

立法會
Legislative Council

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Legislative Council
Panel on Financial Affairs

Minutes of Meeting held on
Monday, 7 May 2001 at 10:45 am
in the Chamber of the Legislative Council Building

- Members present** : Hon Ambrose LAU Hon-chuen, JP (Chairman)
Hon Henry WU King-cheong, BBS (Deputy Chairman)
Hon James TIEN Pei-chun, JP
Hon Albert HO Chun-yan
Hon LEE Cheuk-yan
Hon Eric LI Ka-cheung, JP
Hon NG Leung-sing
Hon James TO Kun-sun
Hon CHAN Kam-lam
Hon SIN Chung-kai
Hon Jasper TSANG Yok-sing, JP
Hon Emily LAU Wai-hing, JP
- Non-Panel Members attending** : Hon CHAN Yuen-han
Hon LI Fung-ying, JP
- Members absent** : Dr Hon David LI Kwok-po, JP
Hon Bernard CHAN
Dr Hon Philip WONG Yu-hong
- Public officers attending** : For Items III, IV and V
Miss Denise YUE
Secretary for the Treasury

Mr Stanley YING
Deputy Secretary for the Treasury

For Items III and V

Mr LI Kwok-tso
Principal Assistant Secretary for the Treasury

For Item III

Mr SHUM Man-to
Director of Accounting Services

Mr TSANG Chi-hung
Assistant Director of Accounting Services

Mr Frankie LAM
Chief Treasury Account

Clerk in attendance : Mrs Florence LAM
Chief Assistant Secretary (1)4

Staff in attendance : Ms Connie SZETO
Senior Assistant Secretary (1)1

I Information papers issued since the last meeting
(LC Paper No. CB(1) 1069/00-01(01) -- Mandatory Provident Fund Schemes Statistical Digest)

Members noted that the above information paper had been issued since the last meeting.

II Date of next meeting and items for discussion
(LC Papers No. CB(1) 1144/00-01(01),(02) & (03))

2. Members agreed to discuss the following items at the next Panel meeting scheduled for Monday, 4 June 2001:

- (a) Briefing by the Financial Secretary on Hong Kong's latest economic situation;

- (b) The work of the Advisory Committee on Human Resources Development in the Financial Services Sector of Hong Kong; and
- (c) Issues relating to the implementation of the Insurance Intermediaries Quality Assurance Scheme.

3. On agenda item (a), members noted that apart from the briefing on Hong Kong's latest economic situation, the said meeting would also serve as a forum for Members to exchange views with the newly appointed Financial Secretary (FS) on issues of mutual interest and concern. Members agreed that the discussion with FS would focus mainly on aspects including his aspirations and vision in managing his policy portfolio, the budgetary process and mode of consultation with Legislative Council (LegCo) Members, and the management of the fiscal reserves.

4. As the first Monday of July 2001 was a public holiday, members agreed to hold the regular Panel meeting on Tuesday, 3 July 2001 at 10:45 am. Miss Emily LAU suggested, and members agreed, that academics and experts in relevant fields would be invited to attend the meeting and discuss with the Panel the proper use of the fiscal reserves.

III Review of Government Financial Reporting

(LC Papers No. CB(1) 1134/00-01(01) & 1178/00-01(01))

5. The Director of Accounting Services (D/AS) gave a Power Point presentation on Government's initiatives and plans to improve its accounting practices based on the recommendations of the Task Force on Review of the Government's Financial Reporting Policy (the Task Force). He highlighted the major proposals relating to the preparation of Government accounts as follows:

- (a) The Government would continue to prepare the existing cash-based Annual Accounts to demonstrate its compliance with budget appropriations approved by the legislature and the stewardship of cash spending.
- (b) An additional set of accrual-based Consolidated Accounts containing financial statements (comprising a Statement of Financial Position, a Statement of Financial Performance, and a Cash Flow Statement), a Stewardship Statement and a Departmental Service Cost Statement would be prepared on an annual basis to provide the following information:

