EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU
(Limited by guarantee)

REPORT AND ACCOUNTS

FOR THE YEAR ENDED

31 DECEMBER 2019

**EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU**

**REPORT OF THE COUNCIL MEMBERS**

The Council Members have pleasure in submitting their annual report together with the audited financial statements for the year ended 31 December 2019.

**Principal activities and business review**

*A fair review of the Bureau's business*

The Bureau has a limited scope as a specific public service dictated by its Articles of Association in administering a fund, namely the Employees Compensation Insurer Insolvency Scheme to assume responsibility for the liabilities of insurers engaging in employees' compensation business that become insolvent on or after 1 April 2004, as set out in Legal status, Note 1 on page 11 to the Financial Statements which forms part of this Business Review and as also detailed in the Bureau's website at www.eciib.com.hk.

There were no significant developments in the business of the Bureau during the year and it remains in good financial health as summarized by the below key financial information:

| | 2019 | 2018 |
|---|---|---|
| Members' contributions | HK$141.8 million | HK$123.3 million |
| Net assets | HK$2,222.5 million | HK$1,884.4 million |
| Claims paid | Nil | Nil |
| Claims liabilities | Nil | Nil |
| Number of outstanding claims | Nil | Nil |

The Bureau has complied with all relevant laws and regulations for its business throughout the year.

The Bureau reviews its key external service providers including Secretary, Investment managers, Consultant and Custodian and Auditors, Actuaries and Insurance broker on a regular basis and its relationship with them remained strong throughout the year.

The Bureau has in place an agreement with Member, Chevalier Insurance Company Limited for provision of a standby facility for assistance with the administration of claims which thankfully was not activated during the year.

The Council continues to work closely with and is supported by sister organisation, Motor Insurers' Bureau of Hong Kong via an at cost service agreement effective from 1 January 2018 as both Bureaus consider there is common ground and mutual benefit to be gained from closer liaison and being able to speak with one voice on matters of mutual future impact.

*A description of the principal risks and uncertainties facing the Bureau*

The 2018 Actuarial Review highlighted a number of Liquidity and Insurance risks which were noted by Council and considered in the following detailed risk review. A professional external risk review was conducted during 2019 resulting in the establishment of a formal Risk Register to be reviewed annually and establishing that the identified risks of the Bureau fall within the categories of Operational, Market, Credit, Liquidity and Insurance and such are currently all considered to pose no more than an insignificant risk level to the Bureau.

A detailed discussion on the main risks of the Bureau is set out in Management of insurance and financial risk, Note 3 on pages 15 to 17 to the Financial Statements which forms part of this Business Review.

**EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU**

**REPORT OF THE COUNCIL MEMBERS (CONTINUED)**

*A description of the principal risks and uncertainties facing the Bureau (continued)*

*Particulars of important events affecting the Bureau that have occurred since the end of the financial year*

The Council is not aware of any important events affecting the business of the Bureau that have occurred since the end of the financial year.

*An indication of likely future developments in the Bureau's business*

The Council continues to monitor with interest developments in respect of the Insurance Authority ("the IA") and the Policyholders' Protection Scheme which are not expected to have a material impact on the Bureau. Liaison continues with the IA.

**Financial statements**

The results of the Bureau for the year ended 31 December 2019 and the state of affairs of the Bureau as at that date are set out in the financial statements on pages 7 to 19.

**Retained surplus**

Movements in retained surplus during the year are set out in the statement of changes in equity on page 9.

**Council Members**

The Council Members during the financial year and up to the date of this report are:

| | |
|---|---|
| Mr Andrew Wong K.C. | |
| Mr Chan Pui Leung | |
| Mr Ng Wing Fat Ronnie | |
| Mr Jimmy Poon Wing Fai | |
| Mr Harry Wong Kwok Tim | (resigned on 8 August 2019) |
| Mr Hui Kam Kwai | |
| Ms Wong Chi Shun | |
| Mr Chen Zhao Nan | |
| Ms Fok Lai Chu | (resigned on 1 April 2020) |
| Ms Lee Kar Lun | (appointed on 2 April 2020) |

Ms Lee Kar Lun having been appointed to fill a casual vacancy during the year and up to the date of this report, retire at the forthcoming annual general meeting in accordance with article 35(2) of the Bureau's Articles of Association and, being eligible, offers herself for re-election.

