

### HISTORY AND DEVELOPMENT

Emperor Securities and Emperor Futures have become associated companies of EIHL since September 1993 and September 1994 respectively, and both have subsequently become its wholly owned subsidiaries since May 1996, where they have served as the financial brokerage arm of the Emperor Group. Starting from only providing securities brokerage service, the Group has now extended its services to cover a full range of financial products traded on the Stock Exchange and the Futures Exchange as well as commodities and financial futures traded on exchanges in the US and Japan. The Group also provides credit facilities to its clients.

Emperor Securities was incorporated in July 1990 under the name of Fundway Finance Limited and through a series of changes of company name, it is currently registered under the name of Emperor Securities Limited. Emperor Securities was owned as to approximately 99.99% and the remaining 0.01% by Mr. Leung Cho Lam and Ms. Leung Au Wing Yee respectively upon its establishment, both were Independent Third Parties. In September 1993, the entire interest of Emperor Securities was sold to wholly owned subsidiaries of Hong Kong Daily News Holdings Limited (“HKDN” and now known as Graneagle Holdings Limited), a company listed on the Stock Exchange. By virtue of the fact that the Emperor Group was the then largest shareholder interested in approximately 35% of HKDN, Emperor Securities became an associated company of the Emperor Group. The Emperor Group increased its shareholding interest in HKDN to approximately 61% in November 1994 making Emperor Securities a subsidiary. Through subsequent corporate restructuring, Emperor Securities became a wholly owned subsidiary of the Emperor Group since May 1996.

Emperor Securities became a dealer registered under the then Securities Ordinance since January 1991. Holding one “A” share of the Stock Exchange conferred upon Emperor Securities one seat in the Stock Exchange and enables it to provide securities brokerage service to its clients. In order to enhance the trading capability to cope with the expanding business and clientele, Emperor Securities acquired one more “A” share of the Stock Exchange in December 1993. With the strong belief that in long term, the Hong Kong stock market will continue to play an important role as a financial and fund raising center for the Greater China region, Emperor Securities continued to strengthen its trading capacity and further acquired another five “A” shares of the Stock Exchange in 1994, increasing its trading seats in the Stock Exchange to seven. Upon the merger of the Stock Exchange and the Futures Exchange on 6 March 2000 (the “Merger”), these trading seats turned into trading rights on the Stock Exchange and Emperor Securities became a participant with a right to conduct trading of securities on the Stock Exchange. The dealing capacity of a Stock Exchange Participant was used to be determined by the number of Stock Exchange Trading Rights held by it. The recent relaxation of such restriction allows Stock Exchange Participants to increase their dealing capacity by payment of a fee to the Stock Exchange. Such relaxation, together with the advancement of the trading and dealing systems and equipments of the Group, allows Emperor Securities to gear up its capacities to meet the growing needs of its clients with fewer Stock Exchange Trading Rights. As such, Emperor Securities sold three of its Stock Exchange Trading Rights to three separate Independent Third Parties at an aggregate consideration of approximately HK\$1.5 million in 2005. Following the sale of those Stock Exchange Trading Rights, Emperor Securities retains four Stock Exchange Trading Rights.

Emperor Securities started its business by providing securities brokerage service to its clients without offering any share margin financing. Emperor Finance Limited (“Emperor Finance”), a subsidiary of EIHL, used to provide share margin financing services to Emperor Securities’ clients. In order to

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streamline the two related businesses, Emperor Securities had taken over the share margin financing business from Emperor Finance in June 2000. On 12 June 2000, Emperor Securities acquired from Emperor Finance its active margin financing portfolio at a consideration of approximately HK\$98 million which was determined on the basis of Emperor Finance's net book value of the relevant assets and liabilities associated with the margin financing portfolio being transferred as at the date of transfer. In addition to providing share margin financing to its clients for on-market share purchases, Emperor Securities also extends to clients credit facilities which are secured by stocks listed on the Stock Exchange.

To further broaden its scope of services, Emperor Securities became registered as an Options Trading Exchange Participant with the Stock Exchange in September 1995 and was allowed to provide brokerage services for stock options traded on the Stock Exchange. Emperor Securities also participated in various fund raising exercises by acting as underwriter/placing agent of initial public offerings, rights issues, private placing of securities carried out by companies listed/to be listed on the Stock Exchange.

Emperor Futures was incorporated in May 1989 under the name of See Yield Investments Limited and through a series of changes of company name, it is currently registered under the name of Emperor Futures Limited. Emperor Futures was, upon its establishment, owned as to 50% by each of Mr. Ho Kun Shing, Michael and Ms. Yu Sin Yee, Tina who were both Independent Third Parties. In September 1994, the entire interest of Emperor Futures was sold to wholly owned subsidiaries of HKDN. By virtue of the fact that the Emperor Group was then the largest shareholder interested in approximately 35% of HKDN, Emperor Futures became an associated company of the Emperor Group. The Emperor Group increased its shareholding interest in HKDN to approximately 61% in November 1994 making Emperor Futures a subsidiary. Through subsequent corporate restructuring, Emperor Futures became a wholly owned subsidiary of the Emperor Group since May 1996. Emperor Futures held one standard share and one ordinary share in the Futures Exchange which conferred upon Emperor Futures two trading seats at the Futures Exchange. Emperor Futures became a participant of the Futures Exchange with two trading rights upon the Merger.

Emperor Futures was previously a dealer registered under the then Commodities Trading Ordinance and is now a licensed corporation under the SFO. Emperor Futures provides brokerage services covering financial futures and options products. In December 2004, Emperor Futures extended its brokerage services to overseas markets covering commodities and financial futures traded on exchanges in the US and Japan.

Emperor Gold & Silver was incorporated in March 1994 and has a membership with The Chinese Gold & Silver Exchange Society (the "Gold & Silver Exchange") since November 1995. The Gold & Silver Exchange operates in Hong Kong as a registered society and provides a gold market in which its members or investors (through the members) can trade. The Gold & Silver Exchange currently has 171 members. A member shall be in the form of sole proprietorship, partnership or company limited by shares set up in Hong Kong and have minimum paid up capital and net asset value of HK\$5,000,000. The Group gathers information, in particular in the gold market sector, from the Gold & Silver Exchange through Emperor Gold & Silver to serve its sales and research teams as well as the clients of the Group. Other than holding of the membership with the Gold & Silver Exchange, Emperor Gold & Silver has not carried out any business during the Track Record Period.

Emperor Securities Nominees was incorporated in August 1996 for the purpose of providing nominee services to Emperor Securities and its clients.

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Famous Winner was incorporated in September 1999 and since January 2004 holds branch office tenancies for the Group. It now holds the tenancy for the Group's branch office at Sai Ying Poon.

The Group was unable to agree with the landlord on the rental and decided to close down its branch in Mei Foo in April 2005. After the closing down of Mei Foo branch, the Group currently has two branches located at Tsuen Wan and Sai Ying Poon with its head office at Emperor Group Centre in Wanchai.

The Group has built up an extensive and diversified client base. As at 31 December 2006, the Group had 16,781 securities clients of which 9,783 are cash clients and 6,998 are margin clients. At the same time, the Group had 2,060 futures clients.

As at 31 December 2006, the Group had 48 full time employees, 2 part-time employees and 51 account executives of whom 19 are engaged in both securities and futures brokerage services, 17 are engaged in securities brokerage services only and 15 are engaged in futures brokerage services only.

On 2 April 2007, in preparation for the listing of the Shares on the Stock Exchange, the Group underwent a corporate reorganisation whereby the Company became the ultimate holding company of all companies comprising the Group. Details of the corporate reorganisation are set out in the paragraph headed "Reorganisation" in appendix V to this prospectus.

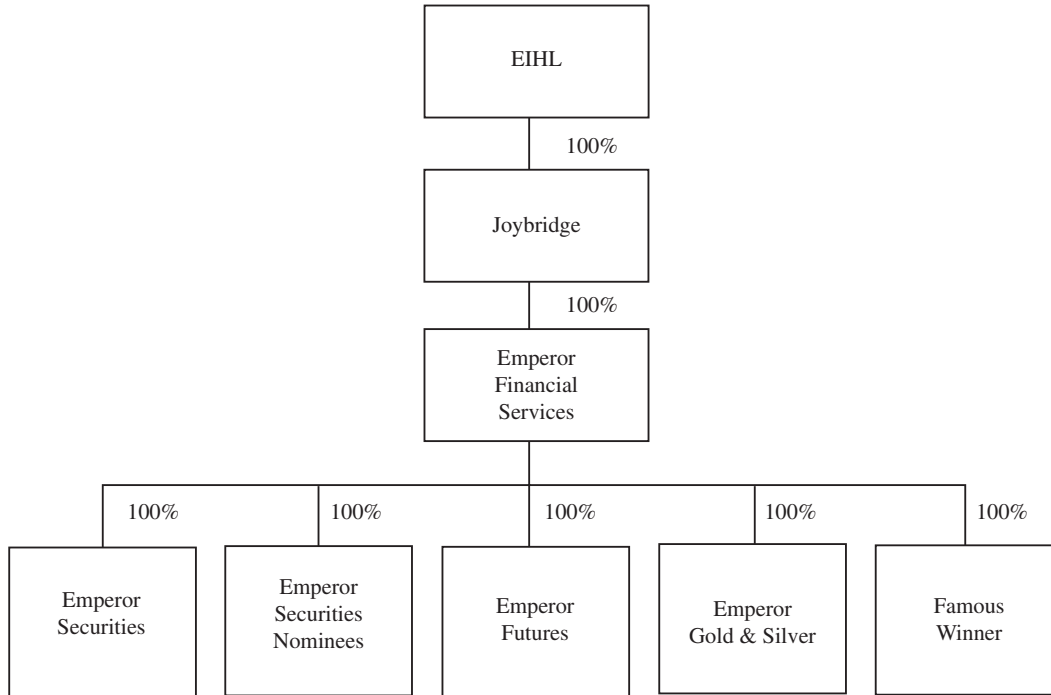
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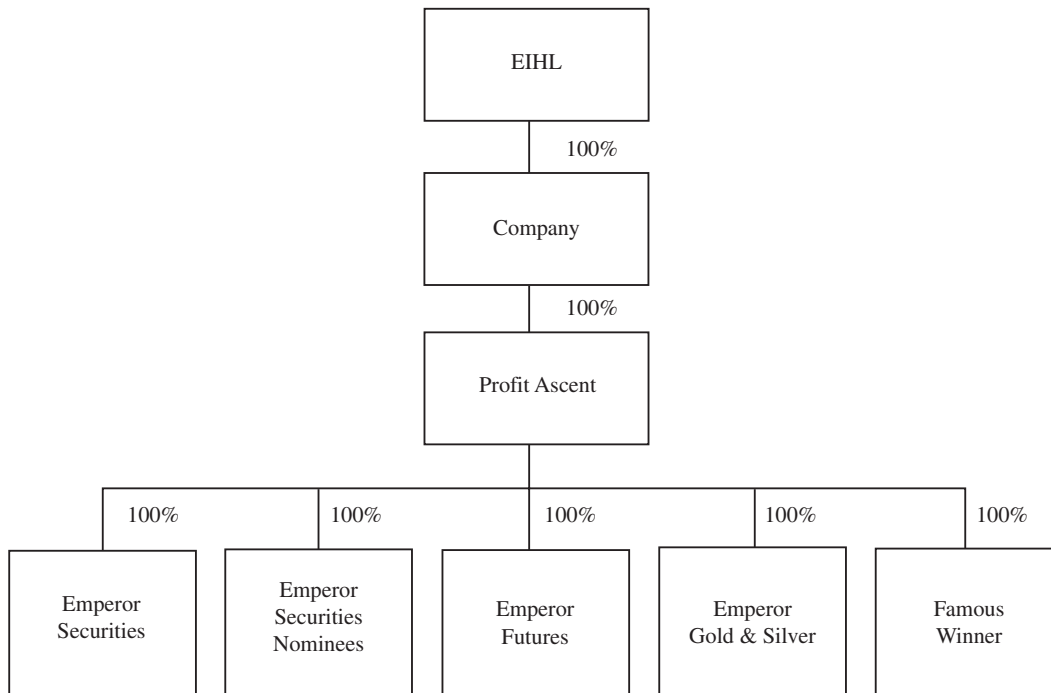
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### REORGANISATION

Set out below is the group structure immediately prior to the Reorganisation:



Set out below is the shareholding and all the subsidiaries of the Group as at the Latest Practicable Date (which is after completion of the Reorganisation but prior to completion of the EIHL Distribution and the Share Offer) :



### **EIHL Distribution**

The Emperor Group is principally engaged in property investment and development and hotel operations. In addition, the Emperor Group is and will, until completion of the EIHL Distribution, be engaged in provision of securities brokerage and financial services through the Group.

As at the Latest Practicable Date, EIHL held 282,635,636 Shares, representing 100% of the issued share capital of the Company. Shares of EIHL are listed on the Stock Exchange. EIHL has strived to restructure its business portfolio to focus primarily on property investment and development as well as hotel operations. On 5 March 2007, the shareholders of EIHL approved the proposal for the spin-off (the “Proposed Spin-off”) of the Group from EIHL. The Proposed Spin-off is still subject to fulfillment of the following outstanding conditions:

- (i) the Listing Committee granting approval for the Proposed Spin-off and the listing of, and permission to deal in, the Shares in issue and to be issued pursuant to the Share Offer and compliance with the stock admission requirements of HKSCC; and
- (ii) the obligations of the Underwriters under the Underwriting Agreement becoming unconditional (including, if relevant, as a result of the waiver of any condition(s) by or on behalf of the Underwriters) and the Underwriting Agreement not being terminated in accordance with their terms or otherwise, on or before the dates and times to be specified therein.

As part of the Proposed Spin-off, a special interim dividend in the form of the EIHL Distribution will be made to shareholders of EIHL. The EIHL Distribution will be satisfied wholly by a distribution in specie to the Qualifying EIHL Shareholders of all the Shares held by EIHL. The EIHL Distribution would be made on the basis that Qualifying EIHL Shareholders would receive one (1) Share for every five (5) EIHL Shares held by them as at the Record Date. The Qualifying EIHL Shareholders (including Charron, being the controlling shareholder of EIHL) would receive such number of Shares pro rata to their respective shareholdings in EIHL. The EIHL Distribution will not be made to the shareholders of EIHL whose addresses recorded on the register of members of EIHL as at the Record Date are outside Hong Kong and to whom the directors of EIHL, after making enquiry and on account either of legal restrictions under the laws of relevant place or the requirements of the relevant regulatory body or stock exchange in that place, consider it necessary or expedient not to distribute the Shares. Any undistributed Shares will be retained by EIHL for sale in the market after commencement of dealing in the Shares on the Stock Exchange for the benefit of the relevant Non-qualifying EIHL Shareholders. Fractional entitlements to the Shares under the EIHL Distribution will be retained by EIHL for sale in the market and EIHL will keep the net proceeds of sale, after deduction of related expenses therefrom, for the benefit of EIHL. The EIHL Distribution is still subject to the listing of Shares becoming unconditional. It is scheduled that definitive certificates for the Shares will be despatched to the Qualifying EIHL Shareholders on 23 April 2007. The controlling shareholder of EIHL, Charron, will receive its pro rata share of the EIHL Distribution and immediately thereafter, will become the controlling Shareholder (assuming that Charron takes up its Assured Entitlement under the Preferential Offer in full).

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### **Preferential Offer**

Apart from the EIHL Distribution, the Qualifying EIHL Shareholders are also invited to subscribe for the Reserved Shares on an assured basis of one (1) Reserved Share for every five (5) EIHL Shares held by them as at the Record Date. Details of the terms and conditions of the Preferential Offer are set out in the section headed “Structure of the Share Offer – Preferential Offer” of this prospectus.

### **Reasons and benefits of the Proposed Spin-off**

The Directors and the directors of EIHL consider that the listing of the Shares and the EIHL Distribution will be beneficial to both the Group and the Emperor Group in the following areas:

- (1) the listing of the Shares will enable the Group, as a separate listed group, to directly raise funds in the capital market to fund its current operations and future business development;
- (2) the listing of the Shares will increase the transparency of business performance of the Group and provides the market with more detailed and timely information of the Group;
- (3) the listing of the Shares will allow the Company to establish its own shareholder base;
- (4) the listing of the Shares will enable EIHL to unlock the value of its investment in the Group; and
- (5) the listing of the Shares will enable future funds raised by EIHL to be focused on the development of the remaining business of the Emperor Group.

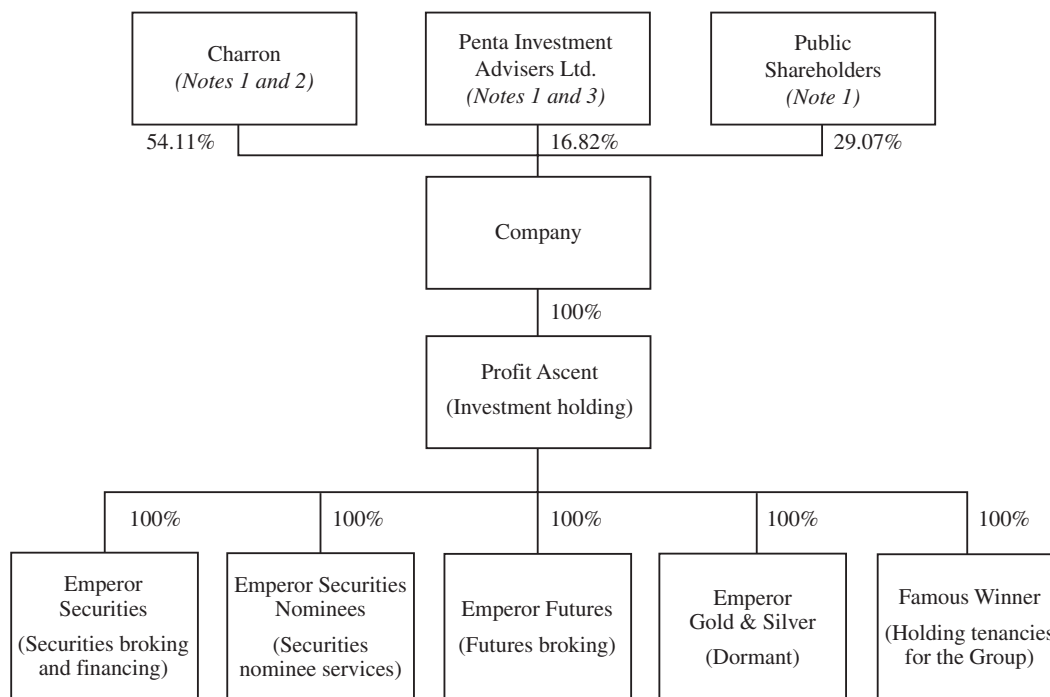
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### CORPORATE STRUCTURE

The shareholding structure of the Company (calculated based on the shareholding of EIHL as at the Record Date) following the Share Offer and the EIHL Distribution is illustrated diagrammatically as follows:



*Notes:*

- (1) Assuming that all the Qualifying EIHL Shareholders have taken up their entitlements under the Preferential Offer.
- (2) The entire issued share capital of Charron is held by Jumbo Wealth Limited ("Jumbo Wealth") in trust for The A&A Unit Trust, a unit trust under The Albert Yeung Discretionary Trust (the "Trust"). The Trust is a discretionary trust set up by Mr. Albert Yeung. By virtue of the SFO, Mr. Albert Yeung, as the settlor of the Trust, is deemed to be interested in the Shares. By virtue of the aforesaid interest of Mr. Albert Yeung, Ms. Luk Siu Man, Semon (spouse of Mr. Albert Yeung) is also deemed to be interested in the Shares.
- (3) By virtue of the SFO, Mr. John Zwaanstra is deemed to be interested in the shares held by Penta Investment Advisers Ltd.

