, the SFC proposed to the Governor-in-Council, upon the request of both Exchanges, that the statutory levy on ODRCF be nil and requested a continuation of the 0% levy for stock options trading, with the situation of both markets to be reviewed in 12 months time. In October 1996, the Governor-in-Council approved the proposals. The nil levy provision for ODRCF became effective on 25 October 1996. The proposal for stock options did not require any change to the Securities Order.

#### SFC Working Group on Automated Trading Systems (ATSS)

4.31 In response to the emergence and use globally of ATSS, the SFC formed a Working Group in mid 1996 to consider the subject matter. The Working Group is chaired by a non-executive director of the SFC and includes representatives of the Exchanges and other professionals involved in the securities and futures markets. The Division provides secretarial and research support to the Working Group.

4.32 ATSS were broadly defined to include any automated system that provides a trading mechanism for securities or futures trading, but excluding the operations of the SEHK and HKFE. After considering the various types of ATSS operations, both internationally and in Hong Kong, and the regulatory regimes developed to date and being developed, the Working Group recommends a pragmatic and flexible approach for Hong Kong and provides a set of general principles in relation to ATSS operations. The Working Group provided its Report to the Commission in January 1997.

4.33 The Commission reviewed the Working Group's Report and considered the regulatory principles set out in the Report necessary and appropriate. The Commission also accepted the Working Group's recommendation to conduct a wider consultation and, based on the Report, published a Public Consultation Paper in February 1997, seeking additional views and comments on the Report. The consultation period ended on 15 March 1997. The Division is reviewing the submissions received.

#### Inter-market Coordination Committee

4.34 In view of the increasing sophistication of financial products and rapid advancement in technology used in the financial markets, the Division proposed the establishment of a standing committee, the Inter-market Coordination Committee. The Committee includes the chief executives of the SEHK, HKFE, HKSCC and SEOCH and a

representative of the Hong Kong Monetary Authority. The Committee advises the constituent bodies on matters which transcend their respective markets and makes periodic recommendations to improve the efficiency of, and to address systemic risk in, these markets.

4.35 The objectives of the Committee include assisting intermediaries in dealing with their capital positions, improving linkages between Hong Kong markets, and providing a forum for development of consistent policy and procedures on risk management. Since its establishment on 22 September 1995, five Committee meetings have been held.

4.36 The main issues discussed at these meetings include the possibility of same-day foreign currency money settlement, information sharing arrangements among Committee members including large risk exposure of clearing members and bank guarantee positions, the feasibility of cross-margining among the three clearing houses, a cross-market contingency plan, the benefits of the Real Time Gross Settlement system to the securities and futures markets, the development of the Hong Kong debt market and a standardised approach for capital adjustments effecting derivative products.

#### Money Laundering

4.37 During the year, the SFC continued to assist the Government in fulfilling Hong Kong's commitments with respect to the recommendations of the Financial Action Task Force (FATF) in combating money laundering. In June 1996, the FATF revised its 40 recommendations which will become effective in June 1998. The Division has forwarded the new recommendations to the SEHK and the HKFE and asked them to draw the attention of their members to the new recommendations. SFC staff are preparing amendments to the Money Laundering Guidance Notes issued by the SFC to intermediaries to reflect the FATF's new recommendations.

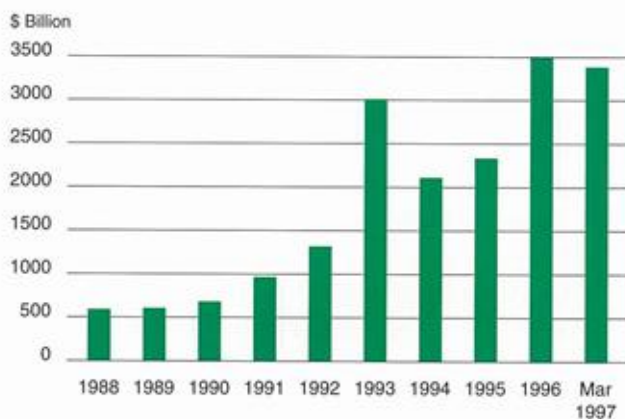
#### Inter-Market Competitive Study

4.38 The SFC invited the Pacific-Basin Capital Markets Research Centre of the University of Rhode Island to conduct a study on the trading of Hong Kong listed securities on the New York and London markets. The objective of the study is to analyse the relevant trading patterns, in particular the role of the relative competitiveness of the various markets. The study comprises a quantitative examination of relevant multi-market trading and its impact on market volatility, liquidity, and efficiency in price discovery and a qualitative analysis of trading by ways of interviews with selected dealers/market makers in London and New York. The report findings will be published in the SFC Bulletin.

Annex I

**Stock Exchange of Hong Kong  
Market Capitalisation**

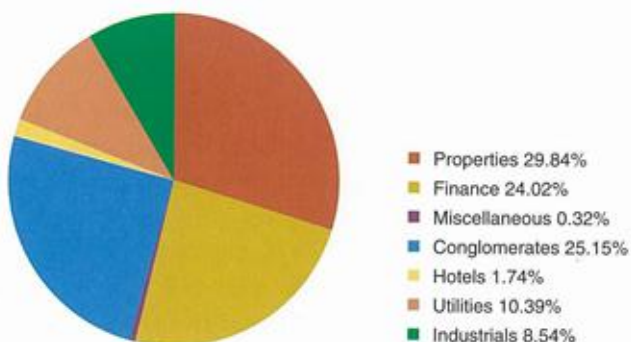
Year ended 31 December



Annex II

**Stock Exchange of Hong Kong  
Market Capitalisation**

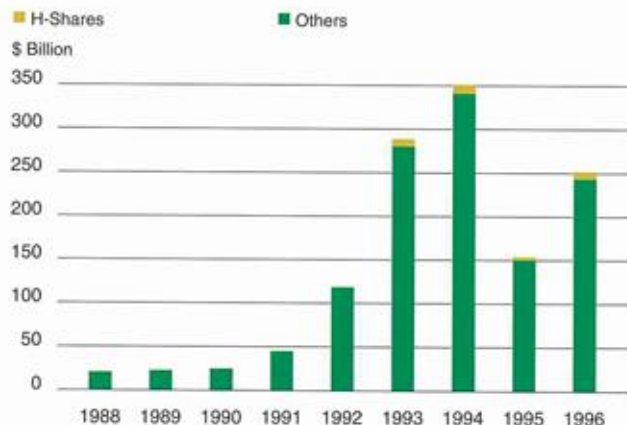
by sector as at 27 March 1997



Annex III

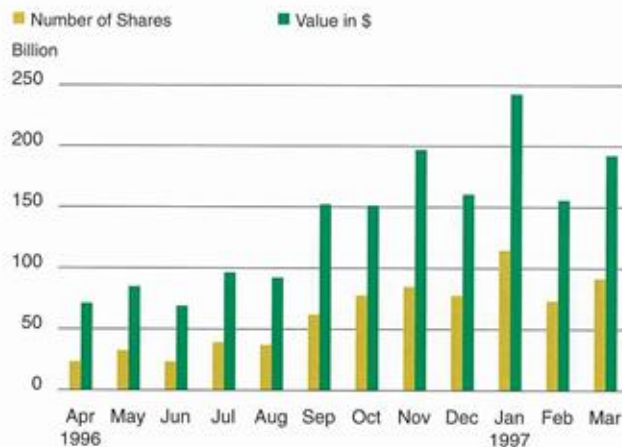
**Stock Exchange of Hong Kong  
Funds Raised**

Year ended 31 December



Annex IV

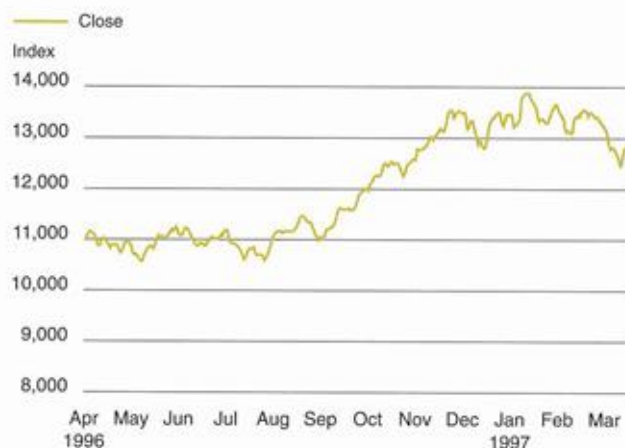
**Stock Exchange of Hong Kong  
Monthly Market Turnover**



Annex V (a)

**Hang Seng Index**

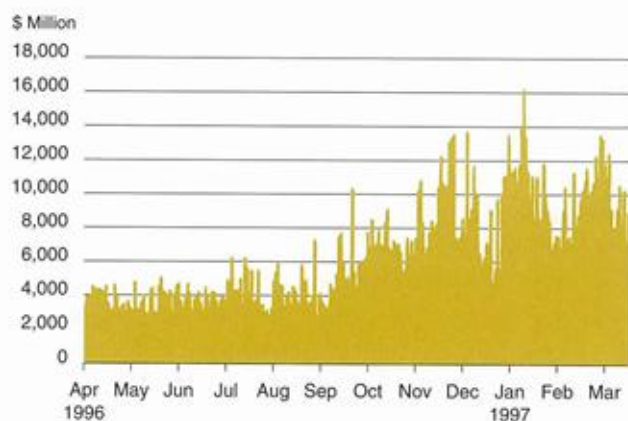
April 1996 - March 1997



Annex V (b)

**Daily Turnover by Value**

April 1996 - March 1997





## Annex VI

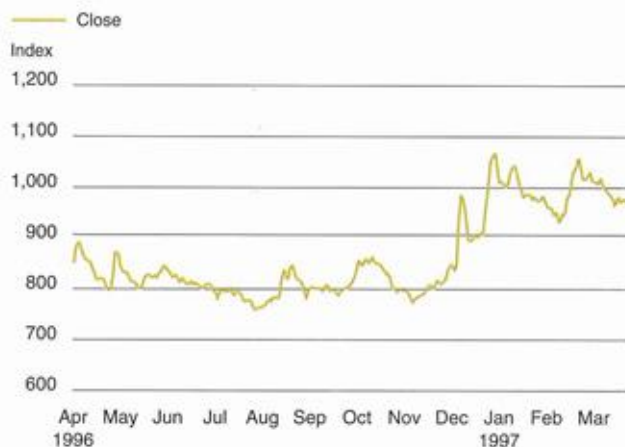
**Stock Exchange of Hong Kong  
Membership Statistics**

