

SECURITIES AND FUTURES ORDINANCE (Chapter 571)

Pursuant to Section 240(9b) of the Securities and Futures Ordinance, the audited financial statements of the Investor Compensation Fund for the financial year ended 31 March 2019 are set out on pages 17634 to 17650.

Keith LUI *Chairman of  
Investor Compensation Fund Committee*

INVESTOR COMPENSATION FUND  
REPORT OF THE INVESTOR COMPENSATION FUND COMMITTEE

The members of the Investor Compensation Fund Committee (the Committee) present their annual report together with the audited financial statements for the year ended 31 March 2019.

**Establishment of the Investor Compensation Fund**

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

**Financial statements**

The financial performance of the Fund for the financial year ended 31 March 2019 and the financial position of the Fund as at that date are set out in the financial statements on pages 17637 to 17650.

**Members of the Committee**

The members of the Committee during the year ended 31 March 2019 and up to the date of this report were:

Mr Keith Lui (Chairman)	
Mr Thomas Allan Atkinson	
Ms Teresa Ko Yuk-yin, JP	(retired on 31 July 2018)
Dr William Wong Ming Fung, SC	(appointed on 1 August 2018)
Mr Lee Kwok Keung	(retired on 31 December 2018)
Mr Tai Chi Kin Calvin	(appointed on 1 January 2019)

**Interests in contracts**

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

**Auditor**

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

27 May 2019

*By order of the Committee  
Keith LUI  
Chairman*

INDEPENDENT AUDITOR'S REPORT  
TO THE SECURITIES AND FUTURES COMMISSION

**Opinion**

*What we have audited*

The financial statements of Investor Compensation Fund (the Fund) established under Part XII of the Securities and Futures Ordinance set out on pages 17637 to 17650, which comprise:

- the statement of financial position as at 31 March 2019;
- the statement of profit or loss and other comprehensive income for the year then ended;

- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

#### *Our opinion*

In our opinion, the financial statements give a true and fair view of the financial position of the Fund as at 31 March 2019, and of its financial performance and its cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards (HKFRSs) issued by the Hong Kong Institute of Certified Public Accountants (HKICPA).

#### **Basis for opinion**

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

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

#### *Independence*

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

#### **Other information**

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

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

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

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

#### **Responsibilities of directors of the SFC for the financial statements**

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

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

#### **Auditor's responsibilities for the audit of the financial statements**

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors of the SFC.
- Conclude on the appropriateness of the directors of the SFC's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

27 May 2019

PricewaterhouseCoopers  
Certified Public Accountants  
Hong Kong

INVESTOR COMPENSATION FUND  
STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME  
FOR THE YEAR ENDED 31 MARCH 2019

*(Expressed in Hong Kong dollars)*

	<i>Note</i>	2019 \$'000	2018 \$'000
<b>Income</b>			
Net investment income	5	38,557	73,603
Exchange difference		(490)	16,504
Recoveries		50	1,620
Compensation payment given up		150	-
		38,267	91,727
<b>Expenses</b>			
Investor Compensation Company Limited expenses	7	5,859	5,729
Auditor's remuneration		172	166
Bank charges		409	968
Professional fees		1,472	4,120
		7,912	10,983
<b>Surplus and total comprehensive income for the year</b>		<b>30,355</b>	<b>80,744</b>

The notes on pages 17641 to 17650 form part of these financial statements.

INVESTOR COMPENSATION FUND  
STATEMENT OF FINANCIAL POSITION  
AS AT 31 MARCH 2019

*(Expressed in Hong Kong dollars)*

	Note	2019 \$'000	2018 \$'000
<b>Current assets</b>			
Financial assets at fair value through profit or loss			
- Debt securities	8	-	1,939,279
- Pooled fund	8	-	350,084
Interest receivable		25,425	17,015
Due from Investor Compensation Company Limited		54	203
Fixed deposits with banks	9	2,365,483	52,586
Cash at bank	9	845	3,347
		2,391,807	2,362,514
<b>Current liabilities</b>			
Creditors and accrued charges		302	1,364
		302	1,364
<b>Net current assets</b>		2,391,505	2,361,150
<b>Net assets</b>		2,391,505	2,361,150
Representing :			
<b>Compensation fund</b>		2,391,505	2,361,150

Approved and authorised for issue by the Securities and Futures Commission on 27 May 2019 and signed on its behalf by

Tim Lui  
Chairman of the SFC

Ashley Alder  
Chief Executive Officer of the SFC

The notes on pages 17641 to 17650 form part of these financial statements.