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### BUSINESS ACTIVITIES

The Group provides a wide range of financial services in Hong Kong, including brokerage services for securities, futures and options traded on the exchanges in Hong Kong, the US and Japan. The Group also provides margin and initial public offer financings as well as loans and advances to its clients in Hong Kong.

#### Stockbroking

The Group's stockbroking business is carried out by Emperor Securities which is a licensed corporation under the SFC to carry on type 1 (dealing in securities) and type 4 (advising on securities) regulated activities. Emperor Securities is a Stock Exchange Participant and is currently holding four Stock Exchange Trading Rights.

The Group executes trades on behalf of its clients in securities listed and traded on the Stock Exchange and provides other related services including equity research, application for new issues and other nominee services such as collection of cash and scrip dividends.

In addition, the Group also participates in the underwriting and placing of securities listed or to be listed by way of initial public offering, rights issue or private placings carried out by issuers listed or to be listed on the Stock Exchange. For each of the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, placing and underwriting commission income accounted for approximately 5.20%, 10.41%, 5.47%, 7.06% and 4.25% respectively of the Group's total turnover.

To complement and support the Group's stockbroking business, Emperor Securities provides research services to its clients. The Group's research team compiles daily reports with commentaries on major financial news and analysis on certain listed companies. The research team may from time to time publish separate company research reports after company visits. The Group's research team has also published its market commentaries in the press and has attended interviews in television financial programs.

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, commission and fee income from stockbroking business accounted for approximately 45.23%, 46.05%, 34.00%, 34.45% and 32.76% respectively of the Group's total turnover.

Each account executive of the Group is responsible for a portfolio of clients whom they serve personally while clients originated by the Group are served by members of the house team. As at 31 December 2006, the Group had about 3,692 active securities clients whose accounts have recorded purchase and/or sale of securities transactions in the past twelve months. These active securities clients include 2,995 cash clients and 697 margin clients, approximately 98.62% of which are retail investors and the remaining 1.38% are corporate clients.

The Group's largest stockbroking client contributed approximately 7.70%, 18.95%, 10.77% and 8.87% respectively of the Group's stockbroking commission income for each of the three years ended 31 March 2006 and the nine months ended 31 December 2006. For the same year/period, the Group's five largest stockbroking clients in aggregate accounted for approximately 30.08%, 34.61%, 33.03% and 26.57% respectively of the Group's stockbroking commission income.



### **Futures and options brokerage**

The Group's futures and options brokerage service is principally provided by Emperor Futures which is a licensed corporation under the SFC to carry on type 2 (dealing in futures contracts) and type 5 (advising on futures contracts) regulated activities. Emperor Futures is a Futures Exchange Participant holding two Futures Exchange Trading Rights. Emperor Futures is also a clearing participant of the HKCC.

Emperor Futures used to provide brokerage services for futures and options traded on the Futures Exchange only, such as HSI futures and mini-HSI futures. In December 2004, Emperor Futures extended its brokerage services to derivative products including commodities and currency futures traded on exchanges in the US and commodities futures traded on exchanges in Japan. The Group maintained trading accounts with independent broking houses (the "Overseas Brokers") which provide brokerage services in respect of these financial and commodities products in the US and Japan. Upon receipt of client orders for products traded in the US and Japan markets, the Group will then place these orders with the relevant Overseas Brokers for their execution on the relevant US and Japan exchanges. As at 31 December 2006, the Group had about 369 active futures clients whose accounts have recorded open and/or close position of future contracts transactions in the past twelve months. These active futures clients comprise approximately 98.37% of retail investors and approximately 1.63% of corporate clients.

Moreover, clients who would like to trade stock options on the Stock Exchange can also place their orders with Emperor Securities which is an Option Trading Exchange Participant of the Stock Exchange.

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, commission income from futures and options broking contributed approximately 6.32%, 3.86%, 13.55%, 13.38% and 22.63% respectively of the Group's total turnover. The substantial increases in commission income from futures and options brokerage in the year ended 31 March 2006 and the nine months ended 31 December 2005 and 2006 were mainly attributable to the substantial increases in turnover of the Group's commodities futures and options trading business in Japan and US in that year/period.

The Group's largest futures and options trading client contributed approximately 37.48%, 30.24%, 11.77% and 32.25% respectively of the Group's futures and options trading commission income for each of the three years ended 31 March 2006 and nine months ended 31 December 2006. For the same year/period, the Group's five largest futures and options trading clients in aggregate accounted for approximately 57.35%, 56.57%, 33.44% and 64.39% respectively of the Group's futures and options trading commission income.

### **Financing**

Emperor Securities offers credit facilities to its clients who wish to purchase securities on a margin basis. Share margin financing offers funding flexibility to the Group's clients by assisting them to leverage their investments. All share margin financing extended to the Group's clients is secured by securities listed on the Stock Exchange and pledged to the Group. As a guideline, the Group lends between 30% and 70% of the value of the HSI constituent stocks and not more than 60% of the value of selected non-HSI constituent stocks depending on the liquidity and market capitalisation of the individual

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stock. It is the Group's policy not to provide margin financing for warrants. The list of the approved securities for which the Group will extend margin financing is approved by the management of the Group based on the regular review and recommendation from the research team of the Group. The Group also provides financing for applications for shares in connection with initial public offerings. The Group will exercise caution in granting margin financing to clients, ensure its risk management policies are followed, conduct regular reviews and assessments on each margin loan granted and comply with the relevant regulations of the governing bodies. Details of the Group's risk management policies with respect to margin financing can be found in the paragraphs headed "Credit risk" and "Market risk" under the subsection headed "Current internal control systems" of this section.

The Group has adopted the following credit control policies and procedures to consider if any impairment allowance for bad and doubtful debts has to be made:

*Comparing underlying asset values with secured margin loans as well as loans and advances and checking whether T+2 settlement basis for cash client receivables is consistently applied*

For secured margin loans as well as loans and advances:

Identify (i) those margin loans as well as loans and advances with aggregate underlying asset values falling below the outstanding amounts due to Emperor Securities and (ii) those loans and advances which are not properly settled in accordance with the terms of the loan agreements.

For cash client receivables:

Identify those receivables which are not properly settled on T+2 settlement basis.

*Subsequent settlements and repayments*

Under the Group's credit policy, calls will be made by the handling account executives and the clients will have to (a) keep the outstanding amounts at a level allowed under the Group's credit policy (for secured margin loans) and (b) settle the overdue amounts (for loans and advances and cash client receivables).

For secured margin loans:

If the secured margin loan clients fail to make good margin calls and the aggregate underlying assets are prolongly below the outstanding amounts, the information of such loans will be referred to the management of Emperor Securities who shall consider taking appropriate follow-up action.

For loans and advances:

If the term loan clients fail to settle the overdue balances in accordance with the terms of the loan agreements, the information of such loans will be referred to the management of Emperor Securities who shall consider taking appropriate follow-up action.

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For cash client receivables:

If the cash clients fail to settle prolongly after T+2 settlement basis, the information of such receivables will be referred to the management of Emperor Securities who shall consider taking appropriate follow-up action.

### *Directors' review and decision*

The directors of Emperor Securities will review the outstanding margin loans, the overdue loans and advances and unsettled cash clients receivables referred from the credit risk control department case-by-case and decide on the appropriate impairment allowance to be made.

As at 31 December 2006, the Group had about 697 active margin clients whose margin securities trading accounts have recorded activities for purchase and/or sale of securities in the past twelve months. For each of the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, interest income derived from the Group's margin financing business accounted for approximately 13.12%, 13.19%, 25.38%, 23.03% and 31.09% of the Group's total turnover respectively.

As at 31 March 2004, 2005 and 2006 and 31 December 2005 and 2006, the margin financing accounts maintained with the Group had a total outstanding loan balance of approximately HK\$66.54 million, HK\$74.77 million, HK\$89.99 million, HK\$72.43 million and HK\$97.54 million respectively. Interest rates charged by the Group for the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006 ranged from prime rate to 8% over prime rate per annum. In determining the interest rate, reference will be made to the credit standing of the relevant clients and the quality of the securities pledged and/or other collaterals given. No aging analysis is disclosed as in the opinion of the Directors, the aging analysis does not give additional value in view of the nature of business of share margin financing.

As at 31 March 2004, 2005 and 2006 and 31 December 2005 and 2006, the total market value of securities pledged as collateral in respect of the loans to margin clients was HK\$882 million, HK\$1,094 million, HK\$1,024 million, HK\$1,234 million and HK\$1,974 million respectively.

The Group made a provision for margin loans of approximately HK\$1.0 million for the year ended 31 March 2004 and a written back of HK\$2.9 million for the year ended 31 March 2005. No provision for margin loans was made for the nine months ended 31 December 2005 and the two years ended 31 March 2006 and a further provision for loans to margin or cash clients of approximately HK\$34,000 was made for the nine months ended 31 December 2006. No bad debts were written off for the Group's margin loans during the Track Record Period.

In addition to margin financing, the Group also provides loans and advances to its clients, which are term loans secured by stocks listed on the Stock Exchange. Details of the Group's risk management policies with respect to loans and advances can be found in the paragraph headed "Credit risk" under the sub-section headed "Current internal control systems" of this section. For each of the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, interest income derived from such loans and advances of the Group accounted for approximately 29.84%, 26.43%, 20.35%, 21.07% and 6.99% of the Group's total turnover respectively.

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As at 31 March 2004, 2005 and 2006 and 31 December 2005 and 2006, approximately HK\$113.4 million, HK\$104.3 million, HK\$97.6 million, HK\$122.4 million and HK\$56.9 million respectively were loans and advances outstanding from the clients of the Group. Interest rates charged by the Group for the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, ranged from fixed rates of 1% to 2.5% per month and variable rate of 3% over prime rate per annum. In determining the interest rates, reference will be made to the credit standing of the relevant clients and the quality of the securities pledged. No aging analysis is disclosed as in the opinion of the directors of the Company, the aging analysis does not give additional value in view of the nature of financing business of the Group.

The Group's loans and advances were secured by listed securities with a total market value of approximately HK\$776 million, HK\$878 million, HK\$699 million, HK\$675 million and HK\$1,388 million as at 31 March 2004, 2005, 2006 and 31 December 2005 and 2006 respectively.

The Group's largest financing client for margin financings or loans and advances contributed approximately 26.33%, 31.76%, 24.16% and 7.03% respectively of the Group's interest income from financing activities for each of the three years ended 31 March 2006 and the nine months ended 31 December 2006. For the same years/period, the Group's five largest financing clients in aggregate accounted for approximately 74.92%, 66.17%, 47.28% and 22.79% respectively of the Group's interest income.

The Group made a provision for loans and advances of approximately HK\$7.0 million for the year ended 31 March 2004 and a written back of HK\$7.0 million for the year ended 31 March 2005 respectively. No provision for loans and advances was made for the two years ended 31 March 2006 and nine months ended 31 December 2005 and 2006. No bad debts were written off for the Group's loans and advances during the Track Record Period.

Details of the Group's accounting policies or loans and receivables, and impairment allowance for bad and doubtful debts are set out in Notes 3 and 4 to the accountants' report contained in appendix I to this prospectus.

## SALES AND MARKETING

The sales and marketing functions of the Group are carried out by its sales and marketing team comprising 51 account executives as at 31 December 2006, who have extensive sales and marketing experience in the finance industry and have knowledge of a wide range of financial products. Unlike other retail business, the Group has not in the past relied on its branch network to solicit clients.

The Directors are of the view that the Group places great emphasis on client relationship and each account executive is responsible for a portfolio of clients whom they serve personally. Nevertheless, as the Group has been focusing on retail clients, branch office will however be convenient to the Group's existing clients and may attract new walk-in clients, and the Group would like to expand its branch network to tap new clients. Going forward, the Group would continue to expand its client portfolio through expansion of its sales team and branch network at suitable locations, advertisement of the Group's business and services, and referral from existing clients.

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### **The Group's top five largest clients**

For the three years ended 31 March 2006 and the nine months ended 31 December 2006, the Group's largest client accounted for approximately 11.36%, 12.58%, 11.05% and 7.30% respectively of the Group's total turnover respectively. During the same period, the Group's top five largest clients, in aggregate, accounted for approximately 35.46%, 34.75%, 26.27% and 20.52% of the Group's total turnover respectively.

During the year ended 31 March 2005, Emperor Securities had acted as an underwriter and received underwriting commission of approximately HK\$2 million for a rights issue made by Emperor Entertainment Hotel Limited (formerly known as Emperor (China Concept) Investments Limited). Accordingly, Emperor Entertainment Hotel Limited became one of the Group's five largest clients for the financial year ended 31 March 2005. Emperor Entertainment Hotel Limited is owned approximately 34.82% by the Emperor Group as at the Latest Practicable Date. Save as the aforesaid, to the knowledge of the Directors, none of the Directors or their respective associates (as defined in the Listing Rules), or the existing Shareholders who own more than 5% of the Company's issued share capital, has any interest in any of the Group's five largest clients.

### **COMPETITION**

As at 31 December 2006, there were a total of 469 local Stock Exchange Participants and 135 local Futures Exchange Participants; 425 and 135 of which are trading participants while the remaining 44 and nil are non-trading participants in the stockbroking and futures trading industry in Hong Kong respectively. Given such keen competition, the Group has to attract and retain skilled staff in order to provide quality service to its clients. The Group places emphasis on building team spirit and relies on the commitment and integrity of its staff to compete against other competitors.

The Directors are of the view that the Group generally has the following competitive advantages:

#### **Long trading history with stable business development**

The Group's financial brokerage arm has commenced its business for more than 12 years with stable business development. The Group has its headquarter in Wanchai together with two retail branches which in aggregate have about 50 account executives. With over 12 years' experience in the brokerage business, the Group has developed an effective operating system. Through the use of its operating system and computer software products, the Directors believe that the Group can offer tailored and instant solutions to meet its clients' needs in turbulent market.

#### **Recognised brand and strong client base**

The Directors believe that the Group's long history helps it establish quality services to its core clients. During the past few years, people in Hong Kong experienced peaks and troughs of the local stock market and economy. During those tough periods, the Group still strived to equip itself to survive in good and bad times and has taken measures including strengthening its brand through advertising, publishing its market commentaries in the press and attending interviews in financial programs on television and building up its client base. As at 31 December 2006, the Group had about 18,841 trading accounts. The Directors believe that this solid client base is built up by the Group's account executives over the years.

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About 73% of the Group's clients have business relationships with the Group for more than five years. About 3,619 clients have been served by the Group's account executives for more than ten years. The Directors are of the view that these long-standing relationships between the account executives, the clients and the Group have contributed to the Group's growth and success over the years.

### **Experienced management**

The managing Director, Ms. Daisy Yeung, and the executive Directors, Mr. Chan Pak Lam, Tom and Mr. Yeung Kun Lee, Sunny, have over ten years of experience in the securities dealing and financial services industry. With their extensive experience, the Directors believe that the Group can master the changing complexities and can react timely to the buoyant market conditions. Please refer to the section headed "Directors, senior management and staff" of this prospectus for further details of the experience of the Group's management team.

### **Competent and dedicated team of professionals**

As at 31 December 2006, the Group had 51 account executives. About 10% of the Group's account executives have stayed with the Group for more than ten years and about 41% have been with the Group for more than five years. In addition, the Group has a team of experienced and loyal support staff. These support staff comprise personnel from the credit risk control, settlement, accounting, research and administration and personnel departments. As at 31 December 2006, about 40% of such staff joined the Group for more than five years. In addition, regular professional training is conducted to update the employees' professional knowledge and skills.

### **Lean and efficient**

The Directors believe that the Group's scale of operations have brought to itself efficiency and fast response to the clients, which minimise the problems of excessive layers of approval normally found in large organizations. The Group strives to always remain healthy and vibrant by constantly and consistently equipping its front line employees through regular professional training. The Directors believe that the main reason for the Group's success in the fiercely competitive industry is its ability to be lean and efficient. For the three years ended 31 March 2006 and the nine months ended 31 December 2005 and 2006, the adjusted net profit margin of the Group was 32.15%, 30.21%, 27.35%, 26.84% and 25.46% respectively.

## **STRATEGIES**

### **Continue to invest in quality people**

The most important asset of the Group is its people. The Group keeps on recruiting qualified account executives with diverse educational backgrounds and/or experience so as to satisfy the varying needs of its client. The Group stresses the importance of integrity, quality service, teamwork and expertise. In order to motivate its employees, the Group has provided discretionary bonus to reward its employees for their contribution to the Group. The Group will also continue to provide regular professional training to its employees to ensure that they keep abreast of new knowledge and skills.

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### **Strong customer base**

Being client oriented is one of the Group's key strategies that contributes to its success. The Group has established standards to maintain the culture of its staff passion and commitment to service. The Directors believe that client relationships are important and the Company's account executives always strive to uphold the well-established relationships with the clients. In order to develop its business, yet reduce the risks at the same time, the Group will further intensify its marketing efforts to expand and diversify its client base into wider spread of backgrounds ranging from high net worth individuals to small retail investors.

As at 31 December 2006, the Group had about 3,692 active securities clients and about 369 active futures clients whose accounts have recorded purchase and/or sale of securities stockbroking transactions and have recorded open and/or close position of futures contracts transactions in the past twelve months. These active securities clients include 2,995 cash clients and 697 margin clients, approximately 98.62% of which are retail investors and the remaining 1.38% is corporate clients. For active futures clients, it includes approximately 98.37% is retail investors and the remaining 1.63% is corporate clients.

As at 31 December 2006, the Group had about 697 active margin clients whose margin securities trading accounts have recorded activities for purchase and/or sale of securities in the past twelve months. In addition, the Group provides to clients loans and advances, all of which are secured by stocks listed on the Stock Exchange.

### **Sales and marketing team**

The Group has an experienced sales and marketing team for both stock and futures trading businesses. As at 31 December 2006, the sales and marketing team comprised 51 account executives, who have regular contacts with the clients. The Directors are of the view that the Group has maintained good business relationship with existing clients and is making progress in establishing network with new clients.

### **Advertising**

As in the past, advertising on television would still be the main channel of promoting the Group's services to the market.



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### REGULATIONS, LICENCES AND TRADING RIGHTS

The securities market in Hong Kong is highly regulated. The principal regulatory bodies governing the Group's business are the SFC, the Stock Exchange and the Futures Exchange. The Group's businesses are subject to a number of legislations and regulations and the respective rules of the Stock Exchange and the Futures Exchange and, upon listing, the Listing Rules.