	Individual		Corporate		Total	
	No.	%	No.	%	No.	%
31 Dec 1988	621	83.92	119	16.08	740	100
31 Dec 1989	574	80.73	137	19.27	711	100
31 Dec 1990	542	78.78	146	21.22	688	100
31 Dec 1991	499	74.37	172	25.63	671	100
31 Dec 1992	423	68.23	197	31.77	620	100
31 Dec 1993	343	59.24	236	40.76	579	100
31 Dec 1994	284	50.44	279	49.56	563	100
31 Dec 1995	230	41.14	329	58.86	559	100
31 Dec 1996	209	37.12	354	62.88	563	100
31 Mar 1997	201	35.83	360	64.17	561	100

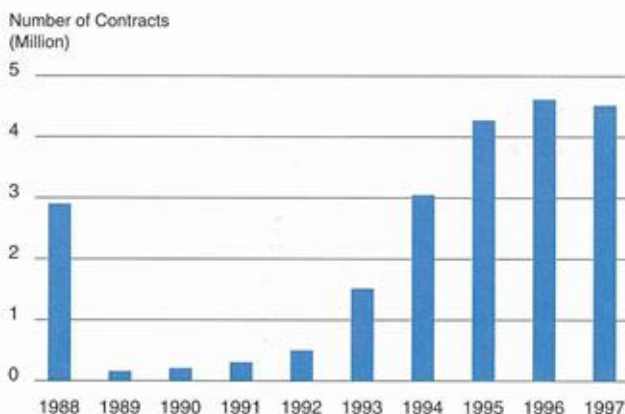
## Annex VII

**Hang Seng China Enterprises Index**

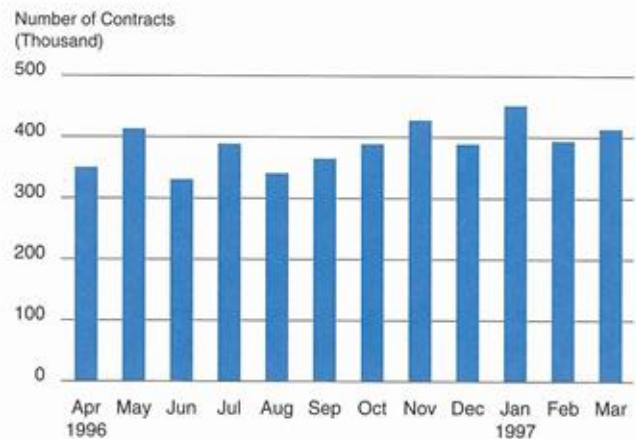
April 1996 - March 1997



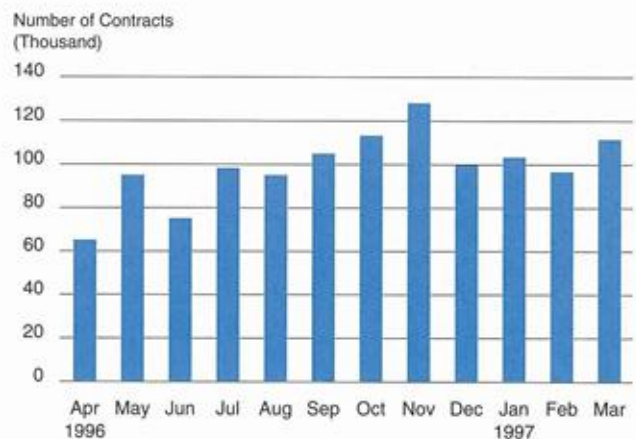
## Annex VIII

**Hong Kong Futures Exchange  
Turnover of Hang Seng Index Futures Contracts 1988-97**  
Year ended 31 March


## Annex IX

**Hong Kong Futures Exchange  
Turnover of Hang Seng Index Futures Contracts**  
April 1996 - March 1997


## Annex X

**Hong Kong Futures Exchange  
Turnover of Hang Seng Index Options Contracts**  
April 1996 - March 1997


## Annex XI

**Hong Kong Futures Exchange  
Number of Members**

31 Dec 1988	102
31 Dec 1989	97
31 Dec 1990	77
31 Dec 1991	80
31 Dec 1992	90
31 Dec 1993	107
31 Dec 1994	115
31 Dec 1995	115
31 Dec 1996	134
31 Mar 1997	134
Trader	0
Broker	5
Futures Commission Merchant	129
Merchant Trader	0

## International Regulatory Cooperation

### Regulatory Agreements

5.1 During the year the SFC continued its commitment to international regulatory cooperation with other jurisdictions. Four regulatory authorities namely, Comisión Nacional del Mercado de Valores of Spain (CNMV), the Securities Commission of New Zealand (NZSC), the Monetary Authority of Singapore and the Ontario Securities Commission signed Memoranda of Understanding (MOUs) with the SFC, bringing the total number of MOUs and similar cooperative arrangements to 24. The CNMV and NZSC possess powers to provide investigatory assistance, similar to section 59A of the Securities and Futures Commission Ordinance, which they are willing to exercise on behalf of the SFC. The SFC has also to date entered into 12 informal exchange of information arrangements with other overseas regulators.

5.2 Recent events have also highlighted the importance of international cooperation amongst regulators of investment management business. The SFC concluded a Declaration on Cooperation and Supervision of Cross-Border Investment Management Activity with the Institut Monétaire Luxembourgeois (IML) on 9 December 1996. This Declaration provides for exchange of information to enhance each authority's ability to regulate activities of persons involved in investment management which are registered with both authorities. The IML Declaration is particularly important in view of the large number of Hong Kong authorised funds domiciled in Luxembourg. Other countries have expressed interest in cooperative agreements in respect of investment management activity, and these will be pursued in the coming year.

5.3 A Memorandum of Regulatory Cooperation and Technical Assistance was concluded between the Intermediaries Division of the SFC and the Administration and Supervision Department of the State Administration of Foreign Exchange of the People's Republic of China. This Memorandum provides for mutual assistance and exchange of information to enhance each party's ability to protect market users, and to maintain market integrity in relation to trading of leveraged foreign exchange, foreign currency stock and foreign exchange futures contracts.

### The International Organisation of Securities Commissions (IOSCO)

5.4 IOSCO, which now has 134 regulatory authority members from 81 jurisdictions representing more than 85% of the world's capital markets, was formed to enable members:

- to cooperate to ensure better regulation of the markets, on the domestic as well as international level, in order to maintain just and efficient markets;
- to exchange information on their respective experience in order to promote the development of domestic markets;
- to unite their efforts to establish standards and an effective surveillance of international securities transactions; and
- to provide mutual assistance to ensure the integrity of the markets by a rigorous application of the standards and by effective enforcement against offences.

5.5 The SFC is an IOSCO member, and a member of its Technical Committee, which is made up of 16 IOSCO members which regulate some of the larger and more developed securities markets in the world. Its objective is to review major regulatory issues related to international securities transactions and to coordinate practical responses to these concerns. Anthony Neoh, QC, Chairman of the SFC, was appointed Chairman of the Technical Committee in 1996.

5.6 During 1996/97, the SFC continued to participate actively in the work of the Technical Committee, including the work of Working Party (WP) 1 on Multinational Disclosure and Accounting, WP2 on Regulation of Secondary Markets, WP3 on Regulation of Market Intermediaries, WP4 on Enforcement and Exchange of Information, and WP5 on Investment Management. The main issues dealt with by the Technical Committee and its Working Parties during the year are summarised below.

### Multinational Disclosure and Accounting

5.7 The work of WP1 on Multinational Disclosure and Accounting concentrates on accounting and auditing matters. The principal task of WP1 is to work with the International Accounting Standards Committee (IASC) to complete a core body of accounting standards that can provide a comprehensive financial reporting framework suitable for international equity offerings. The IASC has accelerated its work with the aim of completing the accounting standards in 1998. The Working Party is also discussing the status of international standards on auditing with the International Auditing Practices Committee and preparing a report on non-accounting disclosures.



## Regulation of Secondary Markets

5.8 WP2 on Regulation of Secondary Markets continued to work this year on the issues raised by the Windsor Declaration, including the monitoring and exchange of information in respect to large exposures and the establishment of a common default procedure. In addition, WP2 is involved in a number of post-Windsor initiatives.

5.9 First, WP2 has been mandated to develop "Event-Specific Guidance to Facilitate Information Sharing" amongst market authorities. Until recently, information-sharing was primarily concerned with fraudulent cross-border market activities and therefore focused on enforcement and market surveillance. However, the focus has now changed to identification of market participants and their trading activities. A tentative agreement has been reached amongst WP2 members on the form and content of the event-specific guidance, and a revised draft is now being prepared for further comments.

5.10 A second major initiative involves the examination of problems and opportunities associated with the use of Internet for securities and futures businesses. To assist this initiative, WP2 conducted an Internet survey and has held preliminary discussions on the issues identified in the survey. The SFC also distributed its consultation document, "Report of the SFC Working Group on Automated Trading Systems" to WP2 members during a recent meeting in Mexico City. The Working Party plans to explore further the potential benefits and implications of the Internet and other electronic networks for the regulation of secondary markets.

5.11 Third, WP2 is now preparing for the issuance to major financial regulatory bodies worldwide of a "Disclosure Framework for Securities Settlement Systems", which will take place following approval by the Technical Committee.

5.12 Amongst its other initiatives, WP2 has produced a survey questionnaire on Comparative Analysis of the Supervision Practices for Regulated Markets and Clearing Houses; is assessing the technical adaptability of members' financial market system components to the "Year 2000 Problem"; and is working with the International Standardisation Organisation on the issue of "Securities Messages Standardisation".

## Supervision of Market Intermediaries

5.13 The mandates assigned to WP3 of defining acceptable methodologies for determining minimum capital standards as well as surveys on systems and controls present an excellent opportunity for securities regulators to formulate responses to the challenges of the globalisation and erosion of the functional and institutional segmentation of finance.

5.14 First, WP3 has recently published a paper on Client Asset Protection. The paper summarises the principal methods whereby client assets are protected in all major jurisdictions. To permit each jurisdiction to assess where it stands in utilising the standards and practices described in the paper, the Technical Committee has approved a request by WP3 to develop a self-assessment questionnaire.