Messrs. Andrew Wong K.C., Jimmy Poon Wing Fai and Chan Pui Leung are to retire at the forthcoming annual general meeting in accordance with article 35(3) of the Bureau's Articles of Association and, being eligible, offer themselves for re-election.

All other remaining Council Members continue in office.

**Council Member's interests in contracts**

No contract of significance to which the Bureau was a party and in which a Council Member of the Bureau had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

### Council Member's interests in contracts (continued)

At no time during the year was the Bureau a party to any arrangements to enable the Council Members of the Bureau to acquire benefits by means of the acquisition of shares in or debentures of any body corporate.

### Management contracts

No contracts concerning the management and administration of the whole or any substantial part of the business of the Bureau were entered into or existed during the year.

### Auditors

The financial statements have been audited by PricewaterhouseCoopers who retire, and being eligible, offer themselves for re-appointment.

By order of the Council

Ronnie Ng Wing Fat
Chairman

Hong Kong, 7 April 2020

# *Independent Auditor's Report*

To the Members of Employees Compensation Insurer Insolvency Bureau
(incorporated in Hong Kong with limited liability by guarantee)

## Opinion

*What we have audited*

The financial statements of Employees Compensation Insurer Insolvency Bureau (the "Bureau") set out on pages 7 to 19, which comprise:

- the statement of financial position as at 31 December 2019;
- the statement of 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 Bureau as at 31 December 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") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

## Basis for Opinion

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

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

*Independence*

We are independent of the Bureau 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.

# *Independent Auditor's Report*

To the Members of Employees Compensation Insurer Insolvency Bureau (Continued)
(incorporated in Hong Kong with limited liability by guarantee)

## Other Information

The Council Members are responsible for the other information. The other information comprises the information included in the report of the Council Members, 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 Council Members and Those Charged with Governance for the Financial Statements

The Council Members 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 the Hong Kong Companies Ordinance, and for such internal control as the Council Members 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 Council Members are responsible for assessing the Bureau'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 Council Members either intend to liquidate the Bureau or to cease operations, or have no realistic alternative but to do so.

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

## 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, in accordance with Section 405 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

# *Independent Auditor's Report*

To the Members of Employees Compensation Insurer Insolvency Bureau (Continued)
(incorporated in Hong Kong with limited liability by guarantee)

## Auditor's Responsibilities for the Audit of the Financial Statements (Continued)

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 Bureau's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Council Members.
- Conclude on the appropriateness of the Council Members' 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 Bureau'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 Bureau 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 those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers

**PricewaterhouseCoopers**
Certified Public Accountants

Hong Kong, 7 April 2020

**EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU**

**STATEMENT OF COMPREHENSIVE INCOME**
**FOR THE YEAR ENDED 31 DECEMBER 2019**

| | Note | 2019 HK$ | 2018 HK$ |
|---|---|---|---|
| Revenue | | | |
| Members' contributions | | 141,782,002 | 123,330,781 |
| | | 141,782,002 | 123,330,781 |
| Other income | | | |
| Net realised and unrealised gains / (loss) on financial assets | | 199,211,382 | (53,331,830) |
| Other investment income | | 5,908,259 | 5,724,262 |
| Interest income on deposits | | 6,192 | 1,103 |
| | | 205,125,833 | (47,606,465) |
| Total revenue and other income | | 346,907,835 | 75,724,316 |
| Less: Expenses | | | |
| Investment management fees | | 4,151,006 | 3,800,789 |
| Investment custody fees | | 1,117,080 | 1,118,111 |
| Accountancy, taxation and secretarial fees | | 1,089,000 | 908,500 |
| Legal and professional fees | | 1,225,207 | 498,300 |
| Insurance | | 273,609 | 216,386 |
| Audit fees | | 161,700 | 154,000 |
| Administration fees | | 780,000 | 760,000 |
| Others | | 53,622 | 85,871 |
| Total expenses | | 8,851,224 | 7,541,957 |
| Surplus for the year | | 338,056,611 | 68,182,359 |
| Other comprehensive surplus | | - | - |
| Total comprehensive surplus for the year | | 338,056,611 | 68,182,359 |

The notes on pages 11 to 19 are an integral part of these financial statements.

EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU

## STATEMENT OF FINANCIAL POSITION
## AS AT 31 DECEMBER 2019

| | Note | 2019 HK$ | 2018 HK$ |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Financial assets at fair value through profit or loss | 7 | 2,196,421,049 | 1,859,817,534 |
| Contributions and other receivables | 8 | 26,602,840 | 24,803,741 |
| Bank balances and cash | 9 | 1,389,351 | 563,367 |
| **Total assets** | | 2,224,413,240 | 1,885,184,642 |
| **EQUITY** | | | |
| Retained surplus | | 2,222,489,179 | 1,884,432,568 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Accrued expenses | | 1,924,061 | 752,074 |
| **Total liabilities** | | 1,924,061 | 752,074 |
| **Total equity and liabilities** | | 2,224,413,240 | 1,885,184,642 |

Approved and authorised for issue by the Council Members on 7 April 2020.

)
) Council Members
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The notes on pages 11 to 19 are an integral part of these financial statements.

**EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU**

**STATEMENT OF CHANGES IN EQUITY**
**FOR THE YEAR ENDED 31 DECEMBER 2019**

| | |
|---|---|
| Total retained surplus: | HK$ |
| Balance at 1 January 2018 | 1,816,250,209 |
| Total comprehensive surplus for the year | 68,182,359 |
| Balance at 31 December 2018 and 1 January 2019 | 1,884,432,568 |
| Total comprehensive surplus for the year | 338,056,611 |
| Balance at 31 December 2019 | 2,222,489,179 |

The notes on pages 11 to 19 are an integral part of these financial statements.

## EMPLOYEES COMPENSATION INSURER INSOLVENCY BUREAU

### STATEMENT OF CASH FLOWS
### FOR THE YEAR ENDED 31 DECEMBER 2019

| | Note | 2019<br>HK$ | 2018<br>HK$ |
|---|---|---|---|
| Operating activities | | | |
| Total comprehensive surplus for the year | | 338,056,611 | 68,182,359 |
| Adjustments for: | | | |
| - Investment expenses | | 5,268,086 | 4,918,900 |
| - Interest income on deposits | | (6,192) | (1,103) |
| - Other investment income | | (5,908,259) | (5,724,262) |
| - Net realised and unrealised (gains)/loss on financial assets | | (199,211,382) | 53,331,830 |
| Operating surplus before changes in working capital | | 138,198,864 | 120,707,724 |
| Increase in contributions and other receivables | | (1,799,100) | (350,316) |
| Increase in accrued expenses | | 1,171,988 | 140,542 |
| Net cash inflow from operating activities | | 137,571,752 | 120,497,950 |
| Investing activities | | | |
| Purchases of financial assets (net) | | (142,633,396) | (126,424,244) |
| Dividend and other investment income received | | 5,908,259 | 5,724,262 |
| Interest received on deposits | | 6,192 | 1,103 |
| Net cash outflow from investing activities | | (136,718,945) | (120,698,879) |
| Net increase/(decrease) in cash and cash equivalents | | 852,807 | (200,929) |
| Cash and cash equivalents at 1 January | | 564,425 | 765,354 |
| Cash and cash equivalents at 31 December | 9 | 1,417,232 | 564,425 |

The notes on pages 11 to 19 are an integral part of these financial statements.

## NOTES TO THE FINANCIAL STATEMENTS

### 1 Legal status

Employees Compensation Insurer Insolvency Bureau (the "Bureau") is a company limited by guarantee and was incorporated under the Hong Kong Companies Ordinance on 18 February 2003. The address of its registered office is Level 54, Hopewell Centre, 183 Queen's Road East, Hong Kong.