In addition, certain members of the Group are required to be licensed with the SFC and apply as participants of the Stock Exchange or the Futures Exchange in order to carry on their businesses. As at the Latest Practicable Date, the Group held the following licences/trading rights which are required to carry on the activities of the Group as described in this prospectus:

<b>Licence/certificate/ participantship holder</b>	<b>Licence/certificate/ participantship</b>	<b>Date of issue/admission re-issue/renewal</b>
Emperor Securities	Licence under SFO to carry on Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities	2 March 2005
	Stock Exchange Trading Right Certificate No. 456, 457, 458 and 459	6 March 2000
	Stock Exchange Participant Certificate	1 February 2006
	HKSCC broker participantship	25 May 1992
	Options Trading Exchange Participantship	4 September 1995
	Money Lenders Licence under the Money Lenders Ordinance	20 June 2006
Emperor Futures	Licence under SFO to carry on Type 2 (dealing in futures contracts) and Type 5 (advising on futures contracts) regulated activities	2 March 2005
	Futures Exchange Trading Right Certificate No. 0050 and 0051	6 March 2000
	Futures Exchange Participant Certificate	6 March 2000
	HKCC Participant Certificate	6 March 2000
Emperor Gold & Silver	The Chinese Gold & Silver Exchange Society Membership Certificate	17 November 1995

Since its establishment, the Group has not experienced any difficulties in renewing any of its licences and participantship or has any of such licences and participantship been revoked.



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The last day to apply for the next renewal of Emperor Securities' Money Lenders Licence under the Money Lenders Ordinance is 29 June 2007. Except for the aforesaid licence, all other licences for the Group do not have specific renewal due date.

The HKCC amends the HKCC rules and procedures whereby every HKCC Clearing Participant shall maintain liquid capital of no less than HK\$5 million or the required liquid capital under the FRR, whichever is greater. The amendment came into operation on 1 November 2005 with a one-year grace period being given to existing HKCC Clearing Participants.

Emperor Futures currently has a paid up share capital of HK\$50 million which is well above the minimum paid-up share capital requirement of HK\$5 million. In addition, Emperor Futures, being a HKCC Clearing Participant, is required to maintain a minimum liquid capital of HK\$5 million which is the highest amount requires under the SFO, the FRR and the Rules of the Futures Exchange. Emperor Futures has at all time complied with such liquid capital requirements.

Emperor Securities, being a Stock Exchange Participant providing securities margin financing, currently has a paid up share capital of HK\$70 million which is well above the minimum paid-up share capital requirement of HK\$10 million. Besides, as both an Option Trading Exchange Participant and a Stock Exchange Participant, Emperor Securities is required to maintain a minimum liquid capital of HK\$5 million under the SFO, the FRR and the Rules of the Stock Exchange. Emperor Securities has at all times been meeting such liquid capital requirements.

### DISCIPLINARY ACTIONS

The Group's operations are subject to the securities laws, rules and regulations promulgated by the SFC and other relevant regulatory authorities of Hong Kong. For the purpose of carrying on its business, the Group's operating subsidiaries, including Emperor Securities and Emperor Futures, and their licensed representatives including responsible officers have to be licensed with the SFC unless specific exemption under the SFO is available. The SFC has in the past instituted disciplinary actions against licensed representatives of the Group for non-compliance with the relevant rules and regulations. The following summarises the public disciplinary actions having been taken by the regulatory authorities against the Group's licensed representatives relating to activities undertaken by them during their employment with the Group from May 1996 (when Emperor Securities and Emperor Futures became wholly owned subsidiaries of the Emperor Group) to the Latest Practicable Date:

**(i) Suspension of registration of a former dealer's representative (now known as licensed representative)**

In July 2001, the SFC announced that it had suspended the registration of Mr. Poon Pong Wah ("Mr. Poon"), a former dealer's representative of Emperor Securities and Emperor Futures, under both the repealed Securities Ordinance and the Commodities Trading Ordinance for a period of 30 months.

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The action stemmed from an inquiry covering the period from May 1996 to April 1998 when Mr. Poon was then a dealer's representative of Emperor Securities and Emperor Futures. The inquiry found that:

- Mr. Poon, without the knowledge or authority of an ex-colleague, used a copy of that ex-colleague's identity card and forged the ex-colleague's signature on Emperor Securities' account opening documents, thereby inducing Emperor Securities to open an account with it in the name of that ex-colleague in order that he could conduct his own trading through that account; and
- Mr. Poon used that account and another account in the name of his wife to conduct his own trading without informing Emperor Securities. Through the above arrangement, Mr. Poon had been able to conduct his own trading and be entitled to the amount of commission income arising therefrom.

The SFC concluded that Mr. Poon's conduct seriously impugned his fitness and properness. In deciding to suspend his registration, the SFC had taken into consideration, among others, that the trading involved was not substantial and no client had suffered any loss.

Mr. Poon left Emperor Securities and Emperor Futures in September 2000.

The Group has subsequently enhanced its account opening procedures whereby the marketing administration department which processes account opening documents shall call the client to verify his identity by telephone.

### **(ii) Public reprimand of a former responsible officer**

In November 2001, SFC made a public reprimand against Ms. Fan Man Seung, Vanessa ("Ms. Fan") in her capacity as a dealing director of Emperor Securities for failing to make sufficient inquiry in respect of the independence of prospective subscribers to an initial public offering of shares of Dong Jian Group Holdings Limited (stock code: 649) (now known as "Shimao International Holdings Limited"), a company listed on the Stock Exchange as from July 1998. Ms. Fan also failed to provide the SFC with detailed and accurate information during the SFC's investigation into the initial public offering. The SFC found that these matters impugned Ms. Fan's fitness and properness and publicly reprimanded her for the above incident in November 2001. Ms. Fan resigned as a responsible officer of each of Emperor Securities and Emperor Futures in March 2007.

The Group has adopted a policy whereby all placees and subscribers are required to execute a form to declare their independence.

### **(iii) Public reprimand and pecuniary fine against a licensed representative**

Ms. Yan Yuk Hing, Liza (“Ms. Yan”), a licensed representative of Emperor Securities and Emperor Futures, failed to keep sufficiently accurate and contemporaneous written record of client’s orders. Those orders were received through the mobile phone of Ms. Yan after office hours between 10 and 23 April 2003 from a margin client who, at the time, did not have an established track record of settlement. The SFC publicly reprimanded and fined her HK\$30,000 for the above incident in March 2007.

The Group has adopted a policy whereby all account executives shall immediately record in the buy/sell tickets details of the trading orders received from clients. The Group has also adopted a policy that for orders received through mobile phones, the marketing administration department has to perform sample check daily to confirm the order details with the client.

### **(iv) Pecuniary fine against a former licensed representative**

Ms. Wong Man Suen, formerly known as Wong Yuen Yu (“Ms. Wong”), while employed as a licensed representative of Emperor Futures made unsolicited calls between April and May 2006 to a person whom she persuaded to open an account with the firm to trade in futures contracts. As a result, that person traded in corn futures through Ms. Wong and sustained loss. Ms. Wong was prosecuted by the SFC for making unsolicited calls, contrary to section 174 of the SFO. Ms. Wong was fined HK\$5,000 and ordered to pay investigation costs of HK\$8,790 to the SFC for the above incident.

Ms. Wong was a licensed representative of Emperor Securities and Emperor Futures until August 2006.

The Group has adopted a policy whereby all account executives are not allowed to engage in cold calling activities.

Save as disclosed above, the Directors, having made all relevant enquiries, are not aware of any other public disciplinary actions having been taken by the regulatory authorities against members of the Group or any of its responsible officers or other licensed representatives relating to activities undertaken by them during their employment with the Group from May 1996 (when Emperor Securities and Emperor Futures became wholly owned subsidiaries of the Emperor Group) to the Latest Practicable Date.

## **PENDING INVESTIGATION CASES INSTIGATED BY THE SFC**

Emperor Securities and/or Emperor Futures are currently involved in the following investigation cases instigated by the SFC:–

1. a case that concerns the internal control of Emperor Securities and Emperor Futures regarding cold calling activities. It is still under investigation by the SFC;
2. a case that concerns the internal control of Emperor Securities as regards protection of its operations and clients’ assets as required under paragraph 4.3 of the Code of Conduct which provides that: “A licensed or registered person should have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its

operations, its clients and other licensed or registered persons from financial loss arising from theft, fraud, and other dishonest acts, professional misconduct or omissions.”

This investigation matter relates to the following complaint cases:

(a) Emperor Securities received a letter dated 29 June 2004 from a person (the “Complainant”) who alleged that an account executive of Emperor Securities sold him an investment product on 30 March 2004 for HK\$80,000. It was alleged that the principal amount together with HK\$5,000 interest would be repaid to the Complainant on 27 April 2004. The purported account executive gave the Complainant a personal cheque in the amount of HK\$85,000. The cheque was subsequently dishonored. The purported account executive then gave the Complainant another cheque issued in the name of her purported supervisor who was then an account executive of Emperor Securities. The purported supervisor claimed that he has never issued such cheque. The cheque was also dishonored. According to the Complainant, the Complainant reported the case to the SFC and it was the SFC that advised the Complainant to approach Emperor Securities for a preliminary investigation of the matter. Emperor Securities issued a reply letter dated 30 June 2004 to inform the Complainant of its findings as follows:

- The purported account executive of Emperor Securities has never acted as such for Emperor Securities;
- The purported supervisor has never supervised the purported account executive of Emperor Securities. He, however, was an account executive of Emperor Securities;
- According to company records, the Complainant’s name was not found in Emperor Securities’ client list;
- Emperor Securities did not offer any “guaranteed fund base investment” product as alleged; and
- With respect to the dishonored cheque of the purported account executive, Emperor Securities could not comment on that. As for the dishonored cheque issued by the purported supervisor who was an account executive of Emperor Securities, it was recalled that the explanation provided by the purported supervisor was he has never issued such cheque. He, however, might have lost a blank cheque or it had been stolen. He had already reported the case to the bank.

Emperor Securities advised the Complainant to report the case to the police. On 2 July 2004, Emperor Securities wrote to the SFC informing it of details of the case.

- (b) In mid December 2003, a client of Emperor Futures made an enquiry with its ex-credit risk control manager who handled complaint cases of Emperor Securities and Emperor Futures as regards some futures trading activities purported to be transacted by the client through a lady (the “Lady”) which was later found out to be the then girlfriend of an account executive of Emperor Futures and Emperor Securities. That account executive was the same account executive involved in the complaint as detailed in paragraph (a) above. From the recollection of the management of Emperor Futures, the former credit risk control manager had then interviewed the above account executive who explained that the enquiry was about private matters. Subsequently, the client wrote to Emperor Futures informing that she had no complaint against Emperor Futures or any person in respect of operation of her account maintained with Emperor Futures. On 8 January 2004, the client signed a third party authorization authorizing the Lady to operate her accounts maintained with Emperor Securities and Emperor Futures. On 14 July 2004, the client approached the Group again and raised for a second time her complaint as regards the above futures trading activities back in 2003. From the recollection of the management of Emperor Futures, the client also alleged that she received no statements of those transactions and the Lady, who claimed herself an account executive of Emperor Futures, owed her a few hundred thousand dollars in connection with this matter. The client also claimed that she had in April 2003 deposited HK\$120,000 into the bank account of Emperor Securities for credit to her securities account maintained with Emperor Securities. It was later revealed that Emperor Securities had credited this sum to another client’s account handled by the then boyfriend of the Lady based on the account number written on the faxed deposit slip received by Emperor Securities. Upon receipt of the complaint, the Group invited the Lady to a meeting to understand the facts. The Lady disclosed that the client was her ex-colleague. According to her recollection, she admitted that the HK\$120,000 was deposited by the client and claimed that she had already repaid the same to the client. In addition, the Lady claimed she had paid the client a few hundred thousand dollars for compensation of her mistake in handling the client’s faxed deposit slip. The Lady alleged that she has never represented herself as an employee or account representative of the Group. According to the SFC, both the Lady and the above account executive admitted to the SFC that the Lady started working as the account executive’s personal assistant at the office of Emperor Securities at the material time, but she was not officially employed by Emperor Securities. Her duties as the account executive’s personal assistant included taking telephone calls from his clients and handling settlement matters on his behalf by, for example, collecting clients’ faxed deposit slips from Emperor Securities’ fax machines, and passing them directly to the staff at the settlement department of Emperor Securities for further processing.

Emperor Futures and Emperor Securities advised the complainant and the Lady to report the matter to the police. Emperor Futures and Emperor Securities also took the initiative to report the incident to the SFC and have undertaken the following actions:–

- On 14 July 2004, Emperor Futures and Emperor Securities suspended the Lady’s client account maintained with them.

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- On 15 July 2004, Emperor Futures and Emperor Securities suspended the duties of the account executive and transferred all the client accounts handled by him to the house team. The account executive resigned from Emperor Futures and Emperor Securities in August 2004.
- In August 2004, the Group adopted a new policy whereby all clients are required to send the deposit slips with full client details (for example, name, account number and signature) indorsed on them to the settlement department directly. The Group further enhanced its policy whereby in the case of a cash deposit or a deposit by cheque, if the deposit slips do not show the identities of the depositors or the drawers of the cheques, such deposits will initially be treated as unidentified deposits. Follow-up actions would be taken by the settlement department to confirm and/or obtain appropriate supporting documentation to evidence the identities of the depositors.
- In September 2004, Emperor Futures and Emperor Securities appointed an independent audit firm to write to the clients handled by the relevant account executive to ascertain whether their account balances, largely as at 30 July 2004, were correct. Except for the above HK\$120,000 deposit, no discrepancies was reported in response to the circularization done by that independent audit firm.
- In January 2007, Emperor Securities and Emperor Futures wrote to clients reminding them to place trading orders only with their handling account executives or the house team.
- In January 2007, Emperor Securities and Emperor Futures issued a memo to its account executives setting out procedures to prevent unlicensed activities and protection of confidential client information when there are visitors at the office premises of Emperor Securities and Emperor Futures. These procedures have been incorporated in the account executive handbooks and operation manual of Emperor Securities and Emperor Futures.

The Group was informed by the SFC that it has completed investigation into the matters as set out in paragraph 2(a) and (b) above. The SFC issued a letter on 18 December 2006 proposing disciplinary actions against Emperor Securities including public reprimand and a fine of HK\$200,000. It appeared to the SFC that Emperor Securities failed to prevent the relevant account executive from engaging the Lady, a non-employee, to perform his functions in Emperor Securities. Further, it appeared that Emperor Securities' equipment for the receipt of clients' settlement instructions and other confidential information are not stored in a restricted area access to which is limited to authorised persons only, putting clients' assets and information at risk of being misused. Emperor Securities has made a submission to the SFC seeking to mitigate the SFC's proposed disciplinary actions.

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To the knowledge of the Directors or according to the provisions of the SFO, the SFC may take actions including suspension or revocation of licences, public or private reprimand, or imposition of a fine against a licensed person and/or its responsible officers or other licensed representatives in respect of any non-compliance with rules or regulations enforced by the SFC. In respect of the above two investigation cases, there is one for which the SFC has proposed against Emperor Securities disciplinary actions which include public reprimand and pecuniary penalty. Emperor Securities has made a submission to seek to mitigate the SFC's proposed disciplinary actions; regardless of the outcome, the Directors believe that the proposed disciplinary actions would not have a material adverse impact on the business, financial position or performance of the Group.

The other investigation case involves internal control system as regards cold calling activities. After considering the area of concern as identified by the SFC in that investigation case, the Directors do not anticipate that any actions, if taken, by the SFC would have a material adverse impact on the business, financial position or performance of the Group.

Save as disclosed above, the Directors, having made all relevant enquiries, are not aware of any other public disciplinary actions being proposed by the regulatory authorities against members of the Group up to the Latest Practicable Date.

Save as disclosed above where the level of disclosure is to the extent that is allowed subject to any secrecy provision under the SFO, the Directors, having made all relevant enquires, are not aware of any other pending investigations being undertaken by the regulatory authorities against any members of the Group up to the Latest Practicable Date.

### IDENTIFIED INTERNAL CONTROL WEAKNESSES

Under the Code of Conduct, a licensee should have internal control procedures and financial and operational capabilities which can be reasonably expected to protect its operations, clients and other licensed or registered persons from financial loss arising from theft, fraud and other dishonest acts, professional misconduct or omissions.

In general, "internal controls" represent the manner in which a business is structured and operated so that reasonable assurance is provided of:

- (a) the ability to carry on the business in an orderly and efficient manner;
- (b) the safeguarding of its and its clients' assets;
- (c) the maintenance of proper records and the reliability of financial and other information used within and published by the business; and
- (d) the compliance with all applicable laws and regulatory requirements.

The following summarizes the internal control weaknesses identified in the operating systems of Emperor Securities or Emperor Futures. Some of the following findings may no longer be relevant as Emperor Securities and Emperor Futures have over time revised or enhanced their internal control systems to meet the applicable laws, rules or regulations:



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### **I. Findings from the most recent limited review of business activities of Emperor Securities conducted by the SFC in around 2000**

#### *1. Compliance with the Securities Ordinance then in force*

- 1.1 On 31 August 2000, Emperor Securities pledged 771 shares of a listed company held by Emperor Securities on behalf of cash client with a bank for facilities granted to Emperor Securities, which contravened section 81(4) of the repealed Securities Ordinance. The breach has been subsequently rectified. Emperor Securities currently has not pledged any client securities for banking facilities.

According to the records maintained by the settlement department, the above incident arose because a staff of the settlement department of Emperor Securities had forgotten to withdraw from the bank (to which securities of margin clients were pledged for banking facilities) 771 shares of that listed company already sold by a margin client for deposit into Emperor Securities' CCASS account for settlement purpose. As a result, 771 shares of that listed company held in Emperor Securities' CCASS account on behalf of cash clients were transferred out of Emperor Securities' CCASS account for settlement.

To avoid the same mistake repeating, the settlement department has developed a new report which shows whether the stock maintained in Emperor Securities' segregated account with CCASS on behalf of margin clients is sufficient for settlement purpose. A staff of the settlement department is assigned to review the report and take necessary action. A double checking system is adopted whereby the work done by the staff is checked by a senior staff of the settlement department.

#### *2. Compliance with the Code of Conduct for Persons Registered with the Securities and Futures Commission then in force ("2001 Code of Conduct")*

##### *2.1 Account opening*

The 2001 Code of Conduct requires a licensed person to establish procedures to satisfactorily ensure the true identity of the client. The account opening procedures then adopted by Emperor Securities did not provide for independent verification of client's identity. Pursuant to the then prevailing account opening procedures, account executives may execute account opening documentation outside the office premises and could act as the only witness for signing the client agreement.

Emperor Securities has adopted a policy whereby the marketing administration department which processes account opening documents shall call the client to verify his identity by telephone.

#### *3. Compliance with FRR*

##### *3.1 Joint Credit Facility*

A joint credit facility obtained by Emperor Securities and Emperor Finance from a bank were interavailable to Emperor Finance and Emperor Securities, which were then both



wholly owned by EIDL. Emperor Securities and Emperor Finance would at all times be jointly and severally liable for all amounts payable in respect of any utilization of the said facility. Since the transfer of the share margin financing business from Emperor Finance to Emperor Securities, there has not been any drawdown of the above banking facility by Emperor Finance. Emperor Finance has ceased to be a borrower of the above banking facility since March 2001.

