**G.N. 3679**

SECURITIES AND FUTURES ORDINANCE (Chapter 571)

Pursuant to section 240(9*b*) of the Securities and Futures Ordinance, the audited financial statements of the Investor Compensation Fund for the financial year ended 31 March 2010 are set out on pages 12695 to 12709.

Keith LUI *Chairman of*
*Investor Compensation Fund Committee*

INVESTOR COMPENSATION FUND (the Fund)
REPORT OF THE INVESTOR COMPENSATION FUND COMMITTEE
(the Committee)

The members of the Committee present their annual report and the audited financial statements for the year ended 31 March 2010.

1. *ESTABLISHMENT OF THE FUND*

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

2. *FINANCIAL RESULTS*

The Committee presents the financial results which are set out in the financial statements on pages 12697 to 12709.

3. *MEMBERS OF THE COMMITTEE*

The members of the Committee during the year ended 31 March 2010 and up to the date of this report were:—

Mr Keith LUI (*Chairman*)

Mr. Gerald GREINER (retired on 1 April 2010)

Mr. Kenneth H. W. KWOK, B.B.S., S.C.

Mrs. Alexa LAM

Mr. Eric YIP (appointed on 1 April 2010)

4. *INTERESTS IN CONTRACTS*

No contract of significance to which the Fund was a party and in which a Committee member had a material interest, whether directly or indirectly, subsisted at the end of the reporting period or at any time during the year.

5. *AUDITOR*

KPMG were first appointed as auditor of the Fund in 2003. KPMG retire and being eligible, offer themselves for re-appointment.

*28 May 2010*

On behalf of the Committee
Keith LUI
Chairman

## INDEPENDENT AUDITOR'S REPORT TO THE SECURITIES AND FUTURES COMMISSION (the SFC)

We have audited the financial statements of Investor Compensation Fund (the Fund) established under Part XII of the Securities and Futures Ordinance set out on pages 12695 to 12709 which comprise the statement of financial position as at 31 March 2010 and the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

*The SFC's responsibility for the financial statements*

The Securities and Futures Ordinance requires the directors of the SFC to keep proper accounts of the Fund and to prepare financial statements of the Fund in respect of each financial year. The directors of the SFC do so on the basis that these financial statements should give a true and fair view in accordance with International Financial Reporting Standards promulgated by the International Accounting Standards Board. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

*Auditor's responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. This report is made solely to you and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

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

*Opinion*

In our opinion, the financial statements give a true and fair view of the state of affairs of the Fund as at 31 March 2010 and of its result and cash flows for the year then ended in accordance with International Financial Reporting Standards.

*28 May 2010*

KPMG
Certified Public Accountants
8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

INVESTOR COMPENSATION FUND
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 MARCH 2010

*(Expressed in Hong Kong dollars)*

| | *Note* | *2010* $'000 | *2009* $'000 |
|---|---|---|---|
| *Income* | | | |
| Net investment income / (loss) | 5 | 154,796 | (32,716) |
| Exchange difference | | 1,733 | (2,596) |
| Recoveries | | 1,345 | — |
| | | 157,874 | (35,312) |
| *Expenses* | | | |
| Investor Compensation Company expenses | 7 | 4,165 | 4,235 |
| Compensation expense | 8 | 363 | 994 |
| Auditor's remuneration | | 86 | 84 |
| Bank charges | | 755 | 768 |
| Professional fees | | 2,975 | 2,827 |
| Sundry expenses | | — | 1 |
| | | 8,344 | 8,909 |
| Surplus/(deficit) and total comprehensive income for the year | | 149,530 | (44,221) |

The notes on pages 12701 to 12709 form part of these financial statements.