INVESTOR COMPENSATION FUND  
STATEMENT OF CHANGES IN EQUITY  
FOR THE YEAR ENDED 31 MARCH 2019

*(Expressed in Hong Kong dollars)*

	Contributions from Unified Exchange Compensation Fund (note 10)	Contributions from Commodity Exchange Compensation Fund (note 10)	Accumulated surplus	Total
	\$'000	\$'000	\$'000	\$'000
Balance at 1 April 2017	994,718	108,923	1,176,765	2,280,406
Surplus and total comprehensive income for the year	-	-	80,744	80,744
Balance at 31 March 2018 and 1 April 2018	994,718	108,923	1,257,509	2,361,150
Surplus and total comprehensive income for the year	-	-	30,355	30,355
Balance at 31 March 2019	<u>994,718</u>	<u>108,923</u>	<u>1,287,864</u>	<u>2,391,505</u>

The notes on pages 17641 to 17650 form part of these financial statements.

INVESTOR COMPENSATION FUND  
STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED 31 MARCH 2019

*(Expressed in Hong Kong dollars)*

	<i>Note</i>	2019 \$'000	2018 \$'000
<b>Cash flows from operating activities</b>			
Surplus and total comprehensive income for the year		30,355	80,744
Adjustments for:			
Net investment income		(38,557)	(73,603)
Exchange difference		490	(16,504)
		(7,712)	(9,363)
Decrease/(increase) in amount due from Investor Compensation Company Limited		149	(128)
Decrease in provision for compensation		-	(476)
Decrease in creditors and accrued charges		(1,062)	(85)
Net cash used in operating activities		(8,625)	(10,052)
<b>Cash flows from investing activities</b>			
Increase in fixed deposits other than cash and cash equivalents		(2,333,384)	-
Debt securities purchased		(165,306)	(1,100,731)
Debt securities sold or redeemed		2,092,869	1,037,862
Pooled fund sold		338,934	36,789
Interest received		52,523	47,094
Net cash (used in)/generated from investing activities		(14,364)	21,014
Net (decrease)/increase in cash and cash equivalents		(22,989)	10,962
Cash and cash equivalents at beginning of the year		55,933	44,971
<b>Cash and cash equivalents at end of the year</b>	<b>9</b>	<b>32,944</b>	<b>55,933</b>
<b>Analysis of the balance of cash and cash equivalents</b>			
		2019 \$'000	2018 \$'000
Fixed deposits with banks		32,099	52,586
Cash at bank		845	3,347
		32,944	55,933

The notes on pages 17641 to 17650 form part of these financial statements.

INVESTOR COMPENSATION FUND  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 MARCH 2019

*(Expressed in Hong Kong dollars)*

1. *Purpose, limitation and principal activity*

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

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

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

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

2. *Money constituting the Fund*

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

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

3. *Significant accounting policies*

(a) *Statement of compliance*

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

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

The Fund has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 14).



(b) *Basis of preparation*

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

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

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

(c) *Recognition of income*

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

(d) *Translation of foreign currencies*

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

(e) *Financial assets*

(i) Classification

From 1 April 2018, the Fund classifies its financial assets in the following measurement categories:

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

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

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

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

(ii) Recognition and derecognition

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

(iii) Measurement

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

### *Debt instruments*

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

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

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

#### (iv) Impairment

From 1 April 2018, the Fund assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortised cost. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

#### (v) Accounting policies applied until 31 March 2018

We have applied HKFRS 9 retrospectively, but have elected not to restate comparative information. As a result, the comparative information provided continues to be accounted for in accordance with the previous accounting policy.

### *Classification*

Until 31 March 2018, we classify our financial assets into the following categories:

- financial assets at fair value through profit or loss, and
- loans and receivables

The classification determined on the purpose for which the investments were acquired. We determined the classification of its investments at initial recognition.

### *Subsequent measurement*

The measurement at initial recognition did not change on the adoption of HKFRS 9. Subsequent to the initial recognition, loans and receivables were carried at amortised cost using the effective interest method. Financial assets at FVPL were subsequently carried at fair value. Gains or losses arising from changes in the fair value are recognised in the statement of profit or loss and other comprehensive income.

### *Impairment*

The Fund assessed at the end of each reporting period whether there was objective evidence that a financial asset was impaired. A financial asset was impaired and impairment losses were incurred only if there was objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event (or events) had an impact on the estimated future cash flows of the financial asset that could be reliably estimated.