5.15 Second, in cooperation with a Committee of the Basle Committee on Banking Supervision, WP3 has also prepared a follow-up survey of the disclosure practices of banks and securities firms as reflected in their 1995 Annual Accounts. This joint Basle/IOSCO survey was published in November 1996.

5.16 Third, a task force has been created to carry out a collaborative project with the relevant sub-group(s) of Basle. The terms of reference are: *"A body of work aimed at defining acceptable methodologies for determining minimum capital standards and supervisory approaches to systems and controls as applied to internationally active securities firms. The capital standards would permit the use of models for the measurement of market risk under prescribed conditions. The standards would also address the appropriateness of the use of statistical techniques to assess credit risk and deal with the methodologies for taking account of funding and liquidity risks incurred by securities firms."*

5.17 Fourth, WP3 has agreed to conduct surveys on supervisory priorities and techniques, capital regulation, and systems and controls. The three surveys are a first step in WP3's use of the Working Party structure to develop a common understanding of these methods and practices.

## Enforcement and Exchange of Information

5.18 WP4 on Enforcement and Exchange of Information finalised its Report on "Measures Available on a Cross-Border Basis to Protect Interests and Assets of Defrauded Investors", which was presented to the Technical Committee in June. The Report, together with detailed information on the subject provided by most WP4 members and 12 other IOSCO members regarding their respective jurisdictions, was published during the IOSCO Annual Conference in September. The Report highlighted the problems confronting regulators in recovering assets of defrauded investors that have been moved to other jurisdictions. It also encouraged IOSCO members to examine the laws and procedures in their own jurisdictions and the need and scope for reform.

5.19 In accordance with the IOSCO Resolution on "Commitment to Basic IOSCO Principles of High Regulatory Standards and Mutual Cooperation", a Self-Evaluation Exercise of all IOSCO members was undertaken.



A sub-group of WP4 conducted a preliminary review of members' responses to this Exercise and presented its findings at the Technical Committee meeting in September 1996. At the Task Force meeting in January 1997 in Hong Kong, it was resolved that a report on certain key aspects of the Exercise should be presented at the next IOSCO Annual Conference in November 1997.

## Investment Management

5.20 Hong Kong continues to be an active participant in WP5 on Investment Management. In 1995, WP5 adopted a new work programme as a result of the Baring crisis. This resulted in the submission to the Technical Committee of papers addressing the issues of regulatory cooperation in emergencies, particularly with respect to suspension of dealing, and an examination of the custody issues affecting collective investment schemes. These papers were adopted by the Technical Committee at its meeting in Montreal in September 1996.

5.21 In 1996, WP5 also took on a new mandate, to review the issues relating to the supervision of fund managers. It is now developing a discussion paper on "Principles for the Supervision of Operators of Collective Investment Schemes", which is intended to be finalised in the coming year. It is hoped that the paper will assist IOSCO members in reaching a common understanding of the reasons why it is important to supervise operators of collective investment schemes, and those activities which are of prime importance in requiring effective supervision. It is also hoped that development of the Principles will enhance cooperation amongst IOSCO members in supervision of the increasingly global investment management industry.

## Ongoing Regulatory Cooperation

5.22 During the year the SFC received and processed 43 enforcement-related requests for information of which 23 were for non-public information. The SFC also received 253 licensing related requests for non-public information from overseas regulatory bodies. The SFC itself made 910 requests to overseas regulatory bodies for non-public licensing-related information and 14 requests for enforcement-related information.

5.23 In addition, the SFC received 14 requests from overseas regulatory authorities for investigatory assistance. The SFC exercised its powers under section 59A of the Securities and Futures Commission Ordinance and section 63A of the Leveraged Foreign Exchange Trading Ordinance in response to four and three of these requests respectively:

one to assist the Australian Securities Commission, three to assist the Securities and Exchange Commission of the United States (US SEC) and three to assist the US Commodity Futures Trading Commission, in accordance with the MOUs with these commissions. The assistance provided in these cases included obtaining non-public records and documents to assist overseas regulators.

5.24 The SFC also provided assistance to the British Columbia Securities Commission (BCSC) in the BCSC's investigation of Goldman Stanley Consultants Inc, Chinamax International Investment Ltd and Andy Chan Ying Leung. This assistance included arranging for an SFC staff member to give expert evidence concerning leveraged foreign exchange trading in Hong Kong to an administrative hearing by the BCSC. The BCSC announced on 27 March 1997 that on the basis of the findings of the administrative hearing it had banned Goldman Stanley and Chinamax from participating in the market in British Columbia and had fined Chan CS100,000 and banned him from participating in the securities market in British Columbia for thirty years.

5.25 The SFC obtained the assistance of the Ontario Securities Commission and the China Securities Regulatory Commission in serving notices to, and facilitating the attendance of, key witnesses for the purpose of Insider Dealing Tribunal hearings. Furthermore, the US SEC, in response to a request from the SFC, obtained certain securities trading records required for one of the SFC's investigations.

5.26 During the year, the SFC, through its Declaration on Cooperation and Supervision of Cross-Border Management Activity with the Investment Management Regulatory Organisation of the United Kingdom, exchanged non-public information and coordinated action during an investigation of Jardine Fleming Investment Management Limited. Details of this action can be found in paragraphs 3.14 - 3.16. The speed with which the investigation was concluded, the compensation paid to investors and the strong disciplinary action taken illustrate the extent to which such international cooperation can enhance the SFC's investigative and disciplinary efforts.



### Legislation

#### Composite Securities and Futures Bill

6.1 On 16 April 1996, after many years of deliberation and discussions with various interested parties, the SFC published a Consultation Paper on a Draft for a composite Securities and Futures Bill. The draft Bill, when enacted, will repeal and replace eight of the ordinances currently administered by the SFC. It will enhance the investor protection functions of the SFC whilst promoting a fair, efficient, competitive and informed market, standardise the licensing regime applicable to dealers and advisers in the securities and futures industry, and generally update and modernise the territory's securities legislation in keeping with Hong Kong's status as an international financial centre.

6.2 The publication of the proposed draft Bill was followed by a period of consultation, originally set at three months but later extended to seven months. During that period, some 20 private briefings and public seminars were given by the Chairman and senior executives of the SFC and approximately 1,000 persons attended these events. At the same time, 50 written submissions were received from constituents of the financial industry; the SFC had agreed with the thrust of many of the representations made and has modified the draft Bill accordingly. In other cases, after giving careful consideration, the SFC either maintained its views, or, whilst sympathetic to the sentiments expressed, decided that they were outside the context of the Bill and should be placed in a "wish list" for further consideration and discussion with the industry at a future date. The SEHK also made extensive comments and observations. The SFC considered the exercise to be of such importance that on 6 December 1996 a further paper entitled the Main Proposed Revisions to the Draft Bill was presented to the market with a one month consultation period.

6.3 Legal Services Division staff are currently discussing with the Financial Services Branch with a view to pursuing the legislative procedure as soon as possible.

#### Securities (Disclosure of Interest) Ordinance

6.4 The Legal Services Division has been working with the other operational Divisions on the proposed amendments to this Ordinance. It is intended to consult the public when the amendments are formulated.

#### Personal Data (Privacy) Ordinance

6.5 The Personal Data (Privacy) Ordinance (PDPO) was enacted in 1995 with the purpose of protecting personal privacy and of facilitating access to personal data. It introduces six data protection principles in relation to the collection, quality, use, security and access of personal data and to the publication of the data user's policy on data

protection. The substantive provisions of the Ordinance came into effect on 20 December 1996.

6.6 The application of the Ordinance is of considerable significance to the SFC which obtains, uses and retains vast quantities of personal data in the performance of its functions as a financial regulator under the various ordinances which it administers. At the same time, the Ordinance provides exemptions by way of recognising other competing public interests, such as the detection and prevention of crime and the maintenance of the stability of the financial markets, and the SFC as a financial regulator is exempt from certain of the statutory requirements. The Division has worked closely with all other SFC divisions in reviewing their respective operational systems and documentation to ensure compliance with the Ordinance and in organising briefings, in cooperation with the Privacy Commissioner's Office, to assist operational staff to address the specific requirements imposed.

#### Amendments to Ordinances and Subsidiary Legislation

6.7 The Securities and Futures Commission Ordinance (SFCO) was amended to introduce approval requirements for changes in substantial shareholdings in a registered person that is a corporation. A new s26A sets out the restrictions and requirements applicable to persons acquiring substantial shareholdings in corporate registered persons. Similar amendments were also made to the Leveraged Foreign Exchange Trading Ordinance (LFETO).

6.8 In order to encourage trading in the financial product, the Securities and Futures Commission (Levy)(Futures Contracts) Order was amended to provide for a nil levy for transactions in the currency futures market of the Futures Exchange.

6.9 The SFC is empowered by the Securities Ordinance (SO) to prescribe limits on the number of stock options contracted on the SEHK that may be held by any person, and such limits are prescribed in the Schedule to the Securities (Exchange - Traded Stock Options) Rules. The Schedule was amended twice in the year under review to include 15 new option classes.

6.10 The Commodities Trading (Trading Limits and Position Limits) Rules were amended to correspond with parallel rule changes made by the Hong Kong Futures Exchange (HKFE) regarding limits on the amount of trading which can be transacted by any person under futures contracts.

6.11 The Securities and Futures Commission (Annual Returns) Rules and the Leveraged Foreign Exchange Trading (Annual Returns) Rules were amended to give the SFC the discretion to accept annual returns from registrants of a common corporate registrant on a common anniversary date.

### **Litigation and other non-criminal contentious proceedings**

#### **Mandarin Resources Corporation Limited (MRC)**

6.12 The Division has been responsible for the carriage of the petition against Mandarin Resources Corporation Ltd and its controlling shareholder which was filed by the SFC in the High Court on 25 June 1996, following consultation with the Financial Secretary. The petition seeks a number of remedies, including redress for the minority shareholders of MRC arising from the manner in which the affairs of MRC are alleged to have been conducted and/or the winding-up of the company.

6.13 The Division has also been involved in protracted litigation arising from the above-mentioned petition proceedings relating to MRC and its controlling shareholder. Particular instances include the withdrawal by MRC of its application for leave to apply for judicial review of the SFC's decision in relation to the company's proposal that its shares resume trading on the SEHK and the permanent stay of a libel action against present and former SFC personnel. The Division continues to be involved in a number of other related proceedings.