A joint overdraft facility was obtained by Emperor Securities, Emperor Futures and Emperor Finance from another bank. According to the bank facility letter, there was an unlimited joint and several covenant to pay any advances under the facility on the part of the borrowers. As such, there would be a contingent liability on the part of Emperor Securities and/or Emperor Futures (as the case may be) for drawdown by the other borrower(s). Accordingly, a financial adjustment would need to be made in respect of that commitment in the liquid capital computation of Emperor Securities and/or Emperor Futures (as the case may be) under the FRR.

The joint credit facilities had been restructured into separate facilities for different entities.

## **II. Findings from the most recent limited review of business activities of Emperor Futures conducted by the SFC in around 2004**

### *1. Compliance with Securities and Futures (Client Money) Rules ("CMR")*

1.1 Emperor Futures' clients who also had margin securities trading accounts with Emperor Securities signed standing authorization form authorizing transfers of funds between their futures and margin securities trading accounts. These standing authorities did not comply with the then CMR in the following respects:

- They did not set out precisely the specific ways and conditions under which transfers between those accounts were to be effected.
- They did not specify the validity period, which should be for a period not exceeding 12 months.
- They did not specify the manner in which the standing authorities were to be revoked.

Emperor Futures has adopted a new standing authorization form which complies with the CMR and the authorization shall be renewed on an annual basis.

1.2 Emperor Futures transferred its commission income earned on clients' trading of futures contracts from clients' segregated bank accounts on a monthly basis. This contravened the CMR, which requires a licensed corporation to transfer amount that is not client money from its segregated account within one business day of its becoming aware that such money is kept in the segregated account.

Emperor Futures has adopted a policy to transfer its commission income earned on clients' trading of futures contracts from clients' segregated bank accounts within one business day of its becoming entitled to the above commission income.

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2. *Compliance with the Securities and Futures (Contract Notes, Statements of Account and Receipts) Rules (“CNR”)*

2.1 The statements of account issued by Emperor Futures did not comply with the requirements of the CNR in the following respects:

- Commission, levy and charges payable in connection with the relevant contracts were not separately stated in the daily statements of account; and
- Though the monthly statements of account sets out contracts made by Emperor Futures on behalf of clients, details of individual contracts were not clearly described therein pursuant to the requirements of the CNR.

Emperor Futures has adopted a revised statements of account which meets the above and other requirements of the CNR.

3. *Dealing records*

3.1 There were instances in which the order receiving time that was time stamped on buy/sell tickets prepared by account executives who placed clients’ trading orders with dealers were behind the order placing time stamped on the buy/sell tickets prepared by dealers. Under the Securities and Futures (Keeping of Records) Rules, intermediaries should keep such trading and other records as are sufficient to explain and reflect the operation of its business. In addition, the Code of Conduct requires a licensed person to record and immediately time stamp records of the particulars of the clients’ instructions for trading orders.

Emperor Futures has clearly set out in its operation manual the requirement that all account executives and dealers shall timely stamp the buy/sell tickets. In addition, briefing session has been conducted to remind the account executives and dealers of the importance of time stamping the buy/sell tickets. A double checking system has been adopted whereby the time stamping of buy/sell tickets is double checked by the dealing department at day end.

3.2 The order placed by a specific client was found not captured on Emperor Futures’ telephone recording system. The placing of that client’s order with the dealer by the account executive was however captured in the telephone recording system. Under the Code of Conduct, the use of mobile phones for receiving client order instructions is discouraged. In circumstances where orders are received by mobile phones, the time of order receipt and the order details should be recorded immediately (e.g. by a call to the office system or in writing by hand).

Emperor Futures has clearly set out in its operation manual that all account executives shall immediately record in the buy/sell tickets details of the trading order received from clients. It has adopted a new format of buy/sell ticket which requires an account executive to clearly record the mode by which the client’s trading orders are received. Emperor Futures has also adopted a policy requiring the marketing administration department to perform sample check on whether details of orders, including the mode by which clients’ trading orders are received, are clearly recorded in the buy/sell ticket. For orders received through mobile phones, they will perform sample check daily to confirm the order details with the client.

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### 4. *Client margin*

- 4.1 The margin status reports available from Emperor Futures' settlement system only showed the required margin calls at maintenance level for all outstanding positions. The margin requirement did not take into account the initial margins that were required for client trades done during the day.

Emperor Futures has adopted a revised margin status report which also shows the initial margin required.

- 4.2 Clients who had a history of transacting exclusively day trades in futures products traded on the Futures Exchange were allowed to conduct day trades without depositing sufficient initial margin. This was a breach of the rules of Futures Exchange and the Code of Conduct which require that an exchange participant shall not transact a day trade on behalf of an established client who has a history of transacting day trades exclusively until and unless the exchange participant has received from the client collateral adequate to cover his initial margin requirements.

Emperor Futures has adopted a policy that all clients (including day traders) must have sufficient initial margin deposit before the execution of any futures transactions.

- 4.3 Account executives did not keep proper records of margin calls other than some rough notes made on internal reports. Emperor Futures is required under the Code of Conduct to maintain proper records of particulars of all margin calls and demands for variation adjustments made on clients.

Emperor Futures has adopted a policy whereby the account executives shall keep a record of the margin calls and making of margin calls via the tape recorded phone is encouraged. Standard code for results of margin calls has been developed by the credit risk control department. In addition, the account executives are also required to report before day end the results of the margin calls to the credit risk control department.

Briefing session has been conducted in respect of, among others, the margin call record policy of Emperor Futures.

### 5. *Designation of discretionary/employees trading accounts*

- 5.1 Emperor Futures had, at the time of SFC's review, two discretionary accounts. Only one of them was designated as "discretionary account" in Emperor Futures' records. In addition, some of Emperor Futures' employees trading accounts were not clearly designated as such in its records. Emperor Futures is required under the Code of Conduct to properly designate these accounts.

- 5.2 In addition, it was noted from sampled listening of telephone tapes that a client of Emperor Futures authorized an account executive of Emperor Securities to place orders on her behalf, Emperor Futures is required to clarify if this account was an account operated by the said

account executive and if so, the controls taken by Emperor Futures to identify all accounts operated by third parties or employees of Emperor Securities and subject them to regular monitoring and review.

Emperor Futures has adopted a policy which requires the credit risk control department to double check the list of discretionary/employee/third party operated trading accounts prepared and updated by the marketing administration department which processes client account opening forms.

Emperor Futures has also adopted a policy to sample check the trading activities of the discretionary accounts and employee trading accounts on a daily basis and to perform sample checking of the trading activities of the associated accounts of employees on a monthly basis.

### 6. *Hold mail arrangements*

#### 6.1 Emperor Futures did not comply with the Code of Conduct in the following respects:

- Firstly, it did not provide some hold mail clients with a risk disclosure statement in respect of the risk of authorizing a licensed corporation to hold mail on their behalf; and
- Secondly, it did not confirm with the clients concerned at least on an annual basis whether they wished to revoke the authorities. Instead, it allowed the authorities to run until clients revoked them.

Emperor Futures has adopted a modified hold mail form which includes a risk disclosure statement that meets the requirements of the Code of Conduct.

Emperor Futures has adopted a policy to confirm with the clients on an annual basis whether they wished to revoke the hold mail authorization.

### 7. *Control over receipts from clients*

#### 7.1 In a number of instances there were unidentified deposits into Emperor Futures' bank accounts and the settlement staff relied on information provided by account executives for the purpose of assigning such deposits to client accounts.

Emperor Futures has adopted a policy whereby all clients are required to send the deposit receipts with client's signature, account number and name on it to settlement department directly; and in the case of a cash deposit or a deposit by cheque, if the deposit receipts received by Emperor Futures do not show the identity of the depositor, such deposit will initially be treated as unidentified deposit. Follow-up actions would be taken by settlement department to confirm with the respective clients and obtain appropriate supporting documentation to evidence the identities of the depositor. If the deposit remains unidentified for more than three months, the accounts department would request the payee details via the receiving bank and take appropriate actions.

### 8. *Information about clients*

- 8.1 In some instances, client's investment objectives, investment experience and financial situation in the clients' account opening forms were not completed. Emperor Futures is required to obtain the above information from clients under the Code of Conduct.

Emperor Futures has adopted a policy which requires the marketing administration staff to check the completeness of the account opening documents and to seek the outstanding information from the client, if any, by phone. Except with senior management's approval, all outstanding information in the account opening documents must be completed within two weeks; otherwise, Emperor Futures will freeze the relevant client's trading account.

### III. Letter of advice from the Stock Exchange

During the pre-opening sessions on 18 and 19 October 2005, a licensed representative of Emperor Securities (the "Licensed Representative") inputted bid and bid-cancel orders, and ask and ask-cancel orders placed by a client which had substantially affected the indicative equilibrium price of a stock. The client explained her intention of placing such orders but the Stock Exchange found the client's explanations incredible as they were contradictory and illogical. The client's order activities had significantly affected the indicative equilibrium price of the relevant stock and might have an impact on the integrity of the market as investors might have a wrong impression on the genuine market prices of the stock.

In addition, the Stock Exchange was concerned that the trading activities of the relevant client had exceeded the credit limit imposed on her on a few occasions, which increased the Group's financial risk and the risk to the overall market.

It was also revealed that the Licensed Representative had inadvertently committed 2 short-selling orders on 31 October 2005. These incorrect order entries were rectified by immediate buy-back from the market and through CCASS. The Licensed Representative had also, on a few occasions in October 2005, inputted an incorrect order quantity because of human error but these orders were cancelled before they were executed. The Stock Exchange was concerned that the Group's control on prevention of short-selling activities might be weak.

The Group held meetings with the Licensed Representative and gave him a warning reminding him to pay more attention when he placed client's orders. It was emphasized to the Licensed Representative that he has the responsibility to ensure that his clients were trading within their respective trading limits and to ensure that their accounts had sufficient number of shares before making any sale order. The Licensed Representative has subsequently left the Group.

The Group has adopted a policy whereby account executives and dealers are required to report to a designated person in the dealing department (the "Responsible Person") whenever they receive a trading order which deviates from the previous closing or market price by a defined limit. Credit risk control department is also required to monitor the trading system to detect any possible irregular trading which, if found, shall be reported to the designated Responsible Person for taking follow-up actions. The Responsible Person shall further report any suspicious cases to the compliance department and senior management.

#### **IV. Letter of advice from the SFC**

SFC issued a letter of advice dated 12 February 2007 to Emperor Futures whereby the SFC advised that in order to improve Emperor Futures' overall supervision and controls, the operation manual and account executives handbook of Emperor Futures should include sections on cold calling, churning and supervision of account executives by team heads. Churning refers to excessive buying and selling in client account(s) by a broker. In addition, the above areas should be made subject to separate training and instruction. For churning to occur, the broker must exercise control over the investment decisions in his or her client account, either through a formal written discretionary agreement or otherwise, and must engage in excessive trading in light of the financial resources and character of the account for the purpose of generating commissions.

Emperor Futures currently has no active discretionary accounts. In addition, Emperor Futures has included in its operation manual sections on cold calling, churning and supervision of account executives by team heads. Training on above areas is included in the training programmes for licensed representatives of Emperor Futures.

#### **V. Review of internal control systems**

The Reviewing Firm has been commissioned to perform review of certain internal control procedures and systems identified by the Directors as the key control systems and procedures of the Company or Emperor Securities or Emperor Futures (the "First Review").

On 29 November 2006, a report (the "First Report") was issued by the Reviewing Firm. The Reviewing Firm has performed field work at the office premises of the Company, Emperor Securities and Emperor Futures during the period from 7 August 2006 to 29 August 2006. After the First Review, the Company and the Joint Sponsors have also engaged the Reviewing Firm to perform a follow-up review (the "Second Review") which was conducted from early December 2006 to 8 December 2006. Subsequent to the Second Review, the Reviewing Firm has performed further review on the prevailing anti-money laundering and terrorist financing policies and procedures ("AML Policies") in two areas on 2 January 2007 and 4 January 2007 respectively (the "Final Review"). On 11 January 2007, a report (the "Second Report") was issued by the Reviewing Firm in respect of the Second Review and Final Review.

For the purpose of performing the reviews, the Reviewing Firm has:

- conducted interviews with the relevant management and staff members;
- reviewed relevant documentations on site;
- performed walkthroughs of processes and systems relating to the scope, where applicable;
- identified findings based on any deficiencies in the design of the controls and developed recommendations for improvement, where appropriate.

### **(A) The First Review**

The following summarises the findings and the recommendations made by the Reviewing Firm in the First Report:

#### **(i) Corporate governance structure**

The Company did not have a full corporate governance structure in place as required by the Stock Exchange at the time of the First Review. Although the Company had enlisted individuals to serve as executive Directors, non-executive Directors, independent non-executive Directors and audit committee members, it had not then established a remuneration committee.

The Company should establish a more comprehensive corporate governance structure in advance of its listing on the Stock Exchange in order to create greater synergies among the Board, related committee members and management, and to enhance the Company's ability to monitor the effectiveness of its internal controls environment. The detailed plan that senior management was developing should address the corporate governance requirements of the Listing Rules and be communicated to all relevant personnel to be involved in the plan. The execution of the plan and timetable should be tracked and followed up regularly.

At the time of the First Review, the Company had limited internal audit capabilities. Internal audit projects were executed by its holding company, EIDL. As a listed company, the management should formalise its own independent internal audit function to ensure that the audit work is being conducted independently and objectively.

#### **(ii) Written policies and procedures**

The Company has not, at the time of the First Review, established written or comprehensive policies and procedures in some key areas. For example:

- The account executives handbook distributed to the account executives did not include ethical principles, such as conflicts of interest and client priority.
- The Company's operational manual did not stipulate crisis management for securities accounts.
- There was no written human resources and training policies and procedures.
- Written and comprehensive enterprise-level risk management policies and procedures had not been developed for managing risks and exposures.
- Written and comprehensive policies and procedures for communication with external parties had not been established.

Without a set of written or comprehensive policies and procedures, it is not possible to provide clear guidance to staff members who handle daily operations and therefore increases the risk that established practices are not properly communicated and adopted consistently. Such policies and procedures should

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be communicated to staff who should be asked to acknowledge receipt of the written policies and procedures. In addition, policies and procedures should be reviewed and updated on a regular basis to ensure that they remain valid and are adapted to reflect any business and system changes.

These measures will help to follow through the established practices, support consistencies and improve the effectiveness of the Company's internal controls and its ability to promote a culture of strong internal control.

### **(iii) AML Policies**

The Company had not conducted a money laundering and terrorist financing risk assessment to determine appropriate enhanced due diligence and monitoring procedures for higher risk customers, business relationships, and transactions as required by the Prevention of Money Laundering and Terrorist Financing Guidance Note (the "AML Guidance Note") adopted by the SFC in April 2006. Furthermore, the then AML policies were incomplete and were missing several critical elements such as screening applicants for business against lists of individuals and entities associated with terrorist financing, United Nations sanctions and politically exposed persons ("PEPs") and conducting the necessary ongoing monitoring to identify suspicious transactions in order to satisfy its legal obligations.

The Company should conduct an assessment of the anti-money laundering ("AML") risks in its business. From this assessment, the Company should define higher risk customers, and implement and document appropriate enhanced due diligence measures for these higher risk activities customers. The revised policies and procedures should be effectively communicated to all employees.

The Company should conduct thorough background checks on its clients as part of its customer due diligence process to identify applicants for business and transactions involving financial criminals, PEPs, and terrorist suspects and sanctioned individuals specified in Gazette notices or other lists circulated by the SFC.

Monitoring activities and systems should be implemented for ongoing monitoring of accounts and transactions to identify suspicious activities for reporting to the Joint Financial Intelligence Unit.

The Company should conduct a periodic review of its AML Policies and controls to ensure they are up to date and effective. This function could be carried out by the internal audit department.

The record keeping and retention procedures should consider measures to facilitate investigation by the law enforcement agencies.

Staff training should be enhanced to ensure that staff understands the AML issues specific to their roles within the Group.

### **(iv) Business plan and risk assessment mechanism**

A formal business plan and risk assessment program had not been formally established for monitoring business performance and operational issues. Without a business plan, the Company may not be able to achieve its overall business goals and effectively manage the operations. Further, without a risk assessment mechanism, management may not be able to effectively handle the changes in market conditions.



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### **(v) Segregation of duties**

The senior compliance manager also acted as the head of credit risk control department to approve credit limit to margin clients and monitor the accounts balances on a daily basis. The compliance function was not segregated nor was it independent from the operations. Moreover, the Company had not developed written job descriptions for all functions, including dealing, settlement, accounting, credit risk monitoring and market research.

The Company should segregate compliance function from operations. In addition, written job descriptions should be developed and communicated to all employees.

### **(vi) Business continuity planning and information system**

The Company shared with its holding company, EIHL, the email server and internet access system. However, with the strict requirements of the Stock Exchange (such as dealing with price sensitive information), the Company should consider separating its information technology system from EIHL to safeguard the leakage of important information.

In addition, the Company did not have its own business continuity plan (“BCP”) to handle potential issues and losses upon possible occurrence of disastrous events and/or system failures. The Company should consider developing a comprehensive, up-to-date and fully tested BCP for its own use.

### **(vii) Compliance with the policies and procedures, relevant codes, guidelines or rules**

The Company did not properly perform certain control procedures, which may lead to non-compliance with the requirements of the Code of Conduct and the FRR, for example:

- Time of cancellation of order was missing on the order ticket for a securities transaction.
- Comparison result of daily liquid capital against the liquid capital stated in the last return submitted to the SFC was not documented.
- Mail list for monitoring the mailing status of each futures account was not maintained.
- List of associated accounts (i.e. accounts associated with staff) was not maintained by the relevant parties for monitoring purpose.

Control procedures not properly executed may lead to non-compliance with the Code of Conduct, or other relevant guidelines and rules, exposing the Company to risk of reprimand by the SFC.

The Company should remind its employees and account executives to follow and comply with the stipulated procedures, relevant codes, guidelines or rules.

### **(viii) Documentation and audit trail**

There were a number of areas in which documentary evidence of the performance of control procedures or of management's review and approval was not maintained.

Lack of audit trail for the Company's operations and transactions makes it difficult to prove that required procedures are properly performed.

The Company should document the actions taken or maintain proper records in order to strengthen the controls over documentation and audit trail.

### **(ix) Evidence of review and approval**

It was noted in the First Review that documentary evidence of management's review and approval was not maintained in certain areas.

Without proper evidence of review and approval of the performance of controls and of controls-related decision-making, management's ability to effectively assess whether the Company's internal controls are operating as intended is hindered. Furthermore, managements' ability to assign accountability to individual responsible for performing and reviewing internal controls and for making controls-related approvals is also impaired.

The Company should emphasise the importance of producing and maintaining written evidence for the review and approval of controls. This should be communicated to all employees, including by making explicit the responsibility for these activities in the formal written policies and procedures which the Reviewing Firm recommend should be established.

## **(B) The Second Review and the Final Review**

Emperor Securities and Emperor Futures have largely taken up the recommendations made by the Reviewing Firm in the First Report. The Reviewing Firm has performed the Second Review and the Final Review on, among others, the remedial work performed by the management of the Group on the significant internal control weaknesses identified in the First Review. The following summarises the remedial work done by the Group and the findings and recommendation, if any, made by the Reviewing Firm following the Second Review and the Final Review as set out in the Second Report:

### **(i) Corporate governance structure**

Members of both the audit committee and remuneration committee have been identified and the two committees were established on 1 March 2007.