Under the provision of the Bureau's Articles of Association, every member shall, in the event of the Bureau being wound up, contribute such amount as may be required to meet the liabilities of the Bureau but not exceeding HK$100 per member. The assets of the Bureau shall be applied solely towards the promotion of the objects of the Bureau as set out in the Bureau's Articles of Association and no part thereof shall be distributed to the members of the Bureau. All insurers authorised by law to carry on employees' compensation insurance business in Hong Kong are required to become members of the Bureau.

The Bureau was set up by the insurance industry to give effect to an agreement entered into on 21 February 2003 between the Government of the Hong Kong Special Administrative Region (the "Government") and the Bureau (the "Insolvency Fund Agreement").

In accordance with the Insolvency Fund Agreement, the Government and the Bureau have agreed to establish the Employees Compensation Insurer Insolvency Scheme to assume responsibility for the liabilities of insurers engaging in employee compensation business that become insolvent on or after 1 April 2004.

### 2 Principal accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented.

### (a) Basis of preparation

The financial statements have been prepared in accordance with Hong Kong Financial Reporting Standard ("HKFRS") and requirements of the Hong Kong Companies Ordinance Cap. 622. They have been prepared under the historical cost convention as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bureau's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 4.

**Changes in accounting policies**

(i) New standards, amendments to standards and interpretations adopted by the Bureau

No standards, amendments and interpretations which are effective for the year beginning on 1 January 2019 are material to the Bureau.

## 2 Principal accounting policies (continued)

### (a) Basis of preparation (continued)

(ii) New standards, amendments to standards and interpretations not yet adopted by the Bureau

Certain new accounting standards, amendments to standards and interpretations have been published that are not mandatory for 31 December 2019 reporting periods and have not been early adopted by the Bureau.

HKFRS 17, 'Insurance Contracts' will replace the current HKFRS 4 'Insurance Contracts'. HKFRS 17 includes some fundamental differences to current accounting in both insurance contract measurement and profit recognition. The general model is based on a discounted cash flow model with a risk adjustment and deferral of unearned profits. An optional, simplified premium allocation approach is permitted for the liability for the remaining coverage for short duration contracts. Additionally, HKFRS 17 requires more granular information and a new presentation format for the statement of comprehensive income as well as extensive disclosures. The standard is effective for accounting periods beginning on or after 1 January 2021. Early adoption is permitted. The Bureau is currently undertaking a review to assess the impact of HKFRS 17.

There are no other HKFRSs, amendments to HKFRSs or HK (IFRIC) interpretations that are not yet effective that would be expected to have a material impact on the Bureau.

### (b) Revenue recognition

(i) Members' contributions

Members' contributions received and receivable are recognised based on gross employees' compensation insurance premiums received and receivable by members from their policyholders.

(ii) Other investment income and interest income on deposits

Other investment income is recognised when the right to receive rebate of investment management expense from the investment manager. Interest income from bank deposits and debt securities is accrued on a time-apportioned basis on the principal outstanding and at the rates applicable.

### (c) Insurance contracts

Insurance contracts are those contracts that transfer significant insurance risk. As a general guideline, the Bureau defines as significant insurance risk the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefits payable if the insured event did not occur. The Bureau believes that the facilities described in Note 1 above meet the definition of insurance contracts.

Claims are charged to income as incurred based on the estimated liability for compensation owed to policyholders. They include claims settlement costs arising from events that have occurred up to the financial reporting date even if they have not yet been reported to the Bureau. The Bureau does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are estimated using the input of assessments for individual cases reported to the Bureau and statistical analyses for the claims incurred but not reported.

**2 Principal accounting policies (continued)**

**(d) Financial assets**

*Classification*

The Bureau 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 Bureau classifies its investments based on both the Bureau's business model for managing those financial assets and the contractual cash flow characteristics of the financial assets. The financial assets at fair value through profit or loss are managed and performance is evaluated on a fair value basis. The Bureau is primarily focused on fair value information and uses that information to assess the assets' performance and to make decisions. Consequently, all investments are measured at fair value through profit or loss.

*Recognition and derecognition*

Regular way purchases and sales of financial assets are recognized on trade-date – the date on which the Bureau commits to purchase or sell the asset. Financial assets are derecognized when the right to receive cash flows from the financial assets have expired or have been transferred and the Bureau has transferred substantially all risks and rewards of ownership.