For loans and receivables carried at amortised cost, the amount of the loss was measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that had not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset was reduced and the amount of the loss was recognised in the statement of profit or loss and other comprehensive income. If a loan had a variable interest rate, the discount rate for measuring any impairment loss was the current effective interest rate determined under the contract. As a practical expedient, the Fund could measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreased and the decrease could be related objectively to an event occurring after the impairment was

recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss was recognised in the statement of profit or loss and other comprehensive income.

(f) *Cash and cash equivalents*

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

(g) *Other receivables*

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

(h) *Provisions for compensation*

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

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

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

(i) *Creditors and accrued charges*

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

(j) *Provisions and contingent liabilities*

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

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

(k) *Related parties*

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

- (a) A person, or a close member of that person's family, is related to the Fund if that person:
  - (i) has control or joint control over the Fund;
  - (ii) has significant influence over the Fund; or
  - (iii) is a member of the key management personnel of the Fund.
- (b) An entity is related to the Fund if any of the following conditions applies:
  - (i) The entity and the Fund are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

- (ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
- (iii) Both entities are joint ventures of the same third party.
- (iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
- (v) The entity is a post-employment benefit plan for the benefit of employees of either the Fund or an entity related to the Fund.
- (vi) The entity is controlled or jointly controlled by a person identified in (a).
- (vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
- (viii) The entity, or any member of a group of which it is a part, provides key management personnel services to the Fund.

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

(l) *Changes in accounting policies*

The HKICPA has issued a number of amendments to HKFRSs that are first effective for the current accounting period of the Fund. Except as described below, these developments have had no material effect on how the Fund's results and financial position for the current or prior periods have been prepared or presented.

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

*HKFRS 9, Financial Instruments*

HKFRS 9 replaces the provisions of HKAS 39, Financial Instruments: Recognition and Measurement that relate to the recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets.

The adoption of HKFRS 9 resulted in changes in accounting policies and potential adjustments to the amounts recognised in the financial statements. In accordance with the transitional provisions in HKFRS 9, comparative figures need not be restated.

As part of the transition to HKFRS 9, financial assets that we managed on a fair value basis had previously been designated at fair value through profit or loss under HKAS 39, continue to be classified as fair value through profit or loss. Other financial assets that were previously measured at amortised cost (eg, fixed deposits with banks) will continue with their classification and measurement.

There was no impact on the amounts recognised in relation to these assets from the adoption of HKFRS 9.

4. *Taxation*

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

5. *Net investment income*

	2019 \$'000	2018 \$'000
Interest income from bank deposits	34,947	828
Interest income on financial assets at fair value through profit or loss	22,629	44,455
Realised (loss)/gain on disposal of pooled fund	(10,350)	989
Realised (loss)/gain on redemption/disposal of debt securities	(8,669)	2,422
Gain on revaluation of pooled fund	—	52,138
Loss on revaluation of debt securities	—	(27,229)
Net investment income	<u>38,557</u>	<u>73,603</u>

6. *Levy from SEHK and HKFE*

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

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

7. *ICC expenses*

The SFC formed the ICC in September 2002 to perform functions on behalf of the Fund in relation to the compensation to investors and other functions under Part III and Part XII of the SFO. The Fund is responsible for funding the establishment and operation of the ICC. For the year ended 31 March 2019, the ICC incurred costs of \$5,859,000 for its operations (2018: \$5,729,000) which were reimbursed by the Fund.

8. *Financial assets at fair value through profit or loss*

	<i>2019</i>	<i>2018</i>
	<i>\$'000</i>	<i>\$'000</i>
(a) Debt securities		
(i) Listing status		
Listed–outside Hong Kong	—	1,103,850
Listed–in Hong Kong	—	443,133
Unlisted	—	392,296
	<u>—</u>	<u>1,939,279</u>
(ii) Maturity profile		
Within one year	—	404,749
After one year but within two years	—	454,873
After two years but within five years	—	1,001,791
After five years	—	77,866
	<u>—</u>	<u>1,939,279</u>

(iii) The weighted average effective interest rate of debt securities on 31 March 2018 was 2.9%.

The debt securities were fully matured or disposed of during the year ended 31 March 2019.

(b) Pooled fund–Unlisted	<u>—</u>	<u>350,084</u>
--------------------------	----------	----------------

The pooled fund, comprising mainly listed equity securities, was fully disposed of during the year ended 31 March 2019.

9. *Fixed deposits with banks and cash at bank*

The effective interest rate on bank deposits at 31 March 2019 ranged from 1.40% to 3.44% (2018: 0.80% to 1.53%). The balances of deposits at both 31 March 2019 and 31 March 2018 mature within one year.