- (i) Statement of Financial Position - major assets and liabilities of the Government including fixed assets, loans, investments and pension;
 - (ii) Statement of Financial Performance - related expenses on assets, such as depreciation and accrued pension benefits, and entities in which the Government had a major interest, such as the Exchange Fund (EF), MTR Corporation Ltd. (MTRC), Kowloon-Canton Railway Corporation (KCRC), the Hong Kong Housing Authority (HKHA), etc.;
 - (iii) Stewardship Statement - non-financial information on major physical assets, i.e. land, buildings, roads, drains, etc. employed by the Government for service delivery; and
 - (iv) Departmental Service Cost Statement - full cost of service delivery for each bureau and department including costs of services provided by other departments, pension and leave cost, and notional costs such as accommodation costs.
- (c) The proposals would be implemented in two phases. Except for the reporting of fixed assets which would be implemented starting from the accounts for 2004-05, all of the above proposals would be implemented from the accounts for 2002-03. A post-implementation review would be conducted in 2006-07 to assess the results achieved and the need for further changes.
- (d) One-off expenditure of \$68 million would be incurred mainly for the identification and valuation of fixed assets and an average annual recurrent expenditure of \$18 million would be incurred between 2002-03 and 2004-05.
- (e) The Task Force would publish its Report for consultation with the public, relevant parties including LegCo Members, accounting profession and accountancy academics, heads of Government departments until the end of June 2001.

6. Members generally expressed support for the Government's initiative to introduce accrual-based accounts. They noted that the proposals would supplement the existing cash-based accounts, increase the Government's transparency and accountability, and enhance cost-control and cost-effectiveness. The move was in line with latest developments in accounting practices of advanced economies. Moreover, there had been similar suggestions proposed by the accounting profession and academics, as well as the Public Accounts Committee in its Report published in 1999 in response to the Director of Audit's Value for Money Audits Report No. 33.

7. On members' enquiry about the impact of the proposals on the current budgeting practices, the Secretary for the Treasury (S for Tsy) affirmed that there would be no change to the preparation of the existing annual Government accounts which would continue to be prepared on the cash accounting basis. She stressed that the accrual-based accounts would present fully the Government's financial position, financial performance, and the resources employed to deliver public services, thus providing more comprehensive financial information about the Government.

8. As to why the Government would not be preparing the annual budget on an accrual basis as in the case of some developed economies, S for Tsy said that full implementation of the accrual-based budgeting for the government accounts would entail fundamental changes to the Government's financial management. This would require careful consideration. The Administration would examine related issues during the post-implementation review to be conducted in 2006-07.

9. In response to the enquiry about the presentation of financial information relating to fiscal reserves, D/AS said that the definition of the fiscal reserve would remain unchanged after the introduction of the accrual-based accounting. In the Consolidated Accounts, the Government's net assets would be presented under three reserves, namely General Reserve, Exchange Fund Reserve and Capital Expenditure Reserve. The General Reserve represented the amount of net assets (total assets less liabilities) of the Government less the amount of net assets of the EF and fixed assets. The Exchange Fund Reserve represented the amount of net assets of the EF, i.e. total assets (including investment income accrued over the years) less liabilities (including mainly the Exchange Fund Certificates of Indebtedness and fiscal reserve). The use of the EF was governed by the Exchange Fund Ordinance (EFO) (Cap. 66). The Capital Expenditure Reserve represented the cumulative amount of funds already spent on the acquisition or construction of those fixed assets to be capitalized after deducting cumulative depreciation. S for Tsy added that as the management of the EF was not the responsibility of the Finance Bureau, she did not have information about the current financial position of the EF at hand.

10. Regarding members' concern as to whether the liabilities relating to pensions for civil servants would be shown in the accrual-based accounts, S for Tsy stressed that the accounts would report the financial position of the Government, including the liability on pensions for civil servants. Even if the liabilities for civil service pensions were to exceed the total Government assets in the accounts, the Government would not be required to commit funds under the annual accounts to pay off the liabilities. She added that it was the existing practice of developed economies to include pension liabilities in the accrual-based accounts. S for Tsy also informed members that according to the consultancy study conducted by the Civil Service Bureau in 2000, the total

pension liabilities for civil servants was in the region of \$250 billion to \$300 billion.

11. Responding to a question about the potential impact on credit ratings, S for Tsy said that the Administration did not envisage that the proposals would have any adverse effect on Hong Kong's ratings. Indeed, it was believed that the provision of accrual Government accounts would facilitate rating agencies in collecting and compiling information about the Government's financial position. She added that copies of the consultation document would also be issued for reference of major international rating agencies.