Terms of reference of both the audit committee and remuneration committee were established and induction training on the authority and responsibilities of the audit and remuneration committees to their respective members has been conducted.

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The Company has set up its own internal audit department which shall report to the audit committee directly. Audit program has been developed and will be updated for future audits which are planned to be performed three times a year. Audit reports will be issued to document the audit findings and to obtain management responses.

**(ii) Written policies and procedures**

The Company had established and documented most of the policies and procedures, failings of which were identified as significant weaknesses in the First Review. For example:

- a new section on ethical principles is included in the account executives handbook.
- crisis management procedures for securities accounts during adverse market conditions were documented in the operational manual.
- the Company has adopted written human resources policies and procedures which cover, among others, training and development.
- the Company had set out and documented the enterprise-level risk management policies which address the issues relating to, for example, provision of new products or services, proprietary trading and changes of legislation, rules and regulations.
- the Company had established policies for communicating with external parties, handling of price sensitive information and responding to enquiries from regulators.

After performing the Second Review, the Reviewing Firm noted that the newly established enterprise-level risk management policies and procedures were not comprehensive. For example, it has not provided for setting up of a risk management committee to monitor the implementation of the established risk management policies and procedures. Subsequent to the Second Review, the Company has further enhanced its policies to include setting up of a risk assessment committee. The risk management committee comprises department heads from the credit risk control department, accounts department, compliance department, dealing department, settlement department, internal audit department and marketing administration department. The Company does not consider it necessary to commission the Reviewing Firm to perform further review on the above. However, the Company places emphasis on risk management and regards it as an on-going activity and is committed to improve and strengthen its risk management policies with reference to changing risk profile and market developments.

Similarly, after performing the Second Review, the Reviewing Firm noted that although the Company has established policies for communicating with external parties, handling and responding to enquiries from regulators, policies relating to dispute resolution, directors' responsibility to maintain confidentiality and review of exceptions to procedures were not included. Subsequent to the Second Review, the management has further revised the policies to include the above areas. The Reviewing Firm has performed review on the above policies and has not identified any further significant weaknesses in this area in the Final Review.

### (iii) AML Policies

Subsequent to the First Review, Emperor Securities and Emperor Futures have made numerous revisions to their AML Policies culminating in the establishment of a new policy statement and related procedures. In addition, Emperor Securities and Emperor Futures have conducted a money laundering and terrorist financing risk assessment to determine appropriate enhanced due diligence and monitoring procedures for higher risk clients, business relationships, and transactions as required under the AML Guidance Note.

However, the Reviewing Firm noted that the following areas still require further refinements and improvements:

- Although information on client profiling including the source of funds, purpose of account, funds flow is obtained on account opening, the information collected is not used to create a profile of expected activity for a client account for the purpose of ongoing due diligence and scrutiny of clients' transaction.

Subsequent to the Second Review, the Company has further revised its policies to include creating a profile of expected activity for a client account for the purpose of ongoing monitoring of the trading activities of the client. This policy has been reviewed by the Reviewing Firm during the Final Review on 2 January 2007. The Reviewing Firm noted that further refinement can be made. For example, the Company should specify in the operation manual the purpose of the client profiling procedure, the details of the procedure to create client profile and the client information to be collected.

The Reviewing Firm has conducted a further review on 4 January 2007 which formed part of its Final Review on the prevailing AML Policies in respect of creating a client profile including creating a profile of expected activity for a client account. No further comment was made by the Reviewing Firm.

- Specific customer due diligence measures for financial and/or professional intermediaries, trusts and non-face to face clients have not been adopted.

Subsequent to the Second Review, the Company has further revised the customer due diligence policies and procedures for non-face to face, trust, financial and professional intermediaries. The Reviewing Firm has during the Final Review reviewed the revised policies and procedures and noted that Emperor Securities and Emperor Futures have adopted policies not to accept accounts from trust, professional intermediaries and foreign financial intermediaries and have refined procedures on client identification for non-face to face accounts. In respect of the non-face to face accounts, no further comments was made by the Reviewing Firm.

- Minimum standards of suitability and competency for key AML sensitive positions have not been specified.

Subsequent to the Second Review, the Company has specified standards of suitability and competency for key AML sensitive positions.

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During the Second Review on 8 December 2006, the Reviewing Firm conducted a walkthrough of applicable AML procedures that had been implemented after the AML Policies were established on 5 December 2006. The walkthroughs were performed on the following transaction samples:

- Two sample transactions of account opening procedures for private individuals who were classified as non-high risk in accordance with the AML Policies;
- One sample transaction of the account opening procedures for a corporate account that was classified as high risk in accordance with the AML Policies;
- One sample transaction of a large cash deposit log; and
- Two sample transactions of the cash deposit procedures including the sample of a large cash deposit log above.

Similarly, findings from the Reviewing Firm during the walkthrough indicated the need for further refinement in the implementation of the policies and procedures in areas, such as:

- Procedures and documentation standards for establishing and verifying the source of funds/wealth for client accounts;
- Procedures to conduct and to evidence background checks. For example, in the walkthrough sample, the background check was only applied to the 51% shareholder and not the other two shareholders holding 20% and 29% of the issued share capital of a corporate client; and
- Procedures to document the identification of the depositors making cash deposits into client accounts.

The Directors take the view that as the AML Guidance Note is recently promulgated, the Group would need time to continue to refine its AML Policies and improve the effectiveness in their implementation, for example by continuous training.

### **(iv) Business plan and risk assessment mechanism**

The Reviewing Firms noted that requirements for drawing up business plan have been established for monitoring business performance and operational issues. However, the newly established risk assessment policy was not comprehensive to include the approach and methodology for execution of such policy. Subsequent to the Second Review, the Company has revised its policies to include the approach for risk assessment.

### **(v) Segregation of duties**

The compliance department and credit risk control department are now segregated and headed by different personnel. Key written job descriptions have been developed and communicated to all staff.

**(vi) Business continuity planning and information system**

The Company has established its own business continuity plan to demonstrate the handling procedures for the occurrence of disastrous events and/or system failures focusing on the operations of Emperor Securities and Emperor Futures. Passwords are used to protect the files with non-public price sensitive information.

**(vii) Compliance with the policies and procedures, relevant codes, guidelines and rules**

The Company has strengthened its procedures to comply with the requirements of the Code of Conduct and the FRR, such as time record of cancellation of order, documentation of comparison results of daily liquid capital, maintenance of mailing list and list of associated accounts.

**(viii) Documentation and audit trail**

It was noted in the Second Review that the Company has maintained documents and records for daily operations and transactions executed for clients as audit trail.

**(ix) Evidence of review and approval**

It was noted in the Second Review that written evidence of management's review and approval of controls and controls-related decision-making has been maintained.

Save as disclosed above, the Reviewing Firm is satisfied that the remedial measures as recommended have been taken up by the Company to address the significant weaknesses identified by the Reviewing Firm in the First Report and the Second Report.

The Directors are of the view that after effecting the remedial work on the significant weaknesses identified by the Reviewing Firm in the First Report and the Second Report, the current control systems of Emperor Securities and Emperor Futures have been significantly enhanced and are effective to enable the Group to, among others, carry out business in an orderly manner and to safeguard its and clients' assets. The management of the Group would oversee the effective implementation of the internal control systems. However, many of the control systems adopted by Emperor Securities and Emperor Futures have a short period of implementation and their effectiveness in implementation is yet to be proven. Further refinement may be required and the management is committed to perform review of the control systems from time to time to further improve their effectiveness. Internal controls, no matter how well designed and operated, can provide only reasonable assurance of achieving an entity's control objective. The likelihood of achievement is affected by limitations inherent to internal control. These include the realities that human judgement in decision-making can be faulty and that breakdowns in internal control can occur because of human failures such as simple errors or mistakes. Continuous training would be conducted to increase the acceptance of the newly and significantly changed control systems and policies. Additionally, controls, whether manual or automated, can be circumvented by the collusion of two or more people or inappropriate management override.

### CURRENT INTERNAL CONTROL SYSTEMS

The following depicts the current internal controls on the Group's major operating areas:

#### **Operational Controls**

##### *1. Segregation of duties and functions*

Key duties and functions are appropriately segregated, particularly those duties and functions when performed by the same individual may result in undetected errors or may be susceptible to abuses which may put the interest of the Group or its clients at risk.

The Group's settlement and accounting functions are separated from its sales and dealing functions. The Group's compliance and credit risk control functions are now separated. The Group has recently established an internal audit department which shall report to the audit committee directly. The Group has segregated reporting line for the staff of each of the settlement, accounting, compliance, credit risk control, account executives, dealing and personnel functions.

The Group has policy on handling price sensitive information. Financial information is handled by the accounts department. Non-public price sensitive information has to be sent by way of password protected file attachments. The Group has its own trading and settlement computer systems which serve to better protect client information. Policy on handling confidential information has been established and communicated to staff. Staff members shall not copy or divulge any price sensitive or confidential information to any person or entity other than those who have a need to know.

##### *2. Opening and handling of client accounts*

Account opening procedures are documented. Information in the account opening form is independently verified by the marketing administration department by tape recorded phone. The Group retains all relevant client information, signature specimens of the clients, and other documentation.

The account executives are requested to ensure that clients are provided with adequate information about the Group and the services to be provided to the clients, together with other relevant documents such as relevant risk disclosure statements, and the nature and scope of fees, penalties and other charges that the Group may charge.

Staff members of the Group are not allowed to open trading accounts with other licensed corporation except with approval from senior management. The staff members are also required to report any accounts maintained by their associates to the Group. The list of associated accounts is updated by the marketing administration department and doubled checked by the credit risk control department. The above list is forwarded to the respective department heads for monitoring and reference.

No staff or director of other licensed corporation is allowed to open an account with the Group unless that licensed corporation has given its written consent.

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The Group provides margin financing services to margin clients to facilitate acquisitions or holdings of listed securities. The Group has adopted a credit evaluation procedure which takes into account both “tangible” and “intangible” factors in assessing clients’ credit worthiness. The credit risk control department will review the relevant client information prior to proposing a credit or trading limit for approval by the responsible officer or senior management.

### 3. *Potential conflict of interest*

The Group has internal control measures to avoid conflict of interest in transactions involving senior management or directors of the Group. Any member of the senior management or directors of the Group who are involved in decision making process (for example, approving credit limit or deciding on whether to give tolerance to clients who fail to meet margin calls within the prescribed time limit) shall not participate in the approval process for matters involving that person’s staff or associated accounts or client accounts of which he/she is the handling account executives. In addition, pursuant to the bye-laws of the Company, a Director shall not vote (nor be counted in the quorum) on any resolution of the Board approving any contract or arrangement or any other proposal in which he or any of his associates is materially interested.

### 4. *Dealing practices*

Staff members of the Group are allowed to open trading accounts with the Group if approval from senior management is obtained. The responsible officers or designated persons in the dealing department will perform random checks on a daily basis of the staff accounts and report any irregularities to senior management.

Staff members shall not deal in any securities based on the information obtained in connection with their employment. Staff members shall not deal in any securities which is on the Group’s restricted dealing list.

Order handling procedures are documented. Prior to executing a client order, account executives have to check the status of the account, sufficiency of available funds or available credit or the sufficiency and availability of securities (as the case may be). Orders shall, where possible, be received through tape recorded telephone system and time-stamped promptly upon receipt and are required to be transmitted to the dealing room immediately. All telephone conversations between account executives and dealers shall be tape recorded and records are kept for at least three months. Dealers have to handle clients’ orders fairly and in the order in which they are received. Immediately after execution of an order, dealers have to fill in a buy/sell ticket and forward it to the settlement department for inputting into the settlement system. The settlement department shall match the data in the settlement system with the trade records received from the clearing houses on the same day.

### 5. *Error trading account and proprietary trading*

Error trades usually arise from mistakes made by staff on data input or incorrect recording of clients’ instructions. Error trades are usually discovered (i) when the relevant dealer confirms the trade with the account executive; or (ii) when account executive confirms the trade with client; or (iii) when the settlement department matches trade records inputted into the Group’s settlement system with that



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received from the clearing houses; or (iv) when the dealing department matches its buy/sell tickets against those prepared by the account executives. Upon discovery of any error trade, the designated person in the dealing department or the responsible officers will be informed immediately and appropriate remedial action will be taken. Monthly report on error trades will be prepared for senior management's review.

The Group currently is not engaged in any proprietary trading activity. Proprietary trading activities, if any, will be subject to trading limits approved by the Directors.

### 6. *Settlement and asset protection*

Clients' signatures on settlement instructions are verified by the credit risk control department. The settlement department will also reconcile the settlement information from clearing houses with the Group's internal record on every trading day.

The settlement department sends daily and monthly statements to clients at their reported addresses. Under no circumstances shall the statements be delivered to clients through account executives. The daily and monthly statements of clients with specific hold mail instructions are kept at the settlement department. Clients or the clients' authorized persons who choose to collect the statements in person are required to acknowledge receipt of the statements. The Group confirms with the clients on an annual basis whether they wish to revoke the hold mail authorization.

Account executives cannot access the settlement system to amend the daily and monthly statements. The Group keeps the client information in the settlement system which access is limited to authorized persons with proper password. For change of account information, clients are required to complete the change of account particular form and provide proper supporting documents. Only authorized persons have access to update and amend the client information kept in the settlement system and the credit risk control department will double check the amended information to ensure that the information is correctly updated.

In compliance with the Securities and Futures (Client Securities) Rules, the Group maintains segregated stock accounts with CCASS for custody of clients' securities. The settlement department will reconcile the securities held under the Group's custody on behalf of clients with the balances of the Group's CCASS stock accounts and physical scrip on a regular basis. Client monies are maintained in segregated accounts with licensed banks in Hong Kong in accordance with the Securities and Futures (Client Money) Rules.

Clients can make payments into their client accounts by crossed cheque, cash, direct bank deposit or transfer. No matter which mode of payment clients choose to use, clients shall provide sufficient evidence to show that the payment has been made; failing which, the Group will temporarily treat the deposits as unidentified deposits. Follow-up actions would be taken by the settlement department to ascertain the identities of the depositors. If the deposit remains unidentified for more than three months, the accounts department would request the payee details via the receiving bank and take appropriate actions.

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The Group has informed its account executives that third party payment is discouraged and acceptance is subject to approval by management. Third party payment also requires the acknowledgement from the client and disclosure of the relationship between the client and the third party.

All cheques to clients must be crossed and issued in the name of the client. Cheques to third party may be allowed at client's request subject to senior management's approval.

In case of deposit of physical scrip which was not registered under the client's name, the client is required to produce the bought and sold note or other documents issued by a licensed broker for the settlement department to verify the ownership. Without the relevant supporting documents, the settlement department will reject the deposit request.

Client requesting a withdrawal of stock in the form of physical scrip shall sign a delivery order and forward the request to the settlement department. When the physical scrip is available, the settlement department will inform the account executive to notify the client to collect the stock. If the scrip is not collected within 5 business days, the settlement department will contact the client directly and request the client to collect the stock as soon as possible. If the scrip is not collected within one month, the settlement department will re-deposit the stock with CCASS.

### 7. *Complaints from clients*

The Group has newly established policies and procedures to ensure proper handling of complaints from clients and that appropriate remedial action shall be taken promptly. Clients may lodge complaints via a designated tape recorded hotline printed on the client statements. Any complaint made through the hotline will be handled by the compliance officer who will document the communication in writing. Pursuant to the Group's policy, the compliance officer has to enquire into the complaint and perform preliminary investigations to understand the facts surrounding the complaint within 10 business days. Upon completion of the fact finding, the compliance officer will report the complaint findings to senior management and write to the client about their findings. Senior management will review findings on each complaint and determine whether any enhancement of the Group's internal control and operation procedures or other appropriate action is required.

### 8. *Anti-Money Laundering*

The Group has implemented policies and procedures to prevent money laundering and terrorist financing. Recently, the Group has made numerous revisions to its relevant policies and procedures culminating in the establishment of a new policy statement and related procedures. The Group has a money laundering and terrorist financing risk assessment system to determine appropriate enhanced due diligence and monitoring procedures for higher risk clients, business relationships, and transactions as required under the AML Guidance Note. However, the Directors take the view that as the AML Guidance Note is recently promulgated, the Group would need time to refine its AML Policies.

### **Risk management**

The Group has policies and procedures to ensure the proper management of risks to which the Group and, if applicable, its clients are exposed, particularly with regard to their identification, whether financial or otherwise, and the provision of timely and adequate information to management to enable it to take appropriate and timely action to contain and otherwise adequately manage such risks.

The Group's risk policies and measurements and reporting methodologies are subject to regular review, particularly prior to the commencement of the Group's provision of new services or products, or when there are significant changes to the products, services, or relevant legislation, rules or regulations that might impact the Group's exposure.

#### *1. Credit risk*

The Group has established policies and procedures to evaluate the financial and other information of the client, including but not limited to tax return, bank statement, employment status, prior to approving client's credit limits. Senior management or Board approval is required for higher level credit limits. The credit limits of clients will be monitored by the credit risk control department from time to time and they are subject to annual review.

The basis for credit review largely follows that for approval of credit limits. In the case of credit review, reference will also be made to the clients' trading and margin call records maintained by the Group.

The credit risk control department will on every trading day compile a list of outstanding loans which are secured by securities representing more than 1% of the total market value of the collaterals held by Emperor Securities. Such list shall be reviewed by a responsible officer or the senior management of the Group. The responsible person shall review the situation and, if needed, take appropriate action, which may include shortening the time given to clients to meet margin calls and/or adjusting downwards the margin ratio for collateral that are classified as high concentrated pledged securities.

The credit risk control department will also, on every trading day, compile a list of outstanding loans which represent more than 5% of the Group's daily trade receivables for review by the responsible officer or the senior management. The responsible person shall review the situation and, if needed take appropriate action, which may include reducing the credit limit of the client and/or shortening the "tolerance" period given to the client to meet outstanding margin calls.

The Group has a list of securities approved as acceptable collaterals with different margin ratios. The research team of the Group shall review and make recommendation on margin ratio for these securities monthly. In addition, the credit risk committee and the head of the research team will review the Group's collateral policy, including the list of securities approved as collateral and their margin ratio, bi-annually.

The credit risk control department and the responsible officers hold regular meetings on a weekly basis to review margin call records of clients. The credit risk committee will meet bi-monthly to review margin calls and newly granted credit limit exceeding a pre-determined limit to see whether the Group's margin call and forced liquidation policy and credit assessment procedures are properly followed. The credit risk committee will also review the margin lending, margin call and collateral policies bi-annually to determine areas for further refinement.

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In addition, the internal audit department will also perform periodic review to ensure that the margin lending, margin call and liquidation policies and procedures of the Group are properly followed. In cases where judgement is made by management in executing the Group's policies, the internal audit department shall refer the case for consideration by the audit committee if the internal audit department has doubt on the justification given by the management.

For granting loans and advances, approval from senior management is required. Senior management will make reference to the quality of the securities pledged and/or other collaterals given to determine the terms of loans and advances. Senior management will review the settlement records of the loans and advances on a monthly basis.