*Measurement*

At initial recognition, the Bureau measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at fair value through profit and loss are expensed in the statement of comprehensive income.

Subsequent to initial recognition, all financial assets at fair value through profit or loss are measured at fair value. Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are presented in the statement of comprehensive income within net realised and unrealised (loss)/gains on financial assets in the period in which they arise.

Dividend income from financial assets at fair value through profit or loss is recognised in the statement of comprehensive income when the Bureau's right to receive payments is established.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Contribution and other receivables mainly consists of members' contribution receivables. They are generally due for settlement within one month and therefore are all classified as current.

Members' contribution receivables are recognised initially at the amount of consideration that is unconditional. The Bureau holds the members' contribution receivables with the objective to collect the contractual cash flows and therefore measures them subsequently at amortised cost using the effective interest method.

## 2 Principal accounting policies (continued)

### (d) Financial assets (continued)

*Impairment*

For Members' contribution receivables, the Bureau applies the simplified approach permitted by HKFRS 9, which requires expected lifetime losses to be recognised from initial recognition of the receivables.

*Fair value*

The fair values of quoted investments are based on current bid prices.

Regular way purchases and sales of investments were recognized on trade-date – the date on which the Bureau commits to purchase or sell the asset. Financial assets carried at fair value through profit or loss were initially recognized at fair value and transaction costs were expensed in the statement of comprehensive income. Financial assets were derecognized when the right to receive cash flows from the investments had expired or had been transferred and the Bureau had transferred substantially all risks and rewards of ownership.

Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category were presented in the statement of comprehensive income in the period in which they arise. Dividend income from financial assets at fair value through profit or loss was recognised in the statement of comprehensive income when the Bureau's right to receive payments was established.

The fair values of quoted investments were based on current bid prices.

### (e) Translation of foreign currencies

The financial statements are presented in Hong Kong dollars, which is the Bureau's functional currency and presentation currency.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income.

### (f) Cash and cash equivalents

In the statement of cash flows, cash and cash equivalents includes cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less and bank overdrafts.

## 3 Management of Insurance and financial risk

### 3.1.1 Financial risk factors

The Bureau is exposed to financial risk through its financial assets. In particular, the key financial risk is from unanticipated volatility of return and other financial market driven events that can change the risk profile of the funds. The most important components of this financial risk are interest rate risk, credit risk, currency risk and price risk.

#### (a) Interest rate risk

The investment portfolio of the Bureau as at 31 December 2019 comprises funds which holds bonds of approximately HK$1,547 million (2018: HK$1,338 million). Interest rate movements can have a material impact on the carrying values of these bond funds.

By investing in the bond funds managed by the investment managers, the Bureau manages its interest rate risk by allowing the investment managers to use certain derivatives to hedge the interest rate risk exposure associated with underlying debt securities of the bond funds where appropriate. The Bureau did not have any derivative transactions in 2019 and 2018.

#### (b) Credit risk

The Bureau has exposures to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. This includes indirect credit risk with respect to investments in funds that holds bonds of HK$1,547 million (2018: HK$1,338 million). The Bureau is also exposed to counterparty credit risk on Bank balances and cash and Contributions and other receivables.

The investment guidelines have been updated since late 2019.

Prior to the updates, the investment guidelines stipulate that no more than 5% of the investment portfolio is held in any one security or with one single issuer, other than a fund or a security representing a collective investment of other securities. In addition, no more than 10% of the investment portfolio is invested in the obligations of a single issuer except for sovereign or supranational borrowers with an AAA rating by Standard & Poor's or equivalent. There are no restrictions on investing in government bonds issued by the United States, Japan, the Republic of Germany, the United Kingdom, Canada, the Republic of France, the Republic of Italy, the Kingdom of Spain and the Netherlands. Investments in bond securities should have a minimum rating of B- as measured by Standard & Poor's or equivalent. The total allocation to BB rated bonds and below as measured by Standard & Poor's or equivalent of the Portfolio cannot exceed 10% of the overall portfolio. Short term investments are maintained at a rating of A1 or above as measured by Standard & Poor's or P1 as measured by Moody's. The above does not apply to Mortgage-Backed Securities.