6.14 The Division also provided legal advice to the Intermediaries Supervision Department regarding Canwell Forex International Ltd (see 1.46 - 1.50), Wei Xin Securities Ltd (see 1.51 - 1.54), Cheung Cheong Woon (see 1.55 - 1.57) and C K Securities Company (see 1.58 - 1.60).

#### **Securities and Futures Appeals Panel**

6.15 In the course of the year, there have been ten appeals to the Securities and Futures Appeals Panel against the SFC's decisions to revoke or suspend the registrations of registered persons. These appeals have yet to be heard.

#### **Insider Dealing**

6.16 During the year, the Division gave legal advice on whether the SFC should refer six cases of suspected insider dealing to the Financial Secretary, with recommendations that the cases be referred in turn by him to the Insider Dealing Tribunal. For further details, see paragraphs 3.32 - 3.45.

### **Criminal cases and disciplinary actions**

6.17 In the year under review, there have been a large number of prosecutions involving short-selling, as well as unregistered dealing and breaches of the provisions of the Securities (Disclosure of Interests) Ordinance and the Protection of Investors Ordinance (PIO).

6.18 In June 1996, the SFC successfully prosecuted the first case of unregistered dealing under the LFETO.

6.19 In August 1996, the SFC brought a prosecution under the PIO in the first case which involved advertising on the Internet. The Defendant pleaded guilty at trial.

### **Other Advisory Services**

6.20 Following the application by Emperor International Exchange (Hong Kong) Company Limited, in September 1994, for a licence under the Leveraged Foreign Exchange Trading Ordinance to conduct business as a leveraged foreign exchange trader, the Division was involved in advising Licensing Division at all stages up to the granting of the licence on 29 January 1997.

6.21 The Division provided legal advice to the Supervision of Markets Division in connection with the SFC's Consultation Paper on Internal Control Guidelines. In addition, proposals were submitted to the Supervision of Markets Divisions with regard to the Unified Exchange Compensation Fund.

6.22 The Division also provided general advisory service upon a wide range of matters including the drafting of Letters of Mindedness and Letters of Decision affecting the fitness and propriety of registered persons in disciplinary inquiries and prospective registrants, restriction notices and the admissibility and sufficiency of evidence in criminal prosecutions.



## China related work

### H-Shares Arbitration Mechanism

6.23 The existing dispute resolution mechanism for H-shares is based upon the legal framework prevailing before the change of sovereignty which makes provisions for the enforcement of arbitral awards originating from China and Hong Kong. Arbitration of disputes relating to H-shares may be held at the China International Economic and Trade Arbitration Commission (CIETAC) or the Hong Kong International Arbitration Centre (HKIAC) at the choice of the parties to the dispute. After 1 July 1997, with the establishment of the Hong Kong Special Administrative Region under Chinese sovereignty, the New York Convention for the enforcement of arbitral awards will no longer be applicable as between China and Hong Kong.

6.24 The Division is working closely with government departments and agencies in China and Hong Kong in an effort to review the relevant legal provisions in the two jurisdictions to ensure that the H-share dispute resolution mechanism may continue to be fully implemented and available to investors.

6.25 The Division continues to maintain a close working relationship with the China Securities Regulatory Commission on issues of mutual interest.

6.26 The Division also continues to be active in conducting seminars and briefings on laws relating to securities and futures regulation for PRC regulators who are seconded to Hong Kong under the terms of the respective Memoranda of Regulatory Cooperation between Hong Kong and the PRC and other visiting professionals and academics. The Division also monitors the development of PRC legislation pertaining to securities, futures, financial and other matters related to its work and prepares summaries for internal use, which assist in enhancing understanding of the two different legal systems and regulatory concepts essential for the efficient monitoring of cross-border investment activities.

## Corporate Resources Division

### Functions

7.1 The primary objective of the Corporate Resources Division is to facilitate the efficient functioning of the SFC by the provision and maintenance of appropriate support services at reasonable cost. Major responsibilities include financial control, budgeting, human resources, training, administration, computer hardware and software management, system development, organisation and methods analysis, data management development and the provision of secretariat services to the Commission and its committees.

### Finance and Administration Department

#### Finance Section

7.2 The Finance Section is responsible for the day-to-day administration of the finances of the SFC.

7.3 SFC revenues are derived from three main sources: an annual recurrent grant from Government approximately equal to the net cost to Government of running the former Office of the Commissioner for Securities and Commodities Trading, a levy (current rate 0.013% of which the SFC receives 0.006%, and the SEHK 0.007%) on transactions recorded on The Stock Exchange of Hong Kong, and a levy (current rate \$1 per contract) on both buyer and seller on transactions recorded on the Hong Kong Futures Exchange, and fees and charges for functions performed for specific identifiable market participants or users. From income over the years, the SFC had accumulated reserves of approximately \$664.88 million as at 31 March 1997. The reserves are invested in accordance with guidelines approved by the Financial Secretary.

7.4 Following a review of the SFC's fees and charges which was undertaken with reference to the volume of work and anticipated level of expenses in the coming year, the scales of fees and charges which have not been revised since 1994/95, have been increased modestly to recover projected costs having regard to an assumed inflation rate of 7%. The revised scales under the Leveraged Foreign Exchange Trading Ordinance were effective from 1 April 1997. The revised fee scales under the Commodities Trading Ordinance and Securities Ordinance, and for the Corporate Finance and Investment Products Divisions, are scheduled to be effective from August 1997.

7.5 The 1997/98 Budget, approved by the Governor in March 1997, is based on a manpower plan of 276, an estimated operating expenditure of \$339 million and a planned operating deficit of about \$72 million. Despite the projected deficit, for the fifth time in as many years, the SFC decided to request Government not to apply to the

Legislative Council for an appropriation from general revenue for 1997/98. The SFC noted, however, that a deficit would not have been projected had a request for an appropriation been made in accordance with the funding principles agreed by the Government and the Legislative Council when the SFC was established.

7.6 In addition to its own funds, four compensation and deposit funds are under the management of the SFC. They are the Unified Exchange Compensation Fund, Commodity Exchange Compensation Fund, Securities Dealers' Deposit Fund and Commodities Dealers' Deposit Fund. These funds totalled approximately \$560.1 million as at 31 March 1997 (See paragraphs 4.22 - 4.25 and sections 10 and 11 : Compensation Funds Financial Statements ) The Finance Section is responsible for maintaining the books and records for the funds and assisting in the management of their investment in accordance with the principles governing the investment of the SFC's own reserves.

#### Administration Section

7.7 The Administration Section is responsible for property and security management, and for office services, supplies and facilities management generally. During the year, a lease renegotiation was conducted successfully for existing office premises at Edinburgh Tower and an office renovation project was undertaken.

### Human Resources Department

#### Function

7.8 The primary function of the Human Resources Department is the maintenance of an efficient, productive and stable workforce throughout the SFC. In so doing, it aims to ensure a multi-jurisdictional and multi-disciplinary skills mix among staff and adopts a private sector ethos in managing and motivating staff with remuneration based strictly on performance.

#### Staffing

7.9 During the year 1996/97, the Commission experienced an increase in turnover, especially in the case of professional staff. Staff turnover for the 12 months ended 31 March 1997 was 17.59% for professional staff (cf 95/96: 10.12%) and 11.74% for general grade staff (cf 95/96: 10.26%), while the overall turnover was 14.86% (cf 95/96: 10.19%).

#### Training & Management Development

7.10 To promote the professionalism of SFC staff and to improve their effectiveness through training and development, training courses based on a Comprehensive



Training Programme, which include a core programme of management and professional skills training and customised technical programmes for staff with particular needs, were arranged for staff during the year.

### Competency Development Project

7.11 Pursuant to the SFC Corporate Plan, a Competency Development Project to specify the core competencies for different levels of staff was conducted during the year. The results form the basis of an integrated approach to different aspects of human resources management, particularly for the development of a more focused training and career development plan. The Project will be completed by mid-1997. In the meantime, views and comments collected during the Project have been drawn on to improve operational effectiveness and efficiency.

### China Training

7.12 In further preparation for the 1997 transition, a series of Chinese Writing Skills courses were arranged in which 40 professional staff participated. Ongoing training in Putunghua was also arranged with 25 classes being held during the year for staff at various levels. Due to the increasing volume of SFC correspondence with China, two training programmes on Simplified Chinese Characters were implemented.

7.13 In order to acquire a better understanding of China's political system and government machinery, and to build contacts with our Mainland counterparts, the SFC, in association with a number of public bodies (the Stock Exchange of Hong Kong Ltd, the Hong Kong Futures Exchange Ltd, the Hong Kong Securities Clearing Company, the Hospital Authority, the Hong Kong Tourist Association and the Hong Kong Trade Development Council), developed a Hong Kong Public Bodies Executive Development Programme (PBEDP) in Beijing. During the year, 18 SFC professional staff participated in three two-week PBEDPs conducted by the National School of Administration (NSA) in Beijing.

7.14 After each of the PBEDPs, post-course delegation visits of about one week were arranged to various government authorities and financial institutions in Beijing and Shanghai.

7.15 In November 1996, a NSA delegation led by the School's Vice-President, Mr Tang Tiehan, visited Hong Kong. Three professors of the delegation team conducted two seminars on topical issues concerning China for about 250 executives of the public bodies listed above.

7.16 In addition to the PBEDP, the SFC organised four four-day training courses in Shenzhen for middle ranking and junior executives. The purpose of the courses was to provide the 80 participants with a basic understanding of the

framework of government in China. Apart from the above, one Executive Director attended the Hong Kong Government Tsing Hua Programme, while four Directors attended the Hong Kong & Shanghai Bank Tsing Hua Programme.

### Training for PRC Regulators

7.17 The 5th Secondment Programme for PRC Securities Regulators was jointly organised by the SFC and SEHK during the year. The Programme, sponsored by the Hong Kong Securities Training Sponsorship Foundation Ltd, was attended by a total of 16 officials from the China Securities Regulatory Commission, the Shanghai Securities Administrative Office, the Shanghai and Shenzhen Stock Exchanges, the Hong Kong & Macau Affairs Office, the Party School of the CCP Central Committee and the Securities & Exchange Commission in Taipei.

7.18 The SFC and the HKFE also jointly organised two one-week training programmes for 23 senior executives from 15 PRC futures exchanges.

### Overseas Training and Secondment

7.19 To widen the SFC staff's exposure to securities and futures regulation in other developed markets, one executive was seconded to the National Association of Securities Dealers in Washington for two months. Nine others attended various training programmes (varying from one to three weeks) organised by overseas regulatory bodies including the SEC and CFTC in the USA, the Australian Securities Commission, and IMRO in the United Kingdom.