### 2. *Market risk*

The Group has risk management measures to quantify the impact to the Group and its clients from changing market conditions. Management will regularly review the Group's balance sheet, profit and loss accounts and credit granted to clients to identify the risk exposure of the Group, especially during adverse market movements.

During trading hours, the credit risk control department and the dealing department will monitor the trading activities of the clients. If the client's credit limit is exceeded, unless with senior management approval for special tolerance, the Group would freeze the clients account until it falls within the approved credit limit. The credit risk control department will also monitor the 20 securities with the highest losing percentages and stocks classified as highly concentrated collaterals of the Group. Follow up action such as reducing the margin ratio for the pledged securities and requiring clients to top up their position would be taken if needed.

Margin calls would be made to clients by the handling account executives if the outstanding loan balances exceed the margin value of clients' portfolio (in the case of securities accounts) or when outstanding balances in his accounts fall below the required maintenance margin level (in the case of futures account). If the client's position fall below the Group's pre-defined level, the Group would liquidate the client's position, unless special tolerance from senior management is given.

In respect of a client's position in foreign currencies, client's margin deposits will be converted into the corresponding foreign currencies so as to minimize the risk of fluctuation in foreign exchange rate to the Group.

### 3. *Liquidity risk*

The above policies for monitoring of concentrated stock also assist the Group to manage its liquidity risk.

The liquid capital of Emperor Securities and Emperor Futures is computed by the accounts department daily in order to fulfill the requirements of the SFC. The accounts department also reviews the Group's liquidity position daily and ensures that it is adequate for the projected funding demand.

### 4. *Operational risk*

Management regularly reviews the Group's operations to ensure that the Group's risk of losses, whether financial or otherwise, resulting from fraud, errors, omissions and other operational and compliance matters, are adequately managed.

The Group has also established its own business continuity plan to protect the Group from risk of interruption to its business continuity.

### **COMPLAINTS RECEIVED BY THE GROUP**

Emperor Securities and/or Emperor Futures received in total six complaints since 1 April 2003 up to the Latest Practicable Date, details of which are summarised as follows (except for two complaint cases which are summarised in the section headed "Pending investigation cases instituted by the SFC" above):—

- (i) On 6 January 2004, a client of Emperor Futures opened two futures contracts with Emperor Futures. By a circular of the HKCC dated 16 January 2004, the margin requirements of futures contracts' open position were temporarily increased during the period from the commencement of trading on 20 January 2004 until the commencement of trading on 26 January 2004. During the trading hours on 21 January 2004, the aggregate of the account balance and the unrealized loss of the outstanding futures contracts maintained in the account of the client fell below 80% of the increased margin requirement. The account executive then made a margin call to that client. That account executive recalled that in the same telephone conversation, he had also informed the client of the new margin requirement. The client then informed the account executive that he could not top up his account to meet the new margin requirement and he instructed the account executive to close the positions on that day. The client complained to the account executive as regards the delay in being notified of the new margin requirement. On 10 February 2004, Emperor Futures informed the client that after its investigation, no negligence was found committed by the account executive causing damages to the client and the margin call was made pursuant to the margin policy set by Emperor Futures from time to time. Emperor Futures received no further complaint from that client.
- (ii) During the trading hours on each of 11 March 2004 and 20 April 2004, the aggregate of the account balance and the unrealized loss of the outstanding futures contracts maintained in the account of a client of Emperor Futures (who was Emperor Futures' company client and whose account was handled by house team) fell below 80% of the margin required on the respective days. Members of the house team then made margin calls to that client. However, the client did not top up his then account balance to meet the respective margin requirements. On both 12 March 2004 and 21 April 2004, the aggregate of the account balance and the unrealized loss of the outstanding futures contracts in that client's account further fell below 50% of the margin required. Emperor Futures then executed forced liquidation of his futures contracts on 12 March 2004 and 21 April 2004 respectively in accordance with Emperor Futures' then margin policy. The client complained to Emperor Futures regarding the above

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forced liquidations of his futures contracts. Emperor Futures explained the margin call and forced liquidation policies effective at the material time to the client. No further complaint was received from that client after the explanation given to him.

- (iii) On 25 February 2006, a client wrote to Emperor Securities complaining that the daily statements of his account dated 22 February 2006 and 23 February 2006 did not accurately record his stockholding as at the above dates. Daily statements of client accounts were printed from data base maintained in the settlement system which was developed and maintained by an external consultant. After enquiry with that system vendor, it was ascertained that the error in the above client's statements arose from a system report printing bug that was found in the client statement printing function. Such system printing bug was then immediately fixed. Emperor Securities had also carried out checking to double check the exact holding of the client at the relevant dates and to verify that the data as contained in its settlement system was accurate. On 28 February 2006, Emperor Securities wrote to the client to explain the inaccuracy on the printed client statements. The client was also informed that his handling account executive had kept an accurate and detailed report of his investment portfolio and could verify the position of his account with him whenever he wanted to place order with Emperor Securities.

Emperor Securities did not receive any further complaint from that client. Emperor Securities had also performed checks through the system vendor to confirm that no other daily client statements had similar inaccuracies.

- (iv) On 19 August 2006, a client called the ex-senior compliance manager of Emperor Securities about the following conduct of the account executive who served her account:
- Selling some shares (the "Subject Stock") in the client's account on 22 May 2006 without obtaining prior authorization from the client;
  - Being constantly unavailable for contact; and
  - Delay in processing withdrawal of the client's share certificates from the client's account as per her request.

On 11 September 2006, that client sent Emperor Securities a complaint letter (the "Letter") in respect of above complaints. She also requested in the Letter a detailed summary of her investment activities through Emperor Securities. On 11 September 2006, Emperor Securities sent to the complainant copies of all the monthly statements of her account which indicates her trading activities carried out through the securities account maintained with Emperor Securities. On 13 September 2006, Emperor Securities acquired from the Stock Exchange the same quantity of the Subject Stock to restore the client's position. Emperor Securities had also arranged withdrawal of the physical share certificates from the client's account as per her instruction. The client acknowledged that the unauthorized trading done by the relevant account executive of Emperor Securities was carried out in good faith and not with malicious intent nor for the purpose of obtaining personal benefit and confirmed that she would not take further action against that account executive. On 20 September 2006, Emperor

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Securities issued a warning letter to that account executive. In reaching that decision, Emperor Securities has taken into consideration of the account executive's previous clean record and that he obtained no personal benefit from the unauthorized trading. On 7 November 2006, Emperor Securities reported this incident to the SFC.

### CONNECTED TRANSACTIONS

The Group has entered into certain agreements and arrangements with its connected persons in the ordinary and usual course of business of the Group during the Track Record Period. Some of these transactions have ceased and some of them are expected to continue after the listing of the Shares on the Main Board of the Stock Exchange. Details of these transactions are as follows:

### DISCONTINUED CONNECTED TRANSACTIONS

#### 1. Corporate guarantees and securities granted by Emperor Group in favour of the Group

During the Track Record Period, EIHL or its various subsidiaries had provided corporate guarantees or pledges against their properties to secure the repayment obligations under the loans and credit facilities advanced by financial institutions to members of the Group.

As at the Latest Practicable Date, the above arrangements have been terminated and the Group's banking facilities are no longer subject to any guarantees or securities given by the Emperor Group.

#### 2. Financial assistance from connected person

Pursuant to an agreement dated 1 March 2004 ("Subordinated Loan Agreement") made between Emperor Securities, Distinct Rich Limited (a wholly owned subsidiary of EIHL) and the SFC, Distinct Rich Limited agreed to extend a revolving credit facility of HK\$220 million to Emperor Securities for a term of two years commencing from 1 March 2004. This loan (the "Subordinated Loan") is unsecured and bears interest at prime rate as quoted from time to time by The Hongkong and Shanghai Banking Corporation Limited which, in the opinion of the Directors, is comparable to the market rate. The Subordinated Loan has been used to fund the initial public offer loans extended to clients and/or meet the FRR requirements for the initial public offer financing business of Emperor Securities. As approved by the SFC on 27 February 2006, the expiry date of the Subordinated Loan Agreement was extended to 29 February 2008.

The maximum amount of the Subordinated Loan during each of the three years ended 31 March 2006 and nine months ended 31 December 2006 were HK\$5 million, HK\$180 million, HK\$170 million and HK\$200 million respectively. The amount of loan interests paid in respect of the Subordinated Loan for each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 were approximately HK\$21,000, HK\$1,626,000, HK\$5,337,000 and HK\$3,227,000 respectively.

On 31 March 2007, the Subordinated Loan Agreement was terminated by mutual agreement between the parties thereto and the parties have confirmed that their respective rights and obligations under the Subordinated Loan Agreement were released and discharged without liability.



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### **3. Introduction fee**

During the year ended 31 March 2004, Emperor Securities paid an introduction fee of HK\$1.2 million to Emperor Finance Limited (“Emperor Finance”), a wholly owned subsidiary of EIHL, for introduction of a term loan client to Emperor Securities. This transaction is a non-recurring event and no new client has been introduced by Emperor Finance to Emperor Securities since then.

### **4. Commission or fee paid to Emperor Group for their acting as sub-underwriters or placees**

During the year ended 31 March 2004, certain wholly owned subsidiaries of EIHL had acted as sub-underwriters or placees for the securities underwritten or placed by the Group, for which they received commission or fee totalling approximately HK\$566,000. The above transactions are on normal commercial terms and at rates no more favourable than those offered by the Group to Independent Third Parties. After the listing of the Shares, the Emperor Group and its associates will not act as sub-underwriters or placees for securities underwritten or placed by the Group.

## **EXEMPT CONTINUING CONNECTED TRANSACTIONS**

### **1. Sharing of administrative services**

The Emperor Group is currently providing administrative and back office support services to the Group and is charging on a cost basis.

The administrative and back office support services provided by the Emperor Group includes information technology support, internal audit, human resources, management and administrative services.

The costs shared between the Group and the Emperor Group included (i) salaries, bonus, provident funds and other related expenses for the staff members of the Emperor Group who are involved in providing information technology support, internal audit, human resources, management and administrative services to both the Group and the Emperor Group and (ii) other expenses which were incidental to the carrying out of the above services such as telecommunication, utilities, printing and stationery etc. The above costs are shared between the Group and the Emperor Group, based on actual usage such as utilisation of staff time or number of head count providing the service.

The Directors consider that the basis of cost allocation of office administrative and back office support services between the Group and the Emperor Group is fair and equitable.

The fees borne by the Group for administrative and back office support services provided by the Emperor Group amounted to approximately HK\$1,346,000, HK\$2,050,000, HK\$1,389,000 and HK\$923,000 respectively for each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 and principally comprise fees charged for the information technology support services and management support provided by the Emperor Group. The Group has put in place new computer systems in several phases between November 2004 and February 2005 resulting in an increase in service fees paid to the Emperor Group for the information technology support services provided during the financial year ended 31 March 2005.



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The Group has recently established its own internal audit department and the Emperor Group has ceased to provide the above service to the Group. During the three years ended 31 March 2006 and up to 30 September 2006, Mr. Chan Pak Lam, Tom was employed by EIHL and part of his salaries during that period was re-allocated to the Group as management fee. On 1 October 2006, Mr. Chan Pak Lam, Tom entered into a full time employment contract with the Group. Other administrative and back office support services will continue and the basis of sharing will remain the same as it is now after the listing of the Shares.

Immediately after the EIHL Distribution and the Share Offer, Charron will become the controlling shareholder of the Group. Charron is also the controlling shareholder holding approximately 57.55% equity interests in EIHL as at the Latest Practicable Date. Accordingly, EIHL and its subsidiaries will upon listing of the Shares be classified as connected persons of the Company under Chapter 14A of the Listing Rules.

Sharing of administrative and back office support services on a cost basis with the Emperor Group will, upon listing of the Shares, constitute continuing connected transactions of the Company under Rule 14A.14 of the Listing Rules, but will be exempted from the reporting, announcement and independent shareholders' approval requirements applicable to continuing connected transactions under Rules 14A.33(2).

### **2. Directors' financial services**

During the Track Record Period, the Group had provided financial services including (i) brokerage services for securities, futures and options trading; and (ii) margin and initial public offer financings to the directors of the Group, a former director (the "Former Director") of the Group whose employment was ceased within the preceding 12-month period and their respective associates on normal commercial terms and at rates comparable to those charged to Independent Third Parties. After the listing of the Shares, the Group will continue to provide the aforesaid financial services to the directors of the Group, the Former Director and their respective associates. During the Track Record Period, the Group had procured the directors of the Group, the Former Director and their respective associates to act as sub-underwriters and placees for securities underwritten and placed by the Group. Up to the Latest Practicable Date, none of the independent non-executive Directors had maintained any accounts with the Group. Financial services provided to Ms. Daisy Yeung (as managing Director) and Mr. Lee Wai Shing (a director of a subsidiary of the Company) will be conducted pursuant to the respective agreements entered into with them on 2 April 2007 (details of which are set out in the sub-section headed "Non-exempt continuing connected transactions" in this section). Ms. Daisy Yeung and her associates are collectively referred to as the "Yeung Family", and Mr. Lee Wai Shing and his associates are collectively referred to as the "Lee Family".

Upon listing of the Shares, the directors of the Group, the Former Director and their respective associates will become connected persons of the Company. As such, the provision of the aforesaid financial services and the payment of commission and fee to the directors of the Group, the Former Director and their respective associates will constitute continuing connected transactions of the Company under Chapter 14A of the Listing Rules.

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- (i) *Commission and interest income received from the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family)*

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2006, income received from the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) represented commission charged for the brokerage services for securities, futures and options dealings and interest income for margin or initial public offer financings provided by the Group and the amounts were set out as follows:

Financial services	For the year ended 31 March		For the nine months ended 31 December	
	2004 HK\$	2005 HK\$	2006 HK\$	2006 HK\$
Commission and brokerage on dealing in securities and equity options	116,490	211,540	72,270	84,760
% to the Group's turnover from dealing in securities and equity options	0.36%	0.67%	0.22%	0.27%
Commission and brokerage fee from dealing in futures and index options contracts	41,940	23,230	2,580	0
% to the Group's turnover from dealing in futures and index options contracts	0.92%	0.88%	0.02%	0.00%
Interest income from margin financing	61,930	24,580	5,120	310
% to the Group's turnover from margin financing	0.92%	0.45%	0.06%	0.00%
Interest income from initial public offer financing	16,890	3,160	5,750	740
% to the Group's turnover from initial public offer financing	0.61%	0.09%	0.04%	0.00%
Total	<u>237,250</u>	<u>262,510</u>	<u>85,720</u>	<u>85,810</u>
% to the Group's total turnover	<u>0.33%</u>	<u>0.38%</u>	<u>0.09%</u>	<u>0.09%</u>

- (ii) *Margin and initial public offer financings provided to the directors of the Group, the Former Director and their associates (other than the Yeung Family and the Lee Family)*

During the Track Record Period, the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) had maintained margin accounts with the Group and obtained initial public offer and margin financings from the Group.

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The maximum amounts of margin loans advanced by the Group to the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) were approximately HK\$2,584,990, HK\$2,170,110, HK\$908,850 and HK\$255,480 respectively during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006.

The amounts of margin loans advanced by the Group to the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) were approximately nil, HK\$2,070, nil and nil respectively as at 31 March 2004, 31 March 2005, 31 March 2006 and 31 December 2006.

The maximum amounts of initial public offer financings advanced by the Group to the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) were approximately HK\$12,189,720, HK\$3,550,570, HK\$4,540,900 and HK\$529,990 respectively during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006.

The historical commission and brokerage income from securities, futures and options trading, interest income from margin or initial public offer financings and amounts of margin or initial public offer financings granted during the Track Record Period were mainly determined by the investment strategies of the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) which were affected by the overall economy and stock market sentiment of Hong Kong.

(iii) *Commission or fee paid to the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family)*

During the Track Record Period, an associate of the Former Director had acted as sub-underwriter and placee for securities underwritten and placed by the Group and received an aggregate commission and fee of about HK\$51,750 during the year ended 31 March 2004.

After the listing of the Shares, the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Family) will not act as sub-underwriters for securities underwritten or placed by the Group.

The Directors (including the independent non-executive Directors) consider that financial services provided to each of the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) and the payment of commission or fee are made in the ordinary and usual course of the Group's business and are on normal commercial terms which are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

Since the Directors cannot ascertain whether the directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) would obtain initial public offer financing from the Group in the future, the Directors have not taken into account initial public offer financing in estimating the total consideration for the financial services to be provided to them for the three years ending 31 March 2009. If initial public offer financing is provided to them in future, the Company will comply with the then relevant requirements of the Listing Rules. As the total consideration for the financial services provided by the Group and the payment of commission and fee to each of the

directors of the Group, the Former Director and their respective associates (other than the Yeung Family and the Lee Family) for each of the three years ending 31 March 2009 is expected to be less than HK\$1,000,000 and that the applicable percentage ratios as defined in Rule 14A.10 of the Listing Rules (other than the profits ratio) will be less than 2.5%, the transactions will qualify for the de minimis exemption criterion under Rule 14A.33(3) of the Listing Rules.

### **3. Licencing of trademarks**

The Group is currently using the trademarks “英皇” and “Emperor” as trade names for its businesses. The trademarks “英皇” and “Emperor” were registered by Emperor Management, a wholly owned subsidiary of EIHL, under the Trade Marks Ordinance in Hong Kong (Chapter 559 of the Laws of Hong Kong) and in the PRC under class 36. The specification of services of class 36 includes, inter alia, provision of loans against securities and brokerage services on securities and commodities. The Group is also using the Logo which is registered under class 36 in the PRC by Emperor Management but not registered in Hong Kong by any member of the Group or by any of its connected person and their associates. Particulars of the Trademarks and the Logo are set out in the sub-section headed “Intellectual property rights of the Group” in appendix V to this prospectus.

Historically, the Trademarks and the Logo were used by EMO and its associates (altogether, the “Forex Group”) before Emperor Management registered them in Hong Kong and the PRC. The Forex Group is engaged in leveraged foreign exchange trading and leveraged gold bullion dealing and is owned by The Yeung Family Discretionary Trust, a discretionary trust set up by Mr. Yeung Lik Shing, Michael (“Mr. Michael Yeung”), the brother of Mr. Albert Yeung. Mr. Albert Yeung is the settlor of The Albert Yeung Discretionary Trust and The Albert Yeung Discretionary Trust indirectly owns Charron, the controlling Shareholder of the Company. Although the Forex Group has been using the Trademarks and the Logo, EMO allows Emperor Management to register the Trademarks and the Logo in Hong Kong and the PRC under class 36 subject to the condition that the Emperor Group has to assign the Trademarks and Logo back to EMO when Emperor Group cease to provide brokerage and margin financing services.

Upon completion of the EIHL Distribution, the Emperor Group will no longer engage in brokerage services for securities, futures and options and margin financing. In this regard, the Emperor Group has therefore agreed to assign the Trademarks and the Logo back to EMO. EMO will then procure the registration of the assignment at its own cost.