After the updates since late 2019, the investment guidelines now stipulate that no more than 5% of the Fund is to be held in any one security, other than a fund or a security representing a collective investment of other securities, unless the security represents an OECD sovereign borrower or issuer (and its agencies).

## 3 Management of Insurance and financial risk (continued)

### 3.1.1 Financial risk factors (continued)

#### (b) Credit risk (continued)

The Bureau manages its credit risk through collective investment vehicles that invest in a diversified portfolio of bond instruments. All credit risk are assumed indirectly through exposure to these vehicles.

As of 31 December 2019, indirect credit risks of the Bureau's Fixed Income Portfolio were diversified across various countries and sectors, with highest exposure to the United States, Japan and Italy. The percentage contributions of duration by these issuers accounted for 59.4% of the Fixed Income Portfolio. Elsewhere, the Bureau's exposure was the highest to France and the United Kingdom, which respectively accounted for 5.3% and 5.2% of the Fixed Income Portfolio.

The above statistics compare to that as of 31 December 2018, when the Bureau's Fixed Income Portfolio was most exposed to bonds issued by the United States, European Monetary Union (EMU) and Germany, which accounted for 79.4% of the portfolio, followed by Japan and Canada, which respectively accounted for 8.2% and 4.5% of the portfolio.

The Bureau measures credit risk and expected credit losses using probability of default, exposure at default and loss given default. Management considers both historical analysis and forward looking information in determining any expected credit loss. The Bureau considers the probability of default to be close to zero as the counterparties of Bank balances and cash and Contributions and other receivables have a strong capacity to meet their contractual obligations in the near term. As a result, no loss allowance has been recognised based on expected credit losses as any such impairment would be wholly insignificant to the Bureau.

The Bureau has no significant concentration of credit risk.

#### (c) Price risk

The Bureau is directly exposed to price risk related to funds and indirectly to the equity securities that the funds invest in. A 10% increase in the market values of the funds would result in a gain of approximately HK$220 million in 2019 (2018: HK$186 million).

#### (d) Currency risk

The Bureau's exposures to foreign exchange risk arise primarily from purchased financial assets that are denominated in currencies other than Hong Kong dollars. As at 31 December 2019, the Bureau did not have significant exposures to foreign exchange risk, as all the financial assets held by the Bureau were either denominated in Hong Kong dollars or US dollars (against which Hong Kong dollars are pegged).

## 3 Management of Insurance and financial risk (continued)

### 3.1.2 Fair value estimation

HKFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and unit trusts.
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).
- Level 3 - inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The following tables present the Bureau's assets that are measured at fair value.

As at 31 December 2019:

| | Level 1 HK$ | Level 2 HK$ | Level 3 HK$ | Total balance HK$ |
|---|---|---|---|---|
| Financial assets (Note 7) | 2,196,421,049 | - | - | 2,196,421,049 |
| **Total assets** | 2,196,421,049 | - | - | 2,196,421,049 |

As at 31 December 2018:

| | Level 1 HK$ | Level 2 HK$ | Level 3 HK$ | Total balance HK$ |
|---|---|---|---|---|
| Financial assets (Note 7) | 1,859,817,534 | - | - | 1,859,817,534 |
| **Total assets** | 1,859,817,534 | - | - | 1,859,817,534 |

### 3.2 Insurance risk and capital risk management

Capital comprises all components of equity as shown in the statement of financial position. The principal insurance and capital risk that the Bureau faces is that the assets of the Bureau are not adequate to discharge its obligations under the terms of the fund agreement. This may arise if the actual claims exceed the carrying amount of the assets available.

## 4 Critical accounting estimates and judgements

Management of the Bureau is not aware of any significant areas where critical judgments are involved in applying the Bureau's accounting policies for the years ended 31 December 2019 and 2018.

## 5 Remuneration of Council Members of the Bureau

In accordance with the Bureau's Articles of Association, the Council Members of the Bureau are not entitled to any remuneration or compensation for services rendered to the Bureau. Accordingly, none of the Council Members of the Bureau received or was due any remuneration during the year.