INVESTOR COMPENSATION FUND
STATEMENT OF FINANCIAL POSITION
AT 31 MARCH 2010

*(Expressed in Hong Kong dollars)*

| | Note | *2010* $'000 | *2009* $'000 |
|---|---|---|---|
| *Current assets* | | | |
| Financial assets designated at fair value through profit or loss | | | |
| —Debt securities | 9 | 1,517,803 | 1,554,614 |
| —Pooled Fund | 9 | 184,523 | 113,112 |
| Interest receivable | | 16,371 | 20,253 |
| Due from Investor Compensation Company | | 261 | 477 |
| Fixed and call deposits with banks | 10 | 150,452 | 116,037 |
| Cash at bank | 10 | 102,283 | 20,074 |
| | | 1,971,693 | 1,824,567 |
| *Current liabilities* | | | |
| Provision for compensation | 8 | 5,656 | 8,032 |
| Creditors and accrued charges | | 895 | 801 |
| Fair value adjustment on unsettled trades | | 7 | 129 |
| | | 6,558 | 8,962 |
| *Net current assets* | | 1,965,135 | 1,815,605 |
| *Net assets* | | 1,965,135 | 1,815,605 |
| Representing:— | | | |
| *Compensation fund* | | | |
| Contributions from Unified Exchange Compensation Fund | 11 | 994,718 | 994,718 |
| Contributions from Commodity Exchange Compensation Fund | 11 | 108,923 | 108,923 |
| Accumulated surplus | | 861,494 | 711,964 |
| | | 1,965,135 | 1,815,605 |

Approved and authorised for issue by the Securities and Futures Commission (the SFC) on 28 May 2010 and signed on its behalf by

Eddy FONG
*Chairman of the SFC*

Martin WHEATLEY
*Chief Executive Officer of the SFC*

The notes on pages 12701 to 12709 form part of these financial statements.

INVESTOR COMPENSATION FUND
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 MARCH 2010

*(Expressed in Hong Kong dollars)*

| | Contributions from Unified Exchange Compensation Fund | Contributions from Commodity Exchange Compensation Fund | Accumulated surplus | Total |
|---|---|---|---|---|
| | $'000 | $'000 | $'000 | $'000 |
| Balance at 1 April 2008 | 994,718 | 108,923 | 756,185 | 1,859,826 |
| Total comprehensive income for the year | — | — | (44,221) | (44,221) |
| Balance at 31 March 2009 | 994,718 | 108,923 | 711,964 | 1,815,605 |
| Balance at 1 April 2009 | 994,718 | 108,923 | 711,964 | 1,815,605 |
| Total comprehensive income for the year | — | — | 149,530 | 149,530 |
| Balance at 31 March 2010 | 994,718 | 108,923 | 861,494 | 1,965,135 |

The notes on pages 12701 to 12709 form part of these financial statements.

# INVESTOR COMPENSATION FUND
# STATEMENT OF CASH FLOWS
# FOR THE YEAR ENDED 31 MARCH 2010

*(Expressed in Hong Kong dollars)*

| | *2010* $'000 | *2009* $'000 |
|---|---|---|
| *Cash flows from operating activities* | | |
| Surplus / (loss) for the year | 149,530 | (44,221) |
| Net investment (income) / loss | (154,796) | 32,716 |
| Exchange difference | (1,733) | 2,596 |
| Decrease in amount due from Investor Compensation Company | 216 | 59 |
| Decrease in unsettled regular purchase of financial assets | — | 46,987 |
| Decrease in provision for compensation | (2,376) | (14,946) |
| Increase / (decrease) in accounts payable and accrued charges | 94 | (85) |
| Net cash (used in) / generated from operating activities | (9,065) | 23,106 |
| *Cash flows from investing activities* | | |
| Purchase of debt securities | (1,158,241) | (1,346,351) |
| Sale or maturity of debt securities | 1,220,937 | 1,279,250 |
| Sale of equity securities | 733 | 861 |
| Interest received | 62,260 | 69,545 |
| Net cash generated from investing activities | 125,689 | 3,305 |
| Net increase in cash and cash equivalents | 116,624 | 26,411 |
| Cash and cash equivalents at beginning of the year | 136,111 | 109,700 |
| *Cash and cash equivalents at end of the year* | 252,735 | 136,111 |

*Analysis of the balance of cash and cash equivalents:—*

| | *2010* $'000 | *2009* $'000 |
|---|---|---|
| Fixed and call deposits with banks | 150,452 | 116,037 |
| Cash at bank | 102,283 | 20,074 |
| | 252,735 | 136,111 |

INVESTOR COMPENSATION FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2010

*(Expressed in Hong Kong dollars)*

1. *PURPOSE, LIMITATION AND PRINCIPAL ACTIVITY*

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

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

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

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

2. *MONEY CONSTITUTING THE FUND*

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

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

3. *SIGNIFICANT ACCOUNTING POLICIES*

The Fund prepares its financial statements in accordance with International Financial Reporting Standards (IFRSs) (including applicable International Accounting Standards and Interpretations) promulgated by the International Accounting Standards Board (IASB). We set out below a summary of our significant accounting policies.