In order to facilitate the use of the Trademarks and the Logo by the Group for its business, Emperor Management, EMO and EIHL have entered into the Trademarks Agreement with the Company on 2 April 2007 pursuant to which Emperor Management has agreed to grant a non-exclusive licence to the Group to use the Trademarks and the Logo at a nominal consideration of HK\$1.00 in connection with the Group’s business pending the assignment of the same to EMO by Emperor Management. The Group has agreed not to sub-license to any other persons or companies for use of the Trademarks and the Logo without written consent of Emperor Management. Emperor Management will maintain the validity and renew the registration of the Trademarks and the Logo.

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Pursuant to the Trademarks Agreement, EMO has agreed to grant a non-exclusive licence to both the Group and the Emperor Group to use the Trademarks and the Logo in connection with the Group's business and the real estate business of the Emperor Group respectively at a nominal consideration of HK\$1.00 after the assignment of the Trademarks and Logo to EMO by Emperor Management. Each of the Group and the Emperor Group has agreed not to sub-license to any other persons or companies to use the Trademarks and the Logo without written consent of EMO.

The Trademarks Agreement permits the Group to use the Trademarks and the Logo so long as the Trademarks and the Logo are registered in the name of EMO. EMO has agreed to maintain at its own cost the registration of the Trademarks and the Logo, including extensions from time to time of such registration upon expiry. EMO undertakes with the Company and EIHL that (i) it will maintain validity of the Trademarks and the Logo and (ii) it will not grant any licence in respect of the business of the Group and the Emperor Group to any party other than the Group, the Emperor Group and the Forex Group itself to use the Trademarks and the Logo.

Emperor Management, a wholly owned subsidiary of EIHL, and the Forex Group will become connected persons of the Company under Chapter 14A of the Listing Rules after listing of the Shares and therefore the arrangement contemplated under the Trademarks Agreement will constitute a continuing connected transaction of the Company under Rule 14A.14 of the Listing Rules. As the consideration for the licence granted under the Trademarks Agreement is nominal, the Trademarks Agreement falls within the de minimis threshold under Rule 14A.33 of the Listing Rules and is exempt from the reporting, announcement and independent shareholders' approval requirements. The Directors (including the independent non-executive Directors) consider that the terms of the Trademarks Agreement are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

### NON-EXEMPT CONTINUING CONNECTED TRANSACTIONS

The following transactions will constitute non-exempt continuing connected transactions of the Company pursuant to the Listing Rules after listing of the Shares. All these continuing connected transactions, except the transactions to be carried out under the Yeung's Financial Services Agreement (as defined hereinunder) which will require independent shareholders' approval, will only be subject to the reporting and announcement requirements and will be exempted from the Listing Rules requirement to obtain independent shareholders' approval on the basis that they fall within the threshold under Rule 14A.34 of the Listing Rules. As set out in the paragraph headed "Waiver application" below, a waiver for strict compliance with the relevant Listing Rules requirements to publish announcement and to obtain independent shareholders' approval (as the case may be) has been applied to and the same has been obtained from the Stock Exchange.

#### 1. Tenancy Agreements

Pursuant to an agreement ("Previous Tenancy Agreement") dated 19 July 2006 entered into between Very Sound Investments Limited ("Very Sound") and Emperor Securities, Very Sound has agreed to lease to the Group a portion of 24th Floor of Emperor Group Centre, 288 Hennessy Road, Wanchai in Hong Kong with a total gross floor area of approximately 7,006 square feet as the Group's head office at a monthly rental of HK\$98,000, exclusive of rates and management fees. The tenancy commenced on 20 January 2006 and was terminated with effect from 9 December 2006 by mutual consent of the parties

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pursuant to a surrender agreement dated 14 February 2007. Emperor Securities entered into another tenancy agreement on 14 February 2007 with Very Sound (this tenancy agreement together with the Previous Tenancy Agreement are collectively called the “Tenancy Agreements”) pursuant to which Very Sound agreed to lease the entire 24th Floor of Emperor Group Centre with a total gross floor area of 9,323 square feet to Emperor Securities at a monthly rental of HK\$150,000. The new tenancy has a two-year term commencing on 10 December 2006 and ending on 9 December 2008.

Prior to the commencement of the Previous Tenancy Agreement, the Emperor Group has charged the Group a rental of HK\$100,000 per month, exclusive of rates and management fees, for the Group’s use of the entire 24th Floor of Emperor Group Centre (with a total gross floor area of approximately 9,323 square feet) for the period from 1 April 2003 to 19 January 2006. During the aforesaid period, the Group has sub-let part of the tenanted property (the “Leased Area”) on the 24th Floor to the Forex Group. The amount of rent paid by the Forex Group to the Group for the year ended 31 March 2004 and 31 March 2005 was approximately HK\$59,000 and HK\$76,000, and the amount of rent paid for the period from 1 April 2005 up to 19 January 2006 was HK\$321,000. The above change on rental paid by the Forex Group was attributable to the change in areas and period of the Leased Area occupied by the Forex Group during the respective years/period. After the commencement of the Previous Tenancy Agreement, the Group ceased to sub-let the Leased Area to Forex Group, and instead, the Emperor Group directly leased the Leased Area to the Forex Group.

Very Sound is an indirect wholly owned subsidiary of EIHL, which is principally engaged in property investment. As such, Very Sound will become a connected person of the Company under Chapter 14A of the Listing Rules after listing of the Shares.

Upon listing of the Shares on the Stock Exchange, the transactions under the Tenancy Agreements will constitute a continuing connected transaction under Chapter 14A of the Listing Rules.

The Directors expect that the annual cap for the Tenancy Agreements will be HK\$1.4 million, HK\$1.8 million and HK\$1.3 million for the year ending 31 March 2007, 31 March 2008 and 31 March 2009 respectively. The annual cap is set based on the total rental payable by the Group to Very Sound pursuant to the terms of the Tenancy Agreements. On such basis, the applicable percentage ratios as defined in Rule 14A.10(10) of the Listing Rules (other than the profits ratio) exceed 2.5% but are less than 25% and the annual caps do not exceed HK\$10,000,000. Accordingly, the Tenancy Agreements will fall within the exemption under Rule 14A.34(2) of the Listing Rules and no independent shareholders’ approval will be required.

Savills Valuation and Professional Services Limited, a professional valuer which is an Independent Third Party, has reviewed the Tenancy Agreements and confirmed that the rental payable under the Tenancy Agreements is the market rental prevailing at the respective commencement dates of the Tenancy Agreements.

### **2. EIHL Financial Services Agreement**

Pursuant to an agreement (“EIHL Financial Services Agreement”) dated 2 April 2007 entered into between the Company and EIHL, the Group has agreed to (i) provide financial services including brokerage services for securities, futures and options trading and acting as placing agent, underwriter or sub-underwriter; and (ii) provide margin loans from time to time to the Emperor Group and its associates on normal commercial terms and at rates no more favourable than those offered to other Independent Third Parties for a term of three years commencing from 1 April 2006 up to 31 March 2009. Items (i) and (ii) are collectively referred to as the “EIHL Financial Services”.

EIHL and its associates will become connected persons of the Company under Chapter 14A of the Listing Rules after listing of the Shares. Accordingly, the EIHL Financial Services Agreement and the transactions contemplated thereunder will constitute continuing connected transactions of the Company under Chapter 14A of the Listing Rules.

In determining the annual caps for the EIHL Financial Services Agreement, the Directors have categorised the transactions under the EIHL Financial Services Agreement into two types:

- (i) commission, brokerage and interest income to be received from the Emperor Group and its associates for the Group’s provision of the EIHL Financial Services; and
- (ii) granting of margin loans by the Group to the Emperor Group and its associates.



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(i) *Commission and interest income received from Emperor Group and its associates*

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2006, income received from EIHL, its wholly owned subsidiaries and its associated company namely Emperor Entertainment Hotel Limited for the EIHL Financial Services represented commission charged for the brokerage services for securities, futures and options dealings and underwriting services and interest income for margin and initial public offer financings provided by the Group. The amounts of the above transactions were set out as follows:

Financial services	For the year ended 31 March		For the nine months ended 31 December	
	2004 HK\$	2005 HK\$	2006 HK\$	2006 HK\$
Commission and brokerage on dealing in securities and equity options	1,359,660	405,910	506,520	111,620
% to the Group's turnover from dealing in securities and equity options	4.15%	1.29%	1.57%	0.36%
Commission and brokerage on dealing in futures and index options contracts	9,360	81,280	226,650	0
% to the Group's turnover from dealing in futures and index options contracts	0.20%	3.07%	1.76%	0.00%
Commission for placing, underwriting and sub-underwriting services	0	2,106,490	0	0
% to the Group's turnover from placing, underwriting and sub-underwriting commission	0.00%	29.54%	0.00%	0.00%
Interest income from margin financing	176,910	99,210	58,410	5,400
% to the Group's turnover from margin financing	2.63%	1.83%	0.68%	0.06%
Interest income from initial public offer financing	3,780	4,440	5,280	0
% to the Group's turnover from initial public offer financing	0.14%	0.12%	0.03%	0.00%
Total	<u>1,549,710</u>	<u>2,697,330</u>	<u>796,860</u>	<u>117,020</u>
% to the Group's total turnover	<u>2.14%</u>	<u>3.94%</u>	<u>0.84%</u>	<u>0.12%</u>



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Since the Directors cannot ascertain whether the Emperor Group and its associates will obtain initial public offer financing from the Group in future, the EIHL Financial Services Agreement does not cover initial public offer financing, which will be subject to compliance with the then prevailing Listing Rule requirements in case there is such financing.

*(ii) Margin and initial public offer financings provided to the Emperor Group*

During the Track Record Period, the Emperor Group had obtained margin and initial public offer financings from the Group.

The maximum amounts of margin loans advanced by the Group to the Emperor Group were approximately HK\$5,761,060, HK\$3,380,390, HK\$1,576,770 and HK\$108,720 for each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 respectively.

The amounts of margin loans advanced by the Group to the Emperor Group were approximately HK\$556,940, HK\$1,409,050, HK\$85,410 and nil as at 31 March 2004, 31 March 2005, 31 March 2006 and 31 December 2006 respectively.

As discussed above, the EIHL Financial Services Agreement does not cover initial public offer financing, for the information of the Shareholders only, the maximum amounts of initial public offer financings provided by the Group to the Emperor Group were approximately HK\$3,423,900, HK\$2,495,000, HK\$1,881,850 and nil during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 respectively.

The relatively larger amount of the Group's commission and brokerage income from the Emperor Group on securities and equity options dealings for the year ended 31 March 2004 as compared to that for the years ended 31 March 2005 and 31 March 2006 was mainly due to the change in investment strategy of the Emperor Group. The Emperor Group changed its investment focus from securities dealings to futures dealings, the Group's commission and brokerage income from the Emperor Group's securities and equity options dealing has decreased in the two years ended 31 March 2006, while there was an increase in the Group's commission and brokerage income from the Emperor Group's futures and index options dealings for the same years.

For the year ended 31 March 2005, the Group had acted as an underwriter of a rights issue made by Emperor Entertainment Hotel Limited, an associated company of EIHL, and charged an underwriting commission of approximately HK\$2.1 million. Save for the above underwriting activity, the Group had not acted as placing agent or underwriter or sub-underwriter for any listed member of the Emperor Group and its associates during the Track Record Period.

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In determining the annual caps for the transactions contemplated under the EIHL Financial Services Agreement, the Directors have taken the following principal factors into consideration:

In relation to:

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|---|---|
| (i) Commission, brokerage and interest income from the Emperor Group and its associates | (1) the expected increase in commission and brokerage income from dealings in securities, futures and options of the Group for the three years ending 31 March 2009;  |
|   | (2) the lowest percentage of the commission and brokerage income received from the Emperor Group for securities, futures and options dealings to the Group's turnover from these activities for over the three years ended 31 March 2006 in view of the decrease in revenue derived from the Emperor Group over the nine months ended 31 December 2006; |
|   | (3) the proportion of fund raised by the listed members of the Emperor Group and its associated companies which was underwritten by the Group during the Track Record Period;   |
|   | (4) the anticipated growth of market capitalisation and fund raising activities of the listed members of the Emperor Group and its associates for the three years ending 31 March 2009;   |
|   | (5) the expected growth of interest income from margin financing of the Group for the three years ending 31 March 2009;   |
|   | (6) the lowest percentage of interest income for providing margin financings received from the Emperor Group to the Group's turnover from margin financings over the three years ended 31 March 2006 in view of the decrease in revenue derived from the Emperor Group over the nine months ended 31 December 2006;                                     |
|   | (7) the expected commission rate and interest rate to be charged on Independent Third Parties under normal commercial terms; and  |

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## BUSINESS

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|  | (8) the expected continuing improvement in the economy and the increasing fund raising activities by way of listing and placements in Hong Kong.  |
| (ii) Margin loan advance to Emperor Group and its associates | <p>(1) the lowest amount of margin loan advanced to the Emperor Group for the year ended 31 March 2006 in view of the decrease in margin loan advanced to the Emperor Group over the three years ended 31 March 2006 and the nine months ended 31 December 2006;</p> <p>(2) the expected improving economy and market sentiment of securities trading in Hong Kong; and</p> <p>(3) the anticipated growth in the business of the Group after listing of the Shares.</p> |

Based on the above factors and information, the annual caps for the EIHL Financial Services Agreement for each of the three years ending 31 March 2009 are set out as follows:

	For the year ending 31 March		
	2007	2008	2009
	HK\$	HK\$	HK\$
(i) Commission and interest income	1,600,000	1,700,000	1,700,000
(ii) Maximum margin loan amount	1,600,000	1,600,000	1,600,000
Total	<u>3,200,000</u>	<u>3,300,000</u>	<u>3,300,000</u>

The Directors (including the independent non-executive Directors) consider that the EIHL Financial Services Agreement was entered into in the ordinary and usual course of the Group's business and is on normal commercial terms which are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

The applicable percentage ratios as defined in Rule 14A.10 of the Listing Rules (other than the profits ratio) of the annual caps under the EIHL Financial Services Agreement exceed 2.5% but are less than 25%, and these annual caps do not exceed HK\$10,000,000. Accordingly, the EIHL Financial Services Agreement falls within the exemption criterion under Rule 14A.34(2) of the Listing Rules and no independent shareholders' approval is required.

### **3. Financial services agreement with the Yeung Family**

Pursuant to an agreement (“Yeung’s Financial Services Agreement”) dated 2 April 2007 entered into between the Company and Ms. Daisy Yeung, the Group has agreed to (i) provide financial services including brokerage service for securities, futures and options trading; and (ii) provide margin loan to the Yeung Family from time to time on normal commercial terms and at rates no more favourable to the Yeung Family than those offered to other Independent Third Parties for a three-year term commencing from 1 April 2006 up to 31 March 2009. Items (i) and (ii) are collectively referred to as the “Yeung’s Financial Services”. Under the Yeung’s Financial Services Agreement, the Group has also agreed to pay commission and fee to the Yeung Family for their acting as placees for the securities underwritten or placed by the Group on normal commercial terms and at rates no more favourable to the Yeung Family than rates charged by other Independent Third Parties. Detailed rates and payment terms will be specified in the individual contracts governing the particular transactions.

Under the Yeung’s Financial Services Agreement, members of the Yeung Family include Ms. Daisy Yeung and her associates. Ms. Daisy Yeung is the managing Director and the other members of the Yeung Family are defined as her associates under the Listing Rules. After the listing of the Shares, Ms. Daisy Yeung and her associates will become connected persons of the Company under Chapter 14A of the Listing Rules. As such, the transactions contemplated under the Yeung’s Financial Services Agreement will constitute continuing connected transactions of the Company under Chapter 14A of the Listing Rules.

In determining the annual caps under the Yeung’s Financial Services Agreement, the Directors have categorized the transactions under the Yeung’s Financial Services Agreement into three types:

- (i) commission, brokerage and interest income to be received from the Yeung Family for providing the Yeung’s Financial Services;
- (ii) margin loans to be provided to the Yeung Family; and
- (iii) commission and fee to be paid to the Yeung Family for their acting as placees for securities underwritten or placed by the Group.

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(i) *Commission and interest income received from the Yeung Family*

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2006, income received from the Yeung Family represented commission charged for the brokerage services for securities, futures and options dealings and interest income for margin and initial public offer financings provided by the Group and the amounts of the above transactions were set out as follows:

	For the year ended 31 March		For the nine months ended 31 December	
Financial services	2004	2005	2006	2006
	HK\$	HK\$	HK\$	HK\$
Commission and brokerage on dealing in securities and equity options	543,420	1,494,660	1,305,420	764,050
% to the Group's turnover from dealing in securities and equity options	1.66%	4.74%	4.04%	2.47%
Commission and brokerage on dealing in futures and index options contracts	336,140	160,000	200	4,500
% to the Group's turnover from dealing in futures and index options contracts	7.35%	6.05%	0.00%	0.02%
Interest income from margin financing	201,040	210,120	474,630	431,750
% to the Group's turnover from margin financing	2.99%	3.88%	5.49%	5.10%
Interest income from initial public offer financing	34,500	2,190	34,550	1,098,440
% to the Group's turnover from initial public offer financing	1.24%	0.06%	0.22%	5.24%
Total	<u>1,115,100</u>	<u>1,866,970</u>	<u>1,814,800</u>	<u>2,298,740</u>
% to the Group's total turnover	<u>1.54%</u>	<u>2.72%</u>	<u>1.91%</u>	<u>2.43%</u>

As shown in the table above, the Group earned interest income from the Yeung Family by providing initial public offer financings to the Yeung Family during the Track Record Period. However, since the Directors cannot ascertain whether the Yeung Family will obtain initial public offer financing from the Group in future, the Yeung's Financial Services Agreement with the Yeung Family does not cover initial public offer financing, which will be subject to compliance with the then prevailing Listing Rules requirements in case such financing is needed.

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## BUSINESS

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(ii) *Margin and initial public offer financings provided to the Yeung Family*

During the Track Record Period, the Yeung Family had obtained margin and initial public offer financings from the Group.

The maximum amounts of margin loans advanced by the Group to the Yeung Family during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 were approximately HK\$8,754,920, HK\$15,468,750, HK\$16,606,610 and HK\$28,436,820 respectively.

The amounts of margin loans advanced by the Group to the Yeung Family were approximately HK\$3,551,850, HK\$5,547,500, HK\$6,143,020 and HK\$3,200,820 as at 31 March 2004, 31 March 2005, 31 March 2006 and 31 December 2006 respectively.

As discussed above, the Yeung's Financial Services Agreement does not cover initial public offer financing, for the information of the Shareholders only, the maximum amounts of initial public offer financings provided by the Group to the Yeung Family during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 were approximately HK\$13,796,510, HK\$2,008,510, HK\$26,934,310 and HK\$590,093,940 respectively.

The historical commission and brokerage income received from the Yeung Family for securities, futures and options trading, interest income by providing margin and initial public offer financings and amounts of margin and initial public offer financing advanced to the Yeung Family during the Track Record Period were mainly determined by the investment strategies of each individual member of the Yeung Family which were largely affected by their own analysis and perception of the economic and stock market condition in Hong Kong.

(iii) *Commission or fee paid to the Yeung Family*

The Group had paid commission or fee to members of the Yeung Family for acting as placees in their personal capacities as clients of the Group for securities underwritten or placed by the Group during the years ended 31 March 2004 and 31 March 2006.