### Internship Programme

7.20 As part of the SFC's long term programme aimed at developing the pool of financial professionals in the Hong Kong market, an SFC Internship Programme was successfully introduced during the year. The Programme aims to equip high-calibre graduates with industry and regulatory knowledge. It will also enable the SFC to identify graduates with good potential for possible further employment at the SFC. Six fresh graduates from the local universities were recruited to the Programme in July 1996. A new group of interns will be recruited in July 1997.

### Employee Relations

7.21 To foster communication and promote professional exchange, sharing sessions were held from time to time by senior executives of the SFC to brief staff on topical issues ranging from the strategic concerns of the SFC, to market integrity, listing policy, case studies and staff policy. A Human Resources Newsletter was issued periodically and talks were organised on health and recreational activities.



## Secretariat

7.22 The Secretariat, which is mainly concerned with SFC corporate governance matters, services Commission Meetings and Committees of the Commission. A number of matters are statutorily reserved to the Commission, as opposed to the Executive. In addition, the Commission is responsible for determining strategic policies and objectives and monitoring achievement of those objectives and compliance with policies. Fourteen Commission Meetings were held during the year.

7.23 The five independent Non-Executive Directors, who have both the varied backgrounds and extensive experience necessary to ensure objectivity and to balance the interests of market practitioners, the investing public, and the community at large, play an important role in the checks and balances applicable to the internal management of the SFC. For example, they hold the Chairmanships, Deputy Chairmanships and casting votes on the Audit Committee (to which the external auditors have unrestricted access), the Budget Committee (which is responsible for the examination of the draft annual Budget before its consideration by the Commission), and the Remuneration Committee (which considers staff salary ranges, the remuneration of Directors being set by the Governor).

7.24 During the year, complementary to the normal external audit, external auditors completed specific reviews of the Commission's systems of internal control in connection with fee collection procedures, human resources systems including payroll and benefit procedures, and investment and safe keeping procedures, and in each case reported to the Audit Committee that the procedures were generally satisfactory.

7.25 The SFC Advisory Committee, which advises the Commission on all policy matters, met four times during the year. Topics discussed by the Advisory Committee include the Rationalisation of Securities and Futures Legislation, an Investor Survey, Short Selling, the Strategic Plan of the Hong Kong Futures Exchange, Proprietary Trading Systems, Leveraged Spot Gold Contracts, the Leveraged Foreign Exchange Trading Regulatory System, Inter-market Coordination, Listed Company Communications, and Management Supervision and Internal Control Guidelines for Registered Persons/Licensed Traders.

7.26 The Management Committee, which comprises senior executives and exercises administrative, financial and housekeeping management powers delegated to it by the Commission, held 13 meetings during the year.

## Information Resources Department

7.27 The Information Resources Department is responsible for the administration of the SFC's technology infrastructure and Corporate information base. It also provides all aspects of technology-related support to the SFC.

7.28 The year saw the beginning of Stage One of the five-year Information Systems Strategic Plan. The theme of Stage One was to upgrade the SFC's basic technology infrastructure to meet the increasing demand in processing capacity, to improve internal and external communications and to rebuild the Licensing Application Processing System. Five major projects — the SFC Internet Web site, a Network Fax System, a Mainframe Computer Upgrade, an Automatic Voice Response System, and an Internet Email System — were implemented during the year. Development work on another major project, the Licensing Application Processing System Rebuild, is in progress.

7.29 The Mainframe Computer (IBM AS/400 System) was upgraded in July 96 to meet the increasing demand for computing capability. The machine upgrade also positioned the SFC to a more up-to-date technological architecture.

7.30 An Automatic Voice Response System (the SFC Infoline) was launched in November 1996. The public can call the Infoline at 2840-9393, 24 hours a day, to obtain information about the SFC. The Infoline also includes a 'fax-on-demand' facility, allowing the public to obtain 'fact sheets' via fax.

7.31 The In-house Email System was enhanced to enable global communications by integration with the Internet in January 1997. SFC PC users can now communicate by electronic mail from their desktops with colleagues via the in-house network and with other organisations and individuals on the Internet.

7.32 The Licensing Rebuild project aims to improve the user-friendliness and system performance of the existing Licensing Application Processing System by redesigning the user interface and enhancing management information reporting under a graphical based client/server environment. The project began in March 1997 and is due to be completed in 1998.



## Corporate Communications Division

### Functions

8.1 The Corporate Communications Division consists of the Public Affairs Department and the Translation Department. The Division's primary functions are to develop policy and procedures in matters relating to public affairs, publications and information and to assist the SFC in maintaining effective relations with the media, stakeholders, and overseas organisations.

8.2 In performing these functions, the Division:

- acts as spokesperson for the SFC and channel of communication between the SFC, the public and the media;
- advises the SFC on public and media relations and responds to media enquiries;
- maintains liaison with SFC stakeholders, including the Legislative Council, Government, the Exchanges, listed companies, intermediaries, and industry organisations;
- develops and organises seminar programs for registered intermediaries and other market practitioners;
- evaluates conferences and other speaking platforms for SFC participation to promote Hong Kong as a financial centre and to publicise the work of the SFC;
- produces publications for market practitioners and the investing public; provides translation services to the SFC; and
- manages the SFC's Internet Web site, located at <http://www.hksfc.org.hk>.

8.3 During the year, the Public Affairs Department:

- organised a high-level conference in Beijing in May 1996 entitled "Hong Kong: Towards a New Financial Era", in cooperation with the Stock Exchange of Hong Kong, Hong Kong Monetary Authority and Hong Kong Futures Exchange.
- worked with the Investor Education unit to promote the SFC's Investor Education programme, including a new series of public service television commercials on the theme "Invest Wisely".
- developed and launched an SFC Web site on the Internet, in cooperation with the Chinese University of Hong Kong and the SFC's Information Resources Department.
- issued 173 press releases, 168 securities disclosure announcements, and 6 consultation papers; conducted 75 individual media interviews and 8 press conferences and media briefings.

# **SFC Financial Statements**

*For the year ended 31st March 1997*

## **Auditors' Report**

### **To The Securities and Futures Commission ("The Commission")**

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

We have audited the financial statements on pages 61 to 68 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

#### **Respective responsibilities of directors and auditors**

The Securities and Futures Commission Ordinance ("the Ordinance") requires the Commission to prepare financial statements and the directors of the Commission do so on the basis that these financial statements should give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgments and estimates are made which are prudent and reasonable and that reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

#### **Basis of opinion**

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Commission in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Commission's circumstances, have been consistently applied and are adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatements. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

#### **Opinion**

In our opinion the financial statements give a true and fair view, in all material aspects, of the state of Commission's financial affairs as at 31st March 1997 and of its surplus and cash flows for the year then ended and have been properly prepared in accordance with accounting principles generally accepted in Hong Kong.

KPMG Peat Marwick  
Certified Public Accountants  
Hong Kong  
19th May 1997



**Securities and Futures Commission**  
**Income and Expenditure Account**

*For the year ended 31st March 1997*

<i>Expressed in HK\$'000</i>	Note	1997	1996
<b>INCOME</b>			
Levies	2&3	\$ 217,551	\$ 134,334
Fees and charges	2&3	94,390	78,120
Investment income	3	40,228	36,953
Others		13,343	7,054
		<u>\$ 365,512</u>	<u>\$ 256,461</u>
<b>EXPENDITURE</b>			
Personnel	5	\$ 204,380	\$ 177,663
Premises			
- rental charges under operating leases	3	31,417	25,998
- other		5,899	5,039
Other expenses	6	55,936	32,953
		<u>\$ 297,632</u>	<u>\$ 241,653</u>
Depreciation	3	6,768	4,211
		<u>\$ 304,400</u>	<u>\$ 245,864</u>
<b>SURPLUS OF INCOME OVER EXPENDITURE FOR THE YEAR</b>			
		\$ 61,112	\$ 10,597
<b>BALANCE BROUGHT FORWARD</b>			
		549,064	538,467
<b>BALANCE CARRIED FORWARD</b>			
		<u>\$ 610,176</u>	<u>\$ 549,064</u>

The notes on pages 64 to 68 form part of these financial statements.

# **Securities and Futures Commission** **Balance Sheet**

*As at 31st March 1997*

<i>Expressed in HK\$'000</i>	Note	1997	1996
FIXED ASSETS	7	\$ 9,009	\$ 7,521
INVESTMENTS	8	\$ 394,690	\$ 345,618
CURRENT ASSETS			
Investments	8	\$ 245,005	\$ 212,591
Bank deposits		36,541	42,549
Debtors, deposits and prepayments	9	34,591	22,215
Cash at bank and in hand		706	445
		<u>\$ 316,843</u>	<u>\$ 277,800</u>
CURRENT LIABILITIES			
Deferred income	3	\$ 23,530	\$ 22,585
Creditors and accrued charges		43,996	16,450
		<u>\$ 67,526</u>	<u>\$ 39,035</u>
NET CURRENT ASSETS		<u>\$ 249,317</u>	<u>\$ 238,765</u>
NET ASSETS		<u>\$ 653,016</u>	<u>\$ 591,904</u>
Representing:			
INITIAL FUNDING BY GOVERNMENT	10	\$ 42,840	\$ 42,840
INCOME AND EXPENDITURE ACCOUNT		610,176	549,064
		<u>\$ 653,016</u>	<u>\$ 591,904</u>

Approved by the Commission on  
19th May 1997 and signed on its behalf by

Anthony Neoh  
Chairman

Roderick E D Chalmers  
Non-executive Director

The notes on pages 64 to 68 form part of these financial statements.