*Basis of preparation*

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

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

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

*Recognition of income*

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

*Net investment income*—Net investment income comprises (i) interest income from bank deposits and debt securities; (ii) unrealised gain or loss on revaluation of debt securities and equity securities and (iii) realised gain or loss on redemption and disposal of debt securities and equity securities. We record interest income as it accrues using the effective interest method.

*Translation of foreign currencies*

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

*Financial instruments*

(i) *Initial recognition*

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

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

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

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

(ii) *Fair value measurement principles*

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

(iii) *Derecognition*

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

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

(iv) *Offsetting*

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

*Impairment*

(i) *Recognition of impairment loss*

We review the carrying amounts of the Fund's assets at the end of each reporting period to determine whether there is any objective evidence of impairment. If any such evidence exists, we estimate the asset's recoverable amount. We recognise in the statement of comprehensive income the difference between the asset's carrying amount and the recoverable amount as an impairment loss whenever the carrying amount of an asset exceeds its recoverable amount.

(ii) *Calculation of impairment loss*

We calculate the recoverable amount of the Fund's receivables by discounting their expected future cash flows to their present value at the original effective interest rate inherent in the asset. We do not discount receivables with a short duration in the calculation of their recoverable amount.

(iii) *Reversals of impairment loss*

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

*Cash and cash equivalents*

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition.

*Other receivables*

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

*Provision for compensation*

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

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

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

*Creditors and accrued charges*

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

*Contingent liabilities*

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

*Related parties*

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

(i) parties that the Fund has the ability, directly or indirectly, to control or to significantly influence in making financial and operating decisions;

(ii) parties that have the ability, directly or indirectly, to control or to significantly influence the Fund in making financial and operating decisions; and

(iii) parties that are subject to common control or common significant influence.

Related parties may be individuals (being members of key management personnel, and/or their close family members) or other entities and include entities which are under the significant influence of related parties of the Fund where those parties are individuals.

*Changes in accounting policies*

The IASB has issued a number of new interpretations and an amendment to IFRSs that are first effective for the current accounting period of the Fund. Of these, the following developments are relevant to the Fund's financial statements:—

- IAS 1 (revised 2007), Presentation of financial statements
- Amendments to IFRS 7, Financial instruments: Disclosures—improving disclosure about financial instruments

The revised standard requires all owner changes in equity to be presented in the statement of changes in equity, whereas all non-owner changes in equity are presented in the statement of comprehensive income. The application of the revised standard did not have any impact on reported surplus or deficit, total income and expense or net assets for any period presented.

As a result of the adoption of the amendments to IFRS 7, the financial statements include expanded disclosures in note 13 about the fair value measurement of the Fund's financial instruments, categorising these fair value measurements into a three-level fair value hierarchy according to the extend to which they are based on observable market data. The Fund has taken advantage of the transitional provisions set out in the amendments to IFRS 7, under which comparative information for the newly required disclosures about the fair value measurements of financial instruments has not been provided.

4. *TAXATION*

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

5. *NET INVESTMENT INCOME / (LOSS)*

| | *2010* $'000 | *2009* $'000 |
|---|---|---|
| Interest income from bank deposits | 129 | 1,497 |
| Interest income on financial assets designated at fair value through profit or loss | 52,853 | 64,446 |
| Realised gain / (loss) on disposal of equity securities | 5 | (34) |
| Realised gain / (loss) on redemption/disposal of debt securities | 4,043 | (14,285) |
| Gain / (loss) on revaluation of equity securities | 71,812 | (88,496) |
| Gain on revaluation of debt securities | 25,954 | 4,156 |
| Net investment income / (loss) | 154,796 | (32,716) |

Interest income from bank deposits and debt securities is derived as follows:—

| | *2010* $'000 | *2009* $'000 |
|---|---|---|
| Interest income on financial assets not at fair value through profit or loss | 129 | 1,497 |
| Interest income on financial assets designated at fair value through profit or loss | 52,853 | 64,446 |
| | 52,982 | 65,943 |

6. *LEVY FROM THE SEHK / HKFE*

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

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

7. *ICC EXPENSES*

The SFC formed the ICC in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the SFO. The Fund is responsible for funding the establishment and operation of ICC. For the year ended 31 March 2010, ICC incurred costs of $4,165,000 for its operations (2009: $4,235,000).