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2006, the amounts of the commission or fee paid to the Yeung Family were as follows:

	For the year ended 31 March		For the nine months ended 31 December	
	2004	2005	2006	2006
	HK\$	HK\$	HK\$	HK\$
Commission or fee paid to the Yeung Family	20,250	—	39,250	—
% to the Group's total commission expenses for placing and underwriting	0.82%	—	0.94%	—

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In determining the annual caps for the transactions contemplated under the Yeung's Financial Services Agreement, the Directors have taken into consideration of the following principal factors:

In relation to:

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|--|---|
| (i) Commission and interest income from the Yeung Family | (1) the expected increase in commission and brokerage income from dealings in securities, futures and options of the Group for the three years ending 31 March 2009;  |
|  | (2) the relative contribution of commission and brokerage income for securities and equity options dealings from the Yeung Family to the Group's total turnover from these activities for each of the two years ended 31 March 2006;  |
|  | (3) potential commission and brokerage income to be received from the Yeung Family for futures and index options dealing for the three years ending 31 March 2009;  |
|  | (4) the expected growth in interest income from margin financings of the Group for the three years ending 31 March 2009;  |
|  | (5) the highest percentage of the interest income received from the Yeung Family for margin financings to the Group's turnover from margin financings during the three years ended 31 March 2006 and potential increase in view of the recent increase in margin financings provided to the Yeung Family; |
|  | (6) the expected commission and interest rates to be charged on Independent Third Parties under normal commercial terms; and  |
|  | (7) the expected continuing improvement in the economy and the positive market sentiment of the stock and futures markets in Hong Kong.   |

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|--|--|
| (ii) Margin loans advanced to the Yeung Family       | <p>(1) the highest amount of margin loans advanced to the Yeung Family during the Track Record Period and its potential increase;</p> <p>(2) the expected improving economy and market sentiment of securities trading in Hong Kong; and</p> <p>(3) the anticipated growth in the business of the Group after listing of the Shares.</p>   |
| (iii) Commission and fee payable to the Yeung Family | <p>(1) the amount of commission paid to the members of Yeung Family as placees in the years ended 31 March 2004 and 31 March 2006;</p> <p>(2) potential underwriting or placing activities which the Yeung Family will act as placees for the Group for the three years ending 31 March 2009;</p> <p>(3) the expected commission rate and fee payable to Independent Third Parties under normal commercial terms; and</p> <p>(4) the expected continuing improvement in the economy and the positive market sentiment of the stock and futures markets in Hong Kong.</p> |

Based on the above factors and information, the Directors expect that the annual caps for the Yeung's Financial Services Agreement for each of the three years ending 31 March 2009 are as follows:

	For the year ending 31 March		
	2007 HK\$	2008 HK\$	2009 HK\$
(i) Commission and interest income	2,500,000	2,900,000	3,100,000
(ii) Maximum margin loan amount	31,000,000	31,000,000	31,000,000
(iii) Commission and fee payment	22,000	24,000	27,000
Total	<u>33,522,000</u>	<u>33,924,000</u>	<u>34,127,000</u>

The Directors (including the independent non-executive Directors) consider that the Yeung's Financial Services Agreement was entered into in the ordinary and usual course of the Group's business and is on normal commercial terms which are fair and reasonable and in the interests of the Company and the Shareholders as a whole.



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Since the applicable percentage ratios as defined in Rule 14A.10 of the Listing Rules (other than the profits ratio) calculated with reference to the annual caps under the Yeung's Financial Services Agreement exceed 2.5%, and the annual caps exceed HK\$10,000,000. Accordingly, the Yeung's Financial Services Agreement is subject to the reporting, announcement and independent shareholders' approval requirements of the Listing Rules.

#### **4. Financial services agreement with the Lee Family**

Pursuant to an agreement ("Lee's Financial Services Agreement") dated 2 April 2007 entered into between the Company and Mr. Lee Wai Shing, the Group has agreed to (i) provide financial services including brokerage services for securities, futures and options trading; and (ii) provide margin loans to the Lee Family from time to time on normal commercial terms and at rates no more favourable than those available to other Independent Third Parties for a three-year term commencing from 1 April 2006 up to 31 March 2009. Items (i) and (ii) are collectively referred to as the "Lee's Financial Services". Detailed rates and payment terms will be specified in the individual contracts governing the particular transactions.

Mr. Lee Wai Shing is a director of a subsidiary of the Company and other members of the Lee Family is defined as his associates under the Listing Rules. After listing of the Shares, the Lee Family will become connected persons of the Company under Chapter 14A of the Listing Rules. As such, the transactions contemplated under the Lee's Financial Services Agreement will become continuing connected transactions of the Company under Chapter 14A of the Listing Rules.

In determining the annual caps under the Lee's Financial Services Agreement, the Directors have categorized the transactions under the Lee's Financial Services Agreement into two types:

- (i) commission, brokerage and interest income to be received from the Lee Family for the Group's provision of the Lee's Financial Services; and
- (ii) margin loans to be provided to the Lee Family.

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## BUSINESS

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(i) *Commission and interest income received from the Lee Family*

For each of the three years ended 31 March 2006 and the nine months ended 31 December 2006, income received from the Lee Family represented commission charged for the brokerage services for securities, futures and options dealings or interest income for margin and initial public offer financings provided by the Group and the amounts of the above transactions were set out as follows:

Financial services	For the year ended 31 March		For the nine months ended 31 December	
	2004 HK\$	2005 HK\$	2006 HK\$	2006 HK\$
Commission and brokerage on dealing in securities and equity options	650	5,400	17,480	115,570
% to the Group's turnover from dealing in securities and equity options	0.00%	0.02%	0.05%	0.37%
Commission and brokerage on dealing in futures and index options contracts	0	0	120	0
% to the Group's turnover from dealing in futures and index options contracts	0.00%	0.00%	0.00%	0.00%
Interest income from margin financing	130	9,710	40,800	58,750
% to the Group's turnover from margin financing	0.00%	0.18%	0.47%	0.69%
Interest income from initial public offer financing	0	280	0	110,930
% to the Group's turnover from initial public offer financing	0.00%	0.01%	0.00%	0.53%
Total	<u>780</u>	<u>15,390</u>	<u>58,400</u>	<u>285,250</u>
% to the Group's total turnover	<u>0.00%</u>	<u>0.02%</u>	<u>0.06%</u>	<u>0.30%</u>

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As shown in the table above, the Group earned interest income from the Lee Family by providing initial public offer financings to the Lee Family during the Track Record Period. However, since the Directors cannot ascertain whether the Lee Family will obtain initial public offer financing from the Group in future, the Lee's Financial Services Agreement does not cover initial public offer financing, which, will be subject to compliance with the then prevailing Listing Rules requirements in case such financing is needed.

*(ii) Margin and initial public offer financings provided to the Lee Family*

During the Track Record Period, the Lee Family had obtained margin and initial public offer financings from the Group.

The maximum amounts of margin loans advanced by the Group to the Lee Family during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 were approximately HK\$220, HK\$365,240, HK\$809,290 and HK\$3,350,240 respectively.

The amounts of margin loans advanced by the Group to the Lee Family were approximately HK\$220, HK\$127,420, HK\$316,680 and HK\$1,196,820 as at 31 March 2004, 31 March 2005, 31 March 2006 and 31 December 2006 respectively.

As discussed above, the Lee's Financial Services Agreement does not cover the initial public offer financing, for the information of the Shareholders only, the maximum amounts of initial public offer financings provided by the Group to the Lee Family during each of the three years ended 31 March 2006 and the nine months ended 31 December 2006 were approximately nil, HK\$344,550, nil and HK\$31,090,880 respectively.

The historical commission and brokerage income and interest received from the Lee Family and the amounts of margin and initial public offer financings provided to them were mainly determined by the investment strategies of each individual member of the Lee Family which were largely affected by their own analysis and perception of the economic and stock market condition in Hong Kong.

During the Track Record Period, the Lee Family has not acted as placees for securities underwritten or placed by the Group. As a result, the Lee's Financial Services Agreement does not cover such services. In the event that such placing opportunities are provided to the Lee Family, the Company will fully comply with the then prevailing Listing Rules requirements.

In determining the annual caps for the transactions contemplated under the Lee's Financial Services Agreement, the Directors have taken into consideration the following principal factors:

In relation to:

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|--|--|
| (i) Commission and interest income from the Lee Family | (1) the income derived from the Lee's Financial Services for the three years ended 31 March 2006;  |
|  | (2) the average monthly income received from the Lee Family for securities and equity options dealings for the nine months ended 31 December 2006; |

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- (3) the expected growth in interest income from margin financing of the Group for the three years ending 31 March 2009;
  - (4) the relative contribution of interest income from margin financings received from the Lee Family to the Group's total interest income from margin financings for each of the three years ended 31 March 2006;
  - (5) potential increase in the Lee Family's activities of dealing in securities, futures and options and obtaining margin financings for the three years ending 31 March 2009;
  - (6) the expected commissions and interest rates to be charged by Independent Third Parties under normal commercial terms; and
  - (7) the expected continuing improvement in the economy and the positive market sentiment of the stock and futures markets in Hong Kong.
- (ii) Margin loans advanced to the Lee Family
  - (1) the amounts of margin loans advanced to the Lee Family for the three years ended 31 March 2006;
  - (2) the highest amount of margin loans advanced to the Lee Family for the nine months ended 31 December 2006 and possible increase in future in view of the increase in trading activities of the Lee Family for the nine months ended 31 December 2006;
  - (3) the expected improving economy and market sentiment of securities trading in Hong Kong; and
  - (4) the anticipated growth in the business of the Group after listing of the Shares.

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Based on the above factors and information, the Directors expect that the annual caps for the Lee's Financial Services Agreement for each of the three years ending 31 March 2009 are set out as follows:

For the year ending 31 March			
	2007	2008	2009
	HK\$	HK\$	HK\$
(i) Commission and interest income	710,000	710,000	710,000
(ii) Maximum margin loan amount	4,800,000	4,800,000	4,800,000
Total	<u>5,510,000</u>	<u>5,510,000</u>	<u>5,510,000</u>

The Directors (including the independent non-executive Directors) consider that the Lee's Financial Services Agreement was entered into in the ordinary and usual course of the Group's business on normal commercial terms which are fair and reasonable and in the interests of the Company and the Shareholders as a whole.

The applicable percentage ratios as defined in Rule 14A.10 of the Listing Rules (other than the profits ratio) calculated with reference to the annual caps exceed 2.5% but are less than 25%, and the annual caps do not exceed HK\$10,000,000. Accordingly, the Lee's Financial Services Agreement falls within the exemption criterion under Rule 14A.34(2) of the Listing Rules and therefore is exempt from independent shareholders' approval requirements but subject to the reporting and announcement requirements.

### Corporate Governance

The Group has internal control measures in place to avoid conflict of interest in transactions involving senior management or directors of the Group. As set out in the operational manual of the Group, any members of the senior management or directors of the Group who are involved in decision making process for operational matters (for example, approving or annual reviewing credit limit or deciding on whether to give tolerance to clients who fail to meet margin calls) shall abstain from making decisions on matters involving that person's employee or associated accounts or client accounts of which he/she is the handling account executive.

### WAIVER APPLICATION

The Directors (including the independent non-executive Directors) are of the opinion that the non-exempt continuing connected transactions, namely the Tenancy Agreements, the EIHL Financial Services Agreement, the Yeung's Financial Services Agreement and the Lee's Financial Services Agreement, (collectively referred to as "Non-exempt Continuing Connected Transactions") have been conducted, and will be carried out, in the ordinary and usual course of business of the Group as well as on normal commercial terms which are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Having considered the factors and information mentioned above, the Directors (including the independent non-executive Directors) also consider that the annual caps set out above for the Non-exempt Continuing Connected Transactions are fair and reasonable and in the interests of the Company and the Shareholders as a whole. Under the Listing Rules, once the Shares are listed on the Stock Exchange, the transactions under the Tenancy Agreements, the EIHL Financial Services Agreement and the Lee's Financial Services Agreement will constitute non-exempt continuing connected transactions of the Company which are subject to the reporting and announcement requirements; whilst the transactions under the Yeung's Financial Services Agreement will constitute non-exempt continuing connected transactions of the Company which are subject to the reporting, announcement and independent shareholders' approval requirements.

The Joint Sponsors are of the view that (i) the Non-exempt Continuing Connected Transactions as mentioned above, are in the ordinary and usual course of the Group's business and on normal commercial terms which are fair and reasonable and in the interests of the Company and the Shareholders as a whole; and (ii) the annual caps for the Non-exempt Continuing Connected Transactions set out above are fair and reasonable so far as the Shareholders are concerned.

The Non-exempt Continuing Connected Transactions are expected to continue after the listing of the Shares on the Stock Exchange, and have been entered into prior to the listing of the Shares. Since such transactions are expected to occur continuously (and details of which have been fully disclosed in this prospectus), the Directors consider that it is impractical to comply with the announcement and the independent shareholders' approval requirements of the Listing Rules. Accordingly, the Company has applied to the Stock Exchange for, and the Stock Exchange has granted to the Company, a waiver pursuant to Rule 14A.42(3) of the Listing Rules (i) from strict compliance with the announcement requirement in relation to the Tenancy Agreements for a period of three years ending 31 March 2009, the EIHL Financial Services Agreement for a period of three years ending 31 March 2009 and the Lee's Financial Services Agreement for a period of three years ending 31 March 2009, and (ii) from strict compliance with the announcement and independent shareholders' approval requirements in relation to the Yeung's Financial Services Agreement for a period of three years ending 31 March 2009. In addition, the Directors confirm that the Company will comply with the relevant provision of Chapter 14A of the Listing Rules, including the proposed annual caps and to comply with rules 14A.35(1), 14A.35(2), 14A.36, 14A.37, 14A.38, 14A.39 and 14A.40 of the Listing Rules in relation to the Non-exempt Continuing Connected Transactions.

In the event that the terms of the above mentioned continuing connected transactions are altered or the Group enters into any new transactions or agreements with any of its connected persons in the future, the Company will comply with the provisions of Chapter 14A of the Listing Rules unless it applies for and obtains a separate waiver from the Stock Exchange. In addition, if the Non-exempt Continuing Connected Transactions continue after the expiry of the current waiver, the Company will comply with the provisions of Chapter 14A of the Listing Rules in relation to any non-exempt continuing connected transactions.

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### RELATIONSHIP WITH EIHL, CHARRON AND THE DIRECTORS

Immediately after completion of the EIHL Distribution and the Share Offer which shall occur prior to 8:00 a.m. on the Listing Date, Emperor Group will cease to hold any Shares (save for acting as a nominee for holding fractional entitlements or Shares that should have been issued and allotted to Non-qualifying EIHL Shareholders) and Charron will become the Company's controlling shareholder holding approximately 54.11% of the Company's existing issued share capital as enlarged by the Share Offer (calculated on the basis that Charron fully takes up its assured entitlements under the Preferential Offer).

To the best knowledge and belief of the Directors having made all reasonable enquiries, as at the Latest Practicable Date, neither Charron nor the Directors have any interest in a business, apart from the Group's business, which competes or is likely to compete, either directly or indirectly, with the Group's business.

Charron is owned by Jumbo Wealth Limited in trust for The A&A Unit Trust, which is a unit trust under The Albert Yeung Discretionary Trust. The settlor of The Albert Yeung Discretionary Trust is Mr. Albert Yeung, the father of Ms. Daisy Yeung who is the managing Director, and its beneficiaries include Ms. Daisy Yeung and other family members of Mr. Yeung Sau Shing, Albert.

On 10 April 2007, the Company entered into a deed of non-competition (the "Deed of Undertaking") with EIHL, Charron, EMO, Future Gain Investments Limited (which is an investment holding company and is wholly owned by The Albert Yeung Discretionary Trust) and Ms. Daisy Yeung.

The Deed of Undertaking is conditional on the following:

- (a) the Listing Committee of the Stock Exchange granting listing of, and permission to deal in, all the Shares in issue and to be issued; and
- (b) the obligations of the Underwriters under the Underwriting Agreement becoming unconditional (including, if relevant, as a result of the waiver of any condition(s) therein) and such agreement not being terminated in accordance with its respective terms or otherwise.

Pursuant to the Deed of Undertaking, each of the covenantors hereby undertakes to the Company that:

- (i) each of the covenantors will not, and will procure that their respective subsidiaries (only applicable if the relevant covenantor is a corporation) and associates (as the case may be) will not, either on its own account or in conjunction with or on behalf of any person, firm or company, carry on or be engaged or interested, directly or indirectly whether as a shareholder (other than as a Shareholder), partner or agent, in (a) margin financing and other financing services of which the securities include the securities listed on the Stock Exchange and other stock exchanges; (b) provision of brokerage services in relation to futures and options products traded on the Stock Exchanges or other stock exchanges; or (c) in any other business that may compete, directly or indirectly, with any business being carried out by any member of the Group in Hong Kong or other jurisdictions from time to time;

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- (ii) EIHL further undertakes that in addition to the restricted activities mentioned in (i) above, it will not, and will procure its subsidiaries not to engage in placing and underwriting activities; and
- (iii) each of the covenantors further unconditionally and irrevocably undertakes to the Company that it will use its best endeavours to procure that its employees and any company under its direct or indirect control (except for those within the Group) as well as their respective employees to observe the restrictions and undertakings contained in the Deed of Undertaking.

The Deed of Undertaking will cease to have effect on the earlier of the date on which:

- (i) the later of the date on which (a) Ms. Daisy Yeung, ceases to be a Director; and (b) Charron ceases to be the substantial shareholder (as defined in the Listing Rules) of the Company; and
- (ii) the Shares cease to be listed and traded on the Stock Exchange.

In order to protect the interests of the independent Shareholders, the following measures will be adopted by the Company in respect of the enforceability of the Deed of Undertaking:

- the independent non-executive Directors will review, on an annual basis, compliance with the Deed of Undertaking by the relevant parties;
- the Company will disclose result of the findings found (if any) by the independent non-executive Directors relating to the enforcement of the Deed of Undertaking in the Company's annual report or, where the Board considers it appropriate, by way of an announcement; and
- the Company will make an annual confirmation as to compliance with the Deed of Undertaking in its annual report.

After completion of the EIHL Distribution and the Share Offer, the Board and the senior management of the Group will operate independently from the board of directors and the senior management of the Emperor Group. Among the three executive Directors, only one (Ms. Daisy Yeung) has family relationship with a member of the board of directors of EIHL, being Ms. Luk Siu Man, Semon who is the chairperson and a non-executive director of EIHL and the mother of Ms. Daisy Yeung. Therefore, the Board has majority of views and opinions from persons independent of EIHL. In addition, the Company has three independent non-executive Directors, who are also independent of EIHL. None of the three independent non-executive Directors has any business or other relationships with other members of the Emperor Group, its substantial shareholders, directors and other senior management, and their respective associates.

After completion of the EIHL Distribution and the Share Offer, the Group is financially independent of the Emperor Group. There will be no financing from the Emperor Group to the Group and the Directors are of the opinion that, taking into account of the Group's internal resources, its banking facilities and the estimated net proceeds of the Share Offer, the Group will have sufficient working capital for its present requirements for at least the next 12 months from the date of publication of this prospectus.