**Securities and Futures Commission**  
**Cash Flow Statement**

*For the year ended 31st March 1997*

<i>Expressed in HK\$'000</i>	Note	1997	1996
Net cash inflow / (outflow) from operating activities	a	\$ 45,369	\$ (14,783)
Returns on investments and servicing of finance			
Interest received		\$ 38,959	\$ 39,313
Investing activities			
Payments to acquire dated securities		\$ (294,271)	\$ (123,654)
Receipts from redemption of dated securities		212,446	98,000
Payments to acquire fixed assets		(8,256)	(5,471)
Receipts from sale of fixed assets		6	66
Net cash outflow from investing activities		\$ (90,075)	\$ (31,059)
Decrease in cash and cash equivalents		\$ (5,747)	\$ (6,529)
Cash and cash equivalents at beginning of the year		42,994	49,523
Cash and cash equivalents at end of the year	b	\$ 37,247	\$ 42,994

a Reconciliation of surplus of income over expenditure to net cash inflow / (outflow) from operating activities:

	1997	1996
Surplus of income over expenditure for the year	\$ 61,112	\$ 10,597
Interest income	(40,567)	(39,015)
Premium on investments	622	2,127
Discount on investments	(283)	(65)
Depreciation charges	6,768	4,211
(Profit) / Loss on disposal of fixed assets	(6)	16
Increase in debtors, deposits and prepayments	(10,768)	(4,615)
Increase in creditors and accrued charges	27,546	6,684
Increase in deferred income	945	5,277
Net cash inflow / (outflow) from operating activities	\$ 45,369	\$ (14,783)

b Analysis of the balance of cash and cash equivalents as shown in the balance sheet:

Bank deposits	\$ 36,541	\$ 42,549
Cash at bank and in hand	706	445
	\$ 37,247	\$ 42,994

## Securities and Futures Commission Notes to the Financial Statements

*Expressed in HK\$'000*

### 1. Status of the Securities and Futures Commission ("the Commission")

The Commission was established under and is governed by the Securities and Futures Commission Ordinance ("the Ordinance").

### 2. Income

Details of the funding of the Commission are set out in Sections 52 to 54 of the Ordinance. In particular,

- a The Commission receives a share of the levy collected by the Stock Exchange of Hong Kong Limited and the levy collected by the Hong Kong Futures Exchange Limited on transactions recorded on the Exchanges at rates specified by the Governor in Council.
- b In each financial year, the Commission shall be paid out of general revenue such moneys as shall be appropriated by the Legislative Council. At the request of the Commission, no appropriation has been made since the financial year ended 31st March 1994.
- c Subsidiary legislation provides for the payment to the Commission of fees or other charges in relation to the functions and services performed by the Commission.

### 3. Significant accounting policies

#### a Depreciation

Depreciation is calculated to write off the cost of fixed assets over their anticipated useful lives on a straight line basis. The anticipated useful lives of personal computers and software (included under computers and application systems in previous years) have been changed from 4 years to 3 years with effect from 1st April 1996 to reflect the current development trend of personal computers. As a result, the depreciation charges for the year were increased by approximately \$1,080,000. The principal depreciation rates used for the year are as follows:

Leasehold improvements	- over the shorter of the period of the respective leases and three years
Furniture and fixtures	- 33 1/3% per annum
Office equipment	- 20% per annum
Personal computers and software	- 33 1/3% per annum
Mainframe computers and application systems	- 25% per annum
Motor vehicles	- 25% per annum

#### b Investments

Investments, representing dated securities, are stated at cost adjusted for the amortisation of premiums and accretion of discounts on purchase over the periods to redemption.

Provisions are made where there has been a permanent diminution in value.



**Securities and Futures Commission**  
**Notes to the Financial Statements**

*Expressed in HK\$'000*

c Recognition of income

(i) Levies

Levies from the two Exchanges are credited to the income and expenditure account on an accruals basis.

(ii) Fees & charges

Annual fees from registered persons and in respect of authorised investment arrangements are credited to the income and expenditure account on a straight line basis over the periods to which they relate. Other fees and charges are credited to the income and expenditure account when receivable.

(iii) Investment income

Investment income is credited to the income and expenditure account on an accruals basis. It comprises interest earned on bank deposits and dated securities and the premium or discount on purchase of dated securities amortised or accreted on a straight line basis over periods to redemption.

d Operating leases

Rental payable under operating leases is accounted for on a straight line basis over the period of the leases.

4. Taxation

In accordance with section 3(3) of the Ordinance, the receipts of the Commission are not subject to Hong Kong taxation under the Inland Revenue Ordinance.

5. Personnel expenses

a Personnel expenses comprise:

	1997	1996
Directors' fees	\$ 1,170	\$ 1,080
Directors' salaries, allowances and gratuities	22,017	20,389
Directors' bonuses	718	481
Staff salaries, allowances and gratuities	171,969	147,626
Retirement benefits	2,741	2,523
Medical and life insurance	4,847	4,434
Overtime pay	918	1,130
	<u>\$ 204,380</u>	<u>\$ 177,663</u>

**Securities and Futures Commission**  
**Notes to the Financial Statements**

*Expressed in HK\$'000*

b The number of Directors whose emoluments fell within the following bands were:

	1997	1996
	No. of directors	No. of directors
Emolument Ranges		
\$0 to \$1,000,000	6	7
\$3,000,001 to \$3,500,000	1	1
\$3,500,001 to \$4,000,000	-	1
\$4,000,001 to \$4,500,000	2	2
\$4,500,001 to \$5,000,000	1	1
\$5,500,001 to \$6,000,000	1	-
	<u>11</u>	<u>12</u>

c The five highest paid individuals during the year were all directors of the Commission, the aggregate remuneration of which has been included in 5(a) and (b) above.

d Retirement benefits are provided to certain categories of staff through a defined contribution scheme. The Commission makes monthly contributions equal to 12% of the basic salary of such staff. Forfeited contributions in respect of staff who leave the Commission prior to qualifying for 100% disbursement of the contributions are used to re-invest into the total pool of contributions and shared by the existing members in the scheme at the end of the scheme year. The amount re-invested during the year was \$492,000 (1996: \$244,000).

**6. Other expenses**

Other expenses comprise:

	1997	1996
Training and development	\$ 8,332	\$ 9,011
Legal and professional services	33,603	11,784
Information and systems services	9,249	7,600
Auditors' remuneration	131	121
General office and insurance	4,621	4,437
	<u>\$ 55,936</u>	<u>\$ 32,953</u>



**Securities and Futures Commission**  
**Notes to the Financial Statements**

*Expressed in HK\$'000*

**7. Fixed Assets**

	Furniture, fixtures and leasehold improvements	Office equipment	Mainframe Computers and application systems	Personal computers and software	Motor vehicles	Total
<b>Cost</b>						
At 1st April 1996	\$ 11,857	\$ 4,052	\$ 20,269	\$ 11,576	\$ 845	\$ 48,599
Additions during the year	1,567	1,037	3,155	2,497	-	8,256
Disposals during the year	(155)	(62)	(6,539)	(612)	-	(7,368)
At 31st March 1997	<u>\$ 13,269</u>	<u>\$ 5,027</u>	<u>\$ 16,885</u>	<u>\$ 13,461</u>	<u>\$ 845</u>	<u>\$ 49,487</u>
<b>Depreciation</b>						
At 1st April 1996	\$ 11,073	\$ 2,119	\$ 19,194	\$ 8,164	\$ 528	\$ 41,078
Charge for the year	1,218	770	1,456	3,113	211	6,768
Written back on disposals	(155)	(62)	(6,539)	(612)	-	(7,368)
At 31st March 1997	<u>\$ 12,136</u>	<u>\$ 2,827</u>	<u>\$ 14,111</u>	<u>\$ 10,665</u>	<u>\$ 739</u>	<u>\$ 40,478</u>
<b>Net book value</b>						
At 31st March 1997	<u>\$ 1,133</u>	<u>\$ 2,200</u>	<u>\$ 2,774</u>	<u>\$ 2,796</u>	<u>\$ 106</u>	<u>\$ 9,009</u>
<b>Net book value</b>						
At 31st March 1996	<u>\$ 784</u>	<u>\$ 1,933</u>	<u>\$ 1,075</u>	<u>\$ 3,412</u>	<u>\$ 317</u>	<u>\$ 7,521</u>

**8. Investments**

	1997	1996
<b>Dated securities</b>		
Maturing after one year		
- unlisted	\$ 315,436	\$ 341,163
- listed in Hong Kong	64,218	4,455
- listed outside Hong Kong	15,036	-
	<u>\$ 394,690</u>	<u>\$ 345,618</u>
Maturing within one year		
- unlisted	\$ 245,005	\$ 191,604
- listed in Hong Kong	-	11,988
- listed outside Hong Kong	-	8,999
	<u>\$ 245,005</u>	<u>\$ 212,591</u>
	<u>\$ 639,695</u>	<u>\$ 558,209</u>
<b>Market value at 31st March</b>		
- unlisted	\$ 559,891	\$ 534,338
- listed in Hong Kong	63,682	16,396
- listed outside Hong Kong	15,090	8,991
	<u>\$ 638,663</u>	<u>\$ 559,725</u>

## Securities and Futures Commission

### Notes to the Financial Statements

*Expressed in HK\$'000*

#### 9. Loans to directors and executives

Included in debtors is an interest-free loan to an executive for initial settling-in purposes amounting to \$202,000 (1996: \$62,000). The loan is repayable in equal installments over eight months.

The maximum balance of outstanding loans to executives during the year was \$303,000 (1996: \$443,000).

#### 10. Initial funding by Government

This represents funds provided by Government to pay for the Commission's non-recurrent and capital expenditure when it was established. These funds are not repayable to Government.

#### 11. Capital commitments

Capital commitments outstanding at 31st March 1997 not provided for in the financial statements were as follows:

	1997	1996
Contracted for	\$ 3,575	\$ 312
Authorised but not contracted for	\$ 20,745	\$ 29,511

#### 12. Operating lease commitments

At 31st March 1997 the Commission had commitments under an operating lease in respect of its premises to make payments in the next year as follows:

	1997	1996
Lease expiring over 5 years	\$ 35,669	\$ 32,997

#### 13. Funds held in escrow

At 31st March 1997 the Commission held \$124,956,000 in escrow (1996: \$119,092,000). These funds are not included in the financial statements as they are not beneficially owned by the Commission.



# **Unified Exchange Compensation Fund Financial Statements**

## **Unified Exchange Compensation Fund ("The Fund") Report of the Securities Compensation Fund Committee ("the Committee")**

The members of the Committee present their annual report and the audited financial statements for the year ended 31st March 1997.

### **1. Establishment of the Fund**

The Fund was established for the purposes set out in Part X of the Securities Ordinance (Chapter 333).

### **2. Financial results**

The financial results are set out in the financial statements presented on pages 71 to 75.