8. *PROVISION FOR COMPENSATION*

| | $'000 |
|---|---|
| Balance as at 31 March 2008 | 22,978 |
| Add: provision made during the year ended 31 March 2009 | 4,679 |
| Less: provision reversed during the year ended 31 March 2009 | (3,685) |
| Less: compensation paid during the year ended 31 March 2009 | (15,940) |
| Balance as at 31 March 2009 | 8,032 |
| Add: provision made during the year ended 31 March 2010 | 363 |
| Less: compensation paid during the year ended 31 March 2010 | (2,739) |
| Balance as at 31 March 2010 | 5,656 |

We maintained provision for liabilities arising from claims received resulting from three default cases for which ICC has published a notice calling for claims pursuant to Section 3 of the Securities & Futures (Investor Compensation-Claims) Rules. The maximum liability of the Fund to claims for these cases is set at $150,000 per claimant. As at 31 March 2010 all provisions were expected to be paid within one year.

9. *FINANCIAL ASSETS DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS*

| | *2010* $'000 | *2009* $'000 |
|---|---|---|
| (*a*) Debt securities | | |
| (i) Listing status | | |
| Listed—outside Hong Kong at quoted market prices | 345,199 | 282,991 |
| Listed—outside Hong Kong based on valuation techniques | 63,001 | 35,630 |
| Listed—in Hong Kong | 51,608 | 110,578 |
| Unlisted | 1,057,995 | 1,125,415 |
| | 1,517,803 | 1,554,614 |
| (ii) Maturity profile | | |
| Within one year | 317,118 | 526,000 |
| After one year but within two years | 406,937 | 237,674 |
| After two years but within five years | 629,833 | 607,542 |
| After five years | 163,915 | 183,398 |
| | 1,517,803 | 1,554,614 |

(iii) The weighted average effective interest rate of debt securities on 31 March 2010 was 2.0% (2009 : 2.7%).

| | | |
|---|---|---|
| (*b*) Pooled fund—Unlisted | 184,523 | 113,112 |

The pooled fund comprises mainly listed equity securities.

10. *DEPOSITS WITH BANKS AND CASH AT BANK*

The effective interest rate on deposits with banks and cash at bank at 31 March 2010 ranged from 0.04% to 0.2% (2009: 0.4% to 0.72%). The balances mature within one year at both 31 March 2010 and 31 March 2009.

11. *CONTRIBUTIONS FROM UECF AND CECF*

Under Sections 74(2) and 75(2) of Schedule 10 of the SFO, the SFC may pay into the Fund such sum of money from the UECF and the CECF as it considers appropriate after 1 April

2003. Up to 31 March 2010, the SFC had $994,718,000 (2009 : $994,718,000) and $108,923,000 (2009 : $108,923,000) paid into the Fund from the UECF and the CECF respectively.

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

12. *RELATED PARTY TRANSACTIONS*

We have related party relationships with the SFC, the ICC, the SEHK, the HKFE and the UECF. During the year, there were no significant related party transactions other than those disclosed in the financial statements (refer to notes 6, 7 & 11).

13. *FINANCIAL INSTRUMENTS*

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

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

(i) *Credit risk*

The Fund's Investment Policy and Administrative Guidelines (Policy) only allows the Fund to invest in pooled funds, fixed rate dated securities rated A or above or in bank deposits. The Policy further limits the Fund's exposure to each issuer and each country, except for holdings of the US Treasuries, any issuances by Hong Kong Government and specified multilateral agencies rated AAA by Moody's or S&P's and approved pooled funds. The Fund's investment managers are responsible for managing the portfolio and ensuring the portfolio's investments meet the investment policy and restrictions and reports thereon on a monthly basis. During the year, the Fund complied with the above investment policy and, as a result, was not exposed to significant credit risk. The maximum exposure to credit risk is the carrying value of the assets in the statement of financial position.

(ii) *Liquidity risk*

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

(iii) *Interest rate risk*

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

The Fund is subject to the risk that future cash flows of a debt security will fluctuate because of changes in market interest rates. In order to manage the re-pricing risk, the Fund adopts a policy of maintaining duration at no more than 2.5 years within its debt securities portfolio. As at 31 March 2010 the duration was 2.11 years (31 March 2009: 2.13 years).

At 31 March 2010, it is estimated that a general increase/decrease of 100 basis points in 3-month interest rates, with all other variables held constant, would decrease/increase the Fund's gains on revaluation of debt securities and the accumulated surplus by approximately $35 million (2009: $35.4 million). Further, at 31 March 2010, it is estimated that a general increase of 100 basis points in 3 month interest rates, with all other variables held constant, would increase the Fund's surplus and accumulated surplus by approximately $3 million (2009: $4.6 million). The extent of any decrease in interest rates is expected to be minimal (2009: 1%) which would decrease the Fund's surplus by an insignificant amount (2009: $4.6 million). Other components of accumulated surplus would not be affected (2009: Nil) by the changes in interest rates.