12. On the valuation of Government's fixed assets for presentation in the accrual account, D/AS explained that different valuation methods would be adopted depending on the nature of the fixed assets. Generally speaking, infrastructure assets, Government buildings and plant and equipment costing \$1 million or above, would be valued at depreciated historical cost. If the historical cost was not available, such as in the case of the Cross-Harbour Tunnel, the assets would be valued at depreciated replacement cost.

13. As to why the Government had adopted different consolidation methodologies for Government assets held by public entities, D/AS explained that this was to reflect the different nature of the assets and the relationship between the Government and these entities. For instance, a line-by-line consolidation method would be adopted for assets held in the HKHA where assets and liabilities of the organization would be combined and presented in the accrual accounts. On the other hand, an equity consolidation method would be used in the case of MTRC and KCRC which were independent organizations run under commercial principles. These assets represented equity investments injected by the Government in these organizations.

14. In response to a question about the rationale for not fully complying with the public sector accounting standards issued by the International Federation of Accountants (IFAC), D/AS said that in formulating the proposals the Task Force had considered the costs and benefits of adopting each of the standards. It concluded that major IFAC standards should be adhered to and applied where appropriate to take into account the particular circumstances of the HKSAR Government. It also noted that the newly promulgated IFAC standards would be subject to revisions in the light of practical experience and changing circumstances. Currently, very few jurisdictions were able to comply fully with the standards.

15. S for Tsy noted members' suggestion that as the proposals in the Report were new to the public, the Government should organize briefings and suitable training for relevant parties such as Members' Assistants and the press to familiarize them with the new accounting practices.

IV Re-ranking of a Deputy Secretary for the Treasury post on a supernumerary basis
(LC Paper No. CB(1) 1144/00-01(04))

16. Members noted the Administration's proposal to upgrade the Deputy Secretary for the Treasury (2) (DS(Tsy)2) post from Administrative Officer (AO) Staff Grade B (D3) to Staff Grade B1 (D4) for a period of three years to reflect the expanded responsibilities of the post.

17. Mr James TIEN expressed support for the proposal. Referring to DS(Tsy)2's responsibility in the management of Government's assets, he enquired about the additional duties to be taken up by the officer concerned in respect of financial negotiations with the newly established Urban Renewal Authority (URA) and how they compared with those of conventional negotiations with statutory bodies, such as the Airport Authority.

18. In response, S for Tsy said that DS(Tsy)2 was in charge of negotiations with concerned parties on arrangements relating to government investments and loans for these bodies. The work involved in financial negotiations would be different depending on the projects to be considered. In respect of the negotiations with the URA, DS(Tsy)2 would assist S for Tsy to examine business plans submitted by the URA and to work out the kind and quantum of financial support to be extended to the organization. DS(Tsy)2 would be responsible for tackling complex financial issues, vetting and assessing the details of over 100 URA projects to be undertaken in future.

19. In response to Mr Henry WU's enquiry, S for Tsy said that the re-ranking of the DS(Tsy) post would be for a period of three years. A review would be conducted towards the end of the period to determine if the post should revert to D3 or remain at D4 level on a permanent basis. As Administrative Officers were general grade staff, if the post had to revert to D3 level, the AO Staff Grade B1 officer occupying the post would be re-deployed to fill another post in the civil service.

V Proper use of the fiscal reserves
(LC Paper No. CB(1) 1144/00-01(05))

20. Members generally were of the view that as Hong Kong had accumulated huge fiscal reserves of over HK\$440 billion, there was considerable room for the Government to earmark more public funds for programmes to improve the livelihood of the general public and to stimulate the economy. However, members noted that in his 1998-99 Budget Speech, FS had defined three purposes for which the fiscal reserves were needed, namely to meet operating, contingency and monetary requirements. The guidelines adopted by the Government in determining the appropriate level of

fiscal reserves was the total of 12 months' government expenditure and the Hong Kong dollar money supply under the M1 definition, allowing a margin of plus or minus 25%. The Administration had explained in the Special Finance Committee meetings held in March 2001 that in order to maintain fiscal prudence in the management of public finances, the Government had to maintain the fiscal reserves at a level within the guidelines.