### **3. Members of the Committee**

The members of the Committee during the year and up to the date of this report were : -

Mr. David John White

Mr. Michael Wu

Mr. Roderick Chalmers

Mr. Paul Chow (resigned on 1 February 1997)

Mr. Alan Howard Smith (resigned on 20 January 1997)

Mr. Alec Tsui (appointed on 1 February 1997)

Mr. Seto Gin Chung, John (appointed on 20 January 1997)

### **4. Interests in contracts**

No contracts of significance to which the Fund was a party and in which a Committee Member had a material interest, whether directly or indirectly, subsisted at the balance sheet date or at any time during the year.

### **5. Auditors**

The retiring auditors, Messrs.KPMG Peat Marwick, being eligible, offer themselves for re-appointment.

On behalf of the Committee

David J White  
Chairman  
15th May 1997

## **AUDITORS' REPORT TO THE SECURITIES & FUTURES COMMISSION ("the Commission")**

We have audited the financial statements of the Unified Exchange Compensation Fund ("the Fund") established under Section 99 of the Securities Ordinance on pages 71 to 75 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

### **Respective responsibilities of the Commission and auditors**

The Securities Ordinance requires the Commission to keep proper accounts of the Fund and to prepare an income and expenditure account and a balance sheet ("the financial statements") of the Fund in respect of each financial year. The directors of the Commission do so on the basis that these financial statements should give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgements and accounting estimates are made which are prudent and reasonable and that reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion to you.

### **Basis of opinion**

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Commission in the preparation of the financial statements and of whether the accounting policies are appropriate to the Fund's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

### **Opinion**

In our opinion the financial statements give a true and fair view of the state of affairs of the Fund as at 31st March 1997 and of its surplus for the year then ended and have been properly prepared in accordance with accounting principles generally accepted in Hong Kong.

KPMG Peat Marwick  
Certified Public Accountants  
Hong Kong.

15th May 1997



**Unified Exchange Compensation Fund  
Income and Expenditure Account**

*For the Year Ended 31st March 1997*

<i>Expressed in Hong Kong Dollars</i>	Note	1997	1996
<b>Income</b>			
Interest and investment income	3	\$ 29,189,684	\$ 27,251,786
Premium amortized/discount accreted	3	298,258	517,596
Other income	3	-	35,211
		<u>\$ 29,487,942</u>	<u>\$ 27,804,593</u>
<b>Expenditure</b>			
Auditors' remuneration		\$ 33,000	\$ 34,000
Bank charges		169,704	127,268
Legal and professional fees		630,979	223,062
Sundry expenses		600	630
		<u>\$ 834,283</u>	<u>\$ 384,960</u>
Surplus on investment before appropriations		\$ 28,653,659	\$ 27,419,633
Balance brought forward		-	-
Balance available for appropriations		<u>\$ 28,653,659</u>	<u>\$ 27,419,633</u>
<b>Appropriations</b>			
Payment to The Stock Exchange of Hong Kong Limited of interest declared at 6.1468% p.a. (1996 - 6.6514% p.a.) pursuant to S105(2)(a) of the Securities Ordinance, Chapter 333		2,055,568	2,082,977
Transfer to Compensation Fund Account	8	26,598,091	25,336,656
Balance carried forward		<u>\$ -</u>	<u>\$ -</u>

The notes on pages 73 to 75 form an integral part of the financial statements

**Unified Exchange Compensation Fund  
Notes to the Financial Statements**

*For the year ended 31st March 1997*

*Expressed in Hong Kong Dollars*

4 Investments	1997	1996
Dated securities		
maturing after one year		
listed in Hong Kong	\$ 35,088,375	\$ -
listed outside Hong Kong	10,024,129	-
unlisted	182,222,140	257,174,733
	<u>\$ 227,334,644</u>	<u>\$ 257,174,733</u>
maturing within one year		
listed in Hong Kong	\$ -	\$ 19,787,586
unlisted	222,006,359	124,266,026
	<u>222,006,359</u>	<u>144,053,612</u>
	<u>\$ 449,341,003</u>	<u>\$ 401,228,345</u>
market value at 31st March		
listed in Hong Kong	\$ 34,696,500	\$ 19,880,000
listed outside Hong Kong	10,060,000	-
unlisted	403,828,600	383,128,000
	<u>\$448,585,100</u>	<u>\$403,008,000</u>

**5 Contributions from the SEHK**

In accordance with Sections 104 and 106 of the SO, the SEHK is required to deposit with the SFC a sum of \$50,000 in respect of each membership of the SEHK not later than one month after membership is taken up. In the absence of claims or other provisions as set out in Section 106 of the SO, the SFC is required to refund to the SEHK from the Fund such deposit within six months after membership ceases.

The SEHK has advised the SFC of twenty nine (29) memberships having been taken up during the six (6) months to 31st March 1997. However, the SEHK had not at 31st March 1997 deposited with the SFC a sum of \$50,000 in respect of each such membership. The liability of the SEHK to the Fund in this respect has not been taken up in these accounts. Any monetary liability of the SEHK that may have existed due to memberships taken up prior to six (6) months before 31st March 1997 would be extinguished by the requirement of the Fund to refund to the SEHK deposits of ceased memberships in accordance with Section 106(1) of the SO, as the number of new members equalled the number of members leaving the SEHK during the period.

During the year \$50,000 was refunded to the SEHK in respect of an ex-member of the SEHK who was expelled from membership of the SEHK in 1988 and whose share was forfeited in 1992 under the SEHK's capital reduction scheme. As the SEHK had fully replenished the Fund in respect of the balance of the payments out from the Fund in respect of this ex-member after the SFC's recoveries action had completed, the SFC refunded \$50,000 to the SEHK. Hence the total contribution from the SEHK was reduced to \$46,450,000 as of 31st March 1997.



**Unified Exchange Compensation Fund**  
**Notes to the Financial Statements**

*For the year ended 31st March 1997*

*Expressed in Hong Kong Dollars*

6. Recovery under subrogation

	1997	1996
Balance brought forward	\$ 451,285	\$ 59,639
Add: Amount recovered during the year	8,180	391,646
Balance carried forward	<u>\$ 459,465</u>	<u>\$ 451,285</u>

Under Section 118 of the SO, the SFC is entitled to receive in place of the claimant, all claims, remedies and distribution of surplus assets on liquidation of the dealer in relation to the loss sustained by the claimant, to the extent of the payment made by the SFC out of the Fund.

7. Excess transaction levy from the SEHK

In accordance with an agreement reached in 1991 between the SFC and the SEHK, the SEHK is to remit any excess of its transaction levy revenue over one third of its budgeted expenses and any income from the transaction levy when its reserves exceed the sum of its immediately preceding two years' recurrent expenditure.

According to the 1994/95 budget of the SEHK approved by the Financial Secretary in August 1994, excess transaction levy will be diverted to the reserves of the SEHK instead of the Fund when the Fund reaches \$400 million.

Accordingly, no excess transaction levy had been transferred to the Fund during the year.

8. Transfer from income and expenditure account

	1997	1996
Balance brought forward	\$ 52,473,003	\$ 27,136,347
Add: Transfer of surplus for the year	26,598,091	25,336,656
Balance carried forward	<u>\$ 79,071,094</u>	<u>\$ 52,473,003</u>

9. Contingent liabilities

Up to the date of this report, claims against seven members had not been determined by the SEHK. No provision for compensation has been made in respect of these claims. According to the SEHK the maximum liability of the Fund to these claims is \$56 million.

**Commodity Exchange Compensation Fund  
Income and Expenditure Account**

*For the year ended 31st March 1997*

<i>Expressed in Hong Kong Dollars</i>	Note	1997	1996
<b>Income</b>			
Interest and investment income	3	\$ 3,139,542	\$ 2,568,983
Premium amortized / discount accreted	3	26,399	32,513
		<u>\$ 3,165,941</u>	<u>\$ 2,601,496</u>
<b>Expenditure</b>			
Auditors' remuneration		\$ 33,000	\$ 34,000
Bank charges		31,739	14,483
Sundry expenses		500	600
Legal and professional fees		49,322	18,849
		<u>\$ 114,561</u>	<u>\$ 67,932</u>
Surplus on investment before appropriations		\$ 3,051,380	\$ 2,533,564
Balance brought forward		-	-
<b>Appropriations</b>			
Transfer to Compensation Fund Account pursuant to S83(2)(a) of the Commodities Trading Ordinance (Chapter 250)	6	3,051,380	2,533,564
Balance carried forward		<u>\$ -</u>	<u>\$ -</u>

The notes on pages 80 to 82 form an integral part of the financial statements



**Commodity Exchange Compensation Fund  
Balance Sheet**

*As at 31st March 1997*

<i>Expressed in Hong Kong Dollars</i>	Note	1997	1996
Investments	3&4	\$ 32,029,228	\$ 23,997,567
Current assets			
Investments	3&4	\$ 18,000,521	\$ 9,971,333
Interest receivable		456,518	316,379
Levy receivable		563,562	571,460
Bank fixed and call deposits		3,970,412	10,140,092
Cash at bank		57,097	15,746
		<u>\$ 23,048,110</u>	<u>\$ 21,015,010</u>
Liabilities			
Accounts payable and accrued charges		\$ 241,838	\$ 245,757
Provision for compensation	7	2,541,175	2,391,861
		<u>\$ 2,783,013</u>	<u>\$ 2,637,618</u>
Net current assets		<u>\$ 20,265,097</u>	<u>\$ 18,377,392</u>
Net assets		<u>\$ 52,294,325</u>	<u>\$ 42,374,959</u>
Representing:			
Compensation Fund			
Contributions to the Fund received on			
and after 23rd August 1985	5	\$ 20,600,000	\$ 21,500,000
Contract levy	3	29,827,902	23,826,075
Transfer from income and expenditure account	6	13,371,819	10,320,439
		<u>\$ 63,799,721</u>	<u>\$ 55,646,514</u>
Deduct: Compensation paid		(20,463,745)	(20,463,745)
Provision for compensation	7	(2,541,175)	(2,391,861)
Add: Recovery under subrogation	3&8	11,499,524	9,584,051
		<u>\$ 52,294,325</u>	<u>\$ 42,374,959</u>

Approved by the Futures Compensation Fund Committee on behalf of the Securities and Futures Commission on 14th May 1997 and signed on its behalf by

David J White  
Chairman

Roderick E D Chalmers  
Committee Member

Ivers W Riley  
Committee Member

The notes on pages 80 to 82 form an integral part of the financial statements

**Commodity Exchange Compensation Fund**  
**Notes to the Financial Statements**

*For the year ended 31st March 1997*

*Expressed in Hong Kong Dollars*

7. Provision for compensation

	1997	1996
Balance brought forward	\$ 2,391,861	\$ 2,237,662
Add: Interest on outstanding claims	149,314	154,199
Balance carried forward	<u>\$ 2,541,175</u>	<u>\$ 2,391,861</u>

8. Recovery from subrogation

	1997	1996
Balance brought forward	\$ 9,584,051	\$ 8,864,717
Add: Amount recovered during the year	1,915,473	719,334
Balance carried forward	<u>\$ 11,499,524</u>	<u>\$ 9,584,051</u>

Under Section 95 of the CTO, the SFC is entitled to receive in place of the claimant, all claims, remedies and distribution of surplus assets on liquidation of the dealer in relation to the loss sustained by the claimant, to the extent of the payment made by the SFC out of the Fund.