## 6 Taxation

The Bureau is exempt under Section 87 of the Hong Kong Inland Revenue Ordinance from payment of any tax chargeable under the Ordinance.

## 7 Financial assets at fair value through profit or loss

| | 2019<br>HK$ | 2018<br>HK$ |
|---|---|---|
| Mutual funds registered in Hong Kong containing | | |
| - Listed bonds | 248,626,175 | 395,400,813 |
| - Listed equities | 584,316,388 | 398,153,023 |
| - Cash deposits | 64,624,854 | 123,849,443 |
| Bond funds registered outside Hong Kong | | |
| - Listed bonds | 1,298,825,751 | 942,413,197 |
| Cash deposits with custodian (Note 9) | 27,881 | 1,058 |
| | 2,196,421,049 | 1,859,817,534 |

The Bureau had investments in the following investment funds. These investment funds manage assets on behalf of third party investors. These funds are financed through the issue of units/shares to investors.

| | Fair value | |
|---|---|---|
| | 2019<br>HK$ | 2018<br>HK$ |
| Investment Funds, at market value: | | |
| Schroder Stable Growth Fund | 330,779,113 | 455,997,975 |
| Schroder Balanced Investment Fund | 566,788,304 | - |
| Schroder Capital Stable Fund | - | 461,405,304 |
| PIMCO Global Bond Fund | 866,854,205 | 942,413,197 |
| JPM Aggregate Bond Fund | 431,971,546 | - |
| | 2,196,393,168 | 1,859,816,476 |

The above investments at 31 December 2019 were classified as financial assets at fair value through profit and loss.

These investments include 9,948,244 units of Schroder Stable Growth Fund (2018: 15,573,701 units), nil units of Schroder Capital Stable Fund (2018: 18,703,093 units), 8,906,164 units of Schroder Balanced Investment Fund (2018: nil), 3,302,230 units of PIMCO Global Bond Fund (2018: 3,875,379 units) and 428,632 units of JPM Aggregate Bond Fund (2018: nil).

## 7 Financial assets at fair value through profit or loss (continued)

The maximum exposure to loss is HK$2,196,393,168 which represents the fair value of the investments in investment funds.

The size of the Schroder Stable Growth Funds during 2019 ranges from HK$7,769 million to HK$8,319 million, the size of the Schroder Balanced Investment Fund ranges from HK$6,933 million to HK$8,929 million, the size of the PIMCO Global Bond Funds ranges from US$11,155 million to US$14,904 million and the size of the JPM Aggregate Bond Funds ranges from US$2,817 million to US$3,066 million. During the year, the Bureau did not provide financial support to unconsolidated structured entities and has no intention of providing financial or other support.

## 8 Contributions and other receivables

These are measured at amortised cost. The fair values of the receivables are estimated to be approximately equal to the carrying amounts of these balances.

There is no concentration of credit risk with respect to these receivables. There is no loss allowance recognised as at 31 December 2019 (2018: nil).

## 9 Cash and cash equivalents

| | 2019<br>HK$ | 2018<br>HK$ |
|---|---|---|
| Bank balances and cash | 1,389,351 | 563,367 |
| Cash deposits with maturity less than three months | 27,881 | 1,058 |
| Cash and cash equivalents | 1,417,232 | 564,425 |

These are measured at amortised cost.

## 10 Events after the balance sheet date

After the outbreak of Coronavirus Disease 2019 ("COVID-19 outbreak") in early 2020, a series of precautionary and control measures have been and continued to be implemented in Hong Kong and also in other jurisdictions.

The COVID-19 has certain impacts on the overall economy, the extent of which will depend on the situation of the epidemic preventive measures, the duration of the epidemic and the implementation of regulatory policies. The COVID-19 has affected the performances of certain investment assets held by the Bureau.

The Bureau will continue to monitor the situation of the COVID-19 and the corresponding impacts to the Bureau, and continue to assess and respond to its impacts on the financial position and operating results of the Bureau.

## 11 Approval of financial statements

The financial statements were approved by the Council on 7 April 2020.