The sensitivity analysis above indicates the instantaneous change in the Fund's accumulated surplus that would arise assuming that the change in interest rates had occurred at the end of the reporting period and had been applied to re-measure those financial instruments held by the Fund which expose the Fund to fair value interest rate risk at the end of the reporting period. The analysis is performed on the same basis for 2009.

(iv) *Exchange rate risk*

The Fund's investment policy allows the Fund to have US dollar foreign exchange exposure. As the HK dollar is pegged with the US dollar, the Fund was not exposed to significant foreign exchange risk.

(v) *Market risk*

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

The Fund invests in units of a pooled fund, which mainly comprises listed equity securities, the performance of which is measured against the benchmark index MSCI AC Pacific ex Japan. It is estimated that a general increase/decrease of 24.2% in the benchmark index would increase/decrease the Fund's profit and accumulated surplus by approximately $36 million (2009: a general increase/decrease of 27.5% in the benchmark index would decrease/increase the Fund's loss and increase/decrease the Fund's accumulated surplus by approximately $23.2 million).

The sensitivity analysis indicates the instantaneous change in the Fund's accumulated surplus that would arise assuming that the changes in the benchmark index had occurred at the end of the reporting period and had been applied to re-measure those financial instruments held by the Fund which expose the Fund to equity price risk at the end of the reporting period. It is also assumed that the fair values of the Fund's investment in pooled fund would change in accordance with the historical correlation with the relevant benchmark index since the portfolio is diversified in terms of industry distribution and that all other variables remain constant. The analysis is performed on the same basis for 2009.

(vi) *Fair values of financial instruments*

The following table presents the carrying value of financial instruments measured at fair value at the end of the reporting period across the three levels of the fair value hierarchy defined in IFRS 7, with the fair value of each financial instrument categorised in its entirety based on the lowest level of input that is significant to that fair value measurement. The levels are defined as follows:—

• Level 1 (highest level): fair values meaured using quoted prices (unadjusted) in active markets for identical financial instruments

• Level 2: fair values measured using quoted prices in active markets for similar financial instruments, or using valuation techniques in which all significant inputs are directly or indirectly based on observable market data

• Level 3: (lowest level): fair values measured using valuation techniques in which any significant input is not based on observable market data

All financial instruments are carried at amounts not materially different from their fair values as at 31 March 2010 and 2009.

Where available, the fair value of the debt securities is the quoted market price. The fair value of unlisted debt securities is determined based on quotes from bond market-makers.

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

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

| | 2010 | | | |
|---|---|---|---|---|
| | Level 1 $'000 | Level 2 $'000 | Level 3 $'000 | Total $'000 |
| *Assets* | | | | |
| Trading securities | | | | |
| —listed | 396,807 | 63,001 | — | 459,808 |
| —unlisted | 277,500 | 780,495 | — | 1,057,995 |
| Pooled fund | | | | |
| —unlisted | 184,523 | — | — | 184,523 |
| | 858,830 | 843,496 | — | 1,702,326 |

During the year there were no significant transfers between financial instruments in Level 1 and Level 2.

14. *CONTINGENT LIABILITIES*

As at the date of this report, in addition to the provision made, as described in note 8, there are other claims received for which currently there is insufficient information to determine the likely level of payment. The maximum liability in respect of these claims is $450,000 (2009: $450,000). This is determined based on the lower of the maximum compensation limit of $150,000 per claimant or the amount claimed.

15. *POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ANNUAL ACCOUNTING PERIOD ENDED 31 MARCH 2010*

Up to the date of issue of these financial statements, the IASB has issued a number of amendments, new standards and interpretations which are not yet effective for the year ended 31 March 2010 and which have not been adopted in these financial statements.

The Fund is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application.

So far it has concluded that the adoption of them is unlikely to result in a restatement of the Fund's results of operations and financial position.

In addition, the following developments may result in amended disclosures in the financial statements, including restatement of comparative amounts in the first period of adoption:—

| | *Effective for accounting periods beginning on or after* |
|---|---|
| *Improvements to IFRS: 2009* | *1 July 2009 or 1 January 2010* |