# Performance Pledges

## Introduction

The SFC's most important function is the protection of investors. While seeking to protect investors, the SFC serves them and market practitioners in a number of ways. As part of the Governor's Serving the Community Scheme, the SFC has made pledges to the public regarding the performance of its responsibilities. Outlined below are standards of service the public can expect from the SFC as well as steps they can take if they wish to seek explanation or make comments on the services they receive.

The public should be aware that the SFC is constrained by its enabling legislation with regard to the information that it can disclose to the public (including complainants), especially with regard to investigations and enforcement matters.

## Investor Enquiries and Complaints

The Investor Education Unit has pledged to give a preliminary response to any enquiry or complaint made by telephone within two working days of the call being received. Written complaints are usually of a more complicated nature and therefore may require more detailed consideration. The Unit undertakes to provide a preliminary response to any written enquiry or complaint within one week of the correspondence being received. During the year, the SFC received 1,653 enquiries and complaints from the investing public. Preliminary responses were provided within these time frames for all cases.

## Investment Products Division

The Investment Products Division has pledged to take up all applications for authorisation of investment products and prospectuses within two working days of their receipt. This pledge has been met in 99% of the applications received over the year. The Division has also pledged to respond to applicants within one week of take-up for unit trust, mutual funds and investment-linked products, and to applicants for other products within two weeks. This pledge was met in 98% of applicants for unit trusts, mutual funds and investment-linked products, and 100% for other products. Each of the cases where some delay was experienced involved complicated policy issues, and responses were made within a few days of the pledged time.

## Takeovers and Mergers Department

The Takeovers and Mergers Department has pledged that it will respond to an announcement on the same day it is received, will issue a requisition on offer/offeree documents within three days of receipt, and will give its decision on waiver applications within five days of receipt of all the information required to process the application. These standards were met in relation to all draft announcements lodged before 6 pm and in relation to offer/offeree documents. They were not met in relation to all waiver applications due to the need to clarify or confirm the information provided in relation to the applications concerned, although in all cases the applicant received a response within five days.

## Licensing Department

The Licensing Department has pledged that it will respond to applications for registrations within two working days of receipt, and process applications from principal agents and representatives within 15 weeks and 10 weeks respectively after they have submitted all supporting documents.

During the year, applications processing time for principal applicants and representatives whose applications were properly completed and supported by proper documentation has been reduced to an average time of 11 weeks and 5 weeks respectively while acknowledgment of applications were generally within the two-day time frame. About 92% of applications were processed within the pledged time frame, as compared with 70% when the SFC made the pledge.

## Monitoring of Pledges - the Public's Role

The SFC will monitor its performance of these pledges and will publish the results of this monitoring annually.

There will of course be occasions when, despite best efforts, the SFC will not be able to meet its performance pledges or will be unable to deal with public enquiries, complaints, or application to everyone's satisfaction. If investors would like to discuss this with a staff member other than the one with whom they have been dealing, they may call the Senior Manager, Corporate Communications on 2849-9287.



## Committees of the SFC

### Advisory Committee

#### Members

Henry Cheng Kar-Shun, Managing Director  
New World Development Co. Ltd.  
Henry Cheong Ying-Chew, Chairman & Chief Executive  
Officer  
Worldsec International Ltd.  
Victor L.L. Chu, Senior Partner  
Victor Chu & Co.  
Paul Fan Chor-Ho, Dealing Director  
Paul Fan Securities Ltd.  
Paul Gallagher, Group Operations Director  
Jardine Fleming Holdings Limited  
Philip J.S. Gray, Executive Chairman  
HSBC James Capel Asia Ltd.  
Leong Ka-Chai, Chairman  
Roctec International Limited  
Liang Xiaoting  
First Deputy General Manager  
Bank of China  
Patrick Wang Shui-Chung, Managing Director  
Johnson Electric Industrial Manufactory Limited  
Kevin A. Westley, Chief Executive  
HSBC Investment Bank Asia Holdings Ltd.  
David Wong, JP, Chairman  
Dah Sing Financial Holding Ltd.  
Dr. Alex Wu Shu-Chih, CBE, JP, Chairman  
Fidelity Management Ltd.  
Laura M Cha, JP, Executive Director (Corporate Finance)  
Securities and Futures Commission  
Anthony Francis Neoh, QC, JP, Chairman  
Securities and Futures Commission  
Michael Wu, JP, Deputy Chairman & Chief Operating  
Officer  
Securities and Futures Commission

### Securities and Futures Appeals Panel

#### Chairman

Robert C Tang, QC, JP

#### Deputy Chairman

Ronny Tong Ka-wah, QC

#### Members

Nicholas Allen, Partner - Audit Department  
Coopers & Lybrand

Iain F Bruce, Senior Partner  
KPMG Peat Marwick  
Marvin Cheung, OBE, JP, Partner  
KPMG Peat Marwick  
Alastair Crawford, Partner  
Freshfields  
(to 19 June 1996)  
Patrick P T Fung, QC  
Dudley L Harding, Partner  
Price Waterhouse  
Guy Henderson, Partner  
Allen & Overy Hong Kong  
(to 13 February 1997)  
Betty M F Ho  
Faculty of Law, University of Hong Kong  
Derek Murphy, Group Vice President  
First Pacific Co Ltd  
(to 10 January 1997)  
Rajat K Jindal, Partner  
Freshfields  
Thomas B Stevenson, Managing Partner  
Ernst & Young  
James P C Tien, OBE, JP, Chairman  
Manhattan Garments (Int'l) Ltd  
William Turnbull, OBE, JP  
Roderick B Woo, Managing Partner  
Zimmern & Co

### Takeovers and Mergers Panel

#### Chairman

Kevin Westley, Chief Executive  
HSBC Investment Bank Asia Holdings Limited  
Representative of Financial Institutions

#### Deputy Chairman

Clifton Chiu, Managing Director  
Harvester (Securities) Company Limited  
Representative of the Stock Exchange of Hong Kong

#### Members

#### Executive Directors and Staff of the Commission

Laura M Cha, Executive Director (Corporate Finance)  
Securities and Futures Commission  
David White, Executive Director (Supervision of Markets)  
Securities and Futures Commission



Mark Dickens

Executive Director (Enforcement)

*(from 1 Jan 1997)*

Senior Director (Corporate Finance)

*(to 31 Dec 1996)*

Securities and Futures Commission

Gerard J McMahon, Executive Director (Enforcement)

Securities and Futures Commission

*(to 31 Dec 1996)*

#### Representative of the Stock Exchange of Hong Kong

Lo Ka-Shui, Deputy Chairman and Managing Director

Great Eagle Holdings Limited

#### Representatives of Financial Institutions

Ian Boyce, Managing Director

Schroders Asia Limited

Dennis Cassidy, Management Consultant

Baines Gwinner

Stephen Clark, Director

Anglo Chinese Corporate Finance Limited

Peter Clarke, Chairman

Merrill Lynch (Asia Pacific) Limited

Victor L L Chu, Director

Kwong On Bank Ltd

Francis Leung, Managing Director

Peregrine Capital Limited

Liang Xiaoting, First Deputy General Manager

Bank of China

Liu Chee Ming, Managing Director

Platinum Securities Company Limited

Anthony Lo, Managing Director

ABN AMRO Hoare Govett Asia Corporate Finance Ltd

Patrick Sun, Director & Head of Investing Banking -

Greater China

Jardine Fleming Holdings Limited

David Blackett, Managing Director

NM Rothschild and Sons (HK) Limited

*(to 15 July 1996)*

#### Representatives of Other Constituencies with an Interest in Takeovers and Mergers

Denys E Connolly, OBE, JP

David Carse, Deputy Chief Executive (Banking)

Hong Kong Monetary Authority

Roderick E D Chalmers, Non-Executive Director

Securities and Futures Commission

Edward W S Cheng, Chief Executive

USI Holdings Limited

Henry H L Fan, Non-Executive Director

Securities and Futures Commission

Philip J S Gray, Executive Chairman

HSBC James Capel Asia Limited

Angelina Lee, Partner

Woo Kwan Lee & Lo

Frederick Ma, Deputy Chairman &

Deputy Managing Director

Kumagai Gumi (HK) Limited

#### Committee on Unit Trusts

##### Chair

Laura M Cha, Executive Director (Corporate Finance)

Securities and Futures Commission

##### Members

David Brennan, Managing Director

Baring International Asset Administration Limited

*(Full member from 1 April 1996)*

Roderick Chalmers, Non-Executive Director

Securities and Futures Commission

Deborah Glass, Senior Director (Investment Products)

Securities and Futures Commission

Jonathan Hubbard, Managing Director

HSBC Trustee (Hong Kong) Limited

Stuart H Leckie, Chairman, Asia-Pacific

Fidelity International Limited

Andrew Lo,

Chairman, Hong Kong Investment Funds Association

Chief Executive, INVESCO Asia Limited

David Lui, Director

Schroders Asia Limited

Robert Williams, Senior Vice President

State Street Bank and Trust Company

Anna H Y Wu, Senior Partner

Robert W H Wang and Company

John Wan, Principal Assistant Secretary

Representative of the Secretary for Financial Services

Hong Kong Government

##### Alternate Members

Peter Lord, Managing Director

LGT Asset Management Limited

Murray Simpson, Managing Director

Templeton Investment Services (Asia) Limited

A Grahame Stott, Managing Director

The Wyatt Company (HK) Limited

Marina Wong, Alternate Director

The Law Debenture Corporation (HK) Limited

Stella Yiu, Director

HSBC Asset Management (HK) Limited



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The Securities Compensation Committee administers the  
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