Reconciliation with the statement of financial position

	2019 \$'000	2018 \$'000
Cash at bank	845	3,347
Fixed deposits with banks	<u>2,365,483</u>	<u>52,586</u>
Amounts shown in the statement of financial position	2,366,328	55,933
Less: Amounts with an original maturity of beyond three months	<u>(2,333,384)</u>	<u>—</u>
Cash and cash equivalents in the statement of cash flows	<u>32,944</u>	<u>55,933</u>

10. *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 2019, the SFC had \$994,718,000 (2018: \$994,718,000) and \$108,923,000 (2018: \$108,923,000) paid into the Fund from the UECF and the CECF respectively.

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

11. *Material related party transactions*

We have related party relationships with the SFC, ICC and the UECF. There were no significant related party transactions other than those disclosed in the financial statements of the Fund for the years ended 31 March 2018 and 2019 (refer to notes 7 and 10).

12. *Financial risk management and fair values*

The financial assets of the Fund mainly comprised fixed deposits with banks (2018: fixed deposits with banks, debt securities and units in a pooled fund). The underlying investments of the pooled fund mainly comprised equity securities.

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

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

(a) Credit risk

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

(b) Liquidity risk

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

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

(c) Interest rate risk

The Fund's interest bearing assets comprised fixed deposits with banks (2018: debt securities and fixed deposits with banks). The Fund's bank deposits are exposed to short-term bank deposit interest re-pricing risk.

As at 31 March 2019, the Fund did not have any investment in debt securities.

At 31 March 2018, the Fund was subject to the risk that future cash flows of a debt security would fluctuate because of changes in market interest rates. In order to manage the re-pricing risk, the Fund adopted a policy of maintaining duration at no more than five years within its debt securities portfolio. As at 31 March 2018, the duration was 2.26 years and it was estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would decrease/increase the Fund's gains on revaluation of debt securities and the accumulated surplus by approximately \$44,803,000.

At 31 March 2019, it was estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would increase/decrease the Fund's interest income and the accumulated surplus by approximately \$23,655,000 (2018: \$2,990,000).

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 periods 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 was performed on the same basis for the year ended 31 March 2018.

(d) Foreign currency risk

The Fund's investment policy allows the Fund to have US dollars and renminbi foreign exchange exposures. As at 31 March 2019, the Fund had exposure to US dollars only. As Hong Kong dollars are pegged with US dollars, the Fund was not exposed to significant foreign exchange risk at the end of the reporting period.

(e) Market risk

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

As at 31 March 2019, the Fund did not have any investment in debt and equity securities.

As at 31 March 2018, the Fund invested in units of a pooled fund, which mainly comprised listed equity securities, the performance of which was measured against the benchmark index MSCI AC Pacific ex Japan. It was estimated that a general increase/decrease of 14.5% in the benchmark index would increase/decrease the Fund's surplus and the accumulated surplus by approximately \$50,062,000.

The sensitivity analysis above indicated 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 was also assumed that the fair values of the Fund's investment in the 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.

(f) Fair values of financial instruments

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

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

All financial instruments are carried at amounts not materially different from their fair values as at 31 March 2019 and 2018.

The fair value of the debt securities as at 31 March 2018 was the quoted market price or based on quotes from bond market-makers.

The fair value of the investment in the unlisted pooled fund as at 31 March 2018 was 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 were listed securities.

Changes in 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.

	2019			
	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
Assets				
Debt securities and pooled fund	—	—	—	—
	2018			
	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
Assets				
Debt securities				
–Listed	1,271,926	275,057	—	1,546,983
–Unlisted	11,169	381,127	—	392,296
Pooled fund				
–Unlisted	350,084	—	—	350,084
	<u>1,633,179</u>	<u>656,184</u>	<u>—</u>	<u>2,289,363</u>

13. *Provision for compensation and contingent liabilities*

The Fund assessed and concluded that there was no provision for compensation as at 31 March 2019 and 2018.

As at the date of this report, there are 15 claims received for which currently there is insufficient information to determine the likely level of payment. The maximum liability in respect of these claims is \$2,121,000 (2018: \$2,375,000). This is determined based on the lower of the maximum compensation limit of \$150,000 per claimant or the amount claimed.

14. *Possible impact of amendments, new standards and interpretations issued but not yet effective for the year ended 31 March 2019*

Up to the date of issue of these financial statements, the HKICPA has issued a number of amendments and new standards which are not yet effective for the year ended 31 March 2019 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 and new standards is expected to be in the period of initial application. So far it has concluded that the adoption of them is unlikely to have a significant impact on the Fund's results of operations and financial position.