21. Miss Emily LAU said that there had been no public consultation on the 1998 guidelines on the fiscal reserves and that some reputable academics and experts had commented that the guidelines were inappropriate. She considered that it was high time for the Government to review the guidelines. Miss LAU urged the Government to make reference to the practice of the US Government to undertake regular review on the level of fiscal reserves. She referred to the comments of the US Congress which recognized the importance of using fiscal reserves for the betterment of the economy, and as a means to enhance economic efficiency and to improve the livelihood of the general public.

22. S for Tsy said that the fiscal reserves had been used to finance budget deficits. For instance, the deficit of HK\$23.2 billion in 1998-99 and the estimated deficit of \$7.8 billion in 2000-01 were financed by drawing down the reserves. Moreover, the investment income of the reserves gained each year was used to fund government expenditure. S for Tsy emphasized the importance of maintaining fiscal prudence in the management of public finances through maintaining adequate fiscal reserves. She cautioned that an unhealthy fiscal position would undermine international confidence and lower the credit rating of Hong Kong. This would raise borrowing costs for business and affect economic growth adversely.

23. In respect of the 1998 guidelines, S for Tsy said that while she was not aware of any criticisms from economists or strong objection within the community when the guidelines were announced, the said guidelines were subject to ongoing reviews. However, any guidelines for determining the level of fiscal reserves should not be subject to frequent changes which might adversely affect the credibility of Government's fiscal policy. Bearing in mind changes in the economy since the said guidelines were adopted in 1998 and the views expressed by the public recently, the Government would conduct a review. It would keep an open mind and welcome any views on the subject.

24. On Miss LAU's suggestion for the Government to make reference to the US practices in maintaining its fiscal reserves, S for Tsy said that due to differences in the nature and size of the two economies, it would be inappropriate to make a direct comparison of the fiscal policies of Hong Kong and the US.

25. In reply to Mr James TIEN's enquiry about the appropriate level of fiscal reserves set by the Government under the 1998 guidelines, S for Tsy said that taking 2000 as an example when the total government expenditure and the monetary base of Hong Kong dollar stood at HK\$250 billion and HK\$204 billion respectively, the lower limit of the reserves should be about HK\$340 billion. According to Government's forecast, the fiscal reserves would stand at HK\$427.5 billion by the end of 2004-05. Hence the level was close to the lower limit of the reserves.

26. Mr TSANG Yok-shing questioned the rationale for the 1998 guidelines. Noting that there was a big increase in the fiscal reserves in 1997-98 as a result of the transfer of HK\$197.1 billion from the Hong Kong Special Administrative Region Government Land Fund to the reserves on 1 July 1997, he was of the view that the 1998 guidelines were to rationalize the retention of this vast amount of public money under the fiscal reserves. He further asked what actions the Government would take when the upper or lower limit of the fiscal reserves level was reached.

27. Regarding actions which the Government would take when the upper limit of the fiscal reserves level was reached, S for Tsy said that a range of measures could be considered to enable the public to reap the benefits of economic prosperity. These included introducing tax concessions, reducing fees and charges, etc. However, the Government expected that the problem of operating deficits would continue in the next few years. Therefore, it was unlikely that the upper limit would be reached. On the other hand, it was still unclear whether the problem of operating deficits was cyclical or structural in nature. The Government's Task Force on Review of Public Finances would continue to examine the matter.

28. In reply to Mr Eric LI's enquiry as to whether there were any international standards for determining the appropriate level of fiscal reserves to be maintained by various economies, S for Tsy said that she was not aware of any such standards. She added that the International Monetary Fund (IMF) had been conducting annual examinations on the fiscal positions of various economies. There had never been any comments from the IMF that Hong Kong had maintained excessive fiscal reserves.

29. Mr LEE Cheuk-yan considered that as the current level of EF had reached HK\$1,000 billion, which was well above the level required to provide full backing for the current monetary base of HK\$220 billion to maintain the stability of the Hong Kong dollar, the need of the fiscal reserves for meeting this monetary purpose had already been met. Members considered that the EF was also public money and should be used for the interests of the people of Hong Kong. Mr James TIEN suggested that the accumulated surplus of the EF which amounted to over HK\$300 billion should be used to finance public programmes. Members considered that there should be flexibility for

transferring money from the EF to the general revenue. Mr Albert HO specifically asked whether there were provisions under the EFO to cater for this purpose.

30. S for Tsy said that the EF and the fiscal reserves were invested together by the Hong Kong Monetary Authority, but they were two separate entities. With effect from April 1998, the fiscal reserves placed with the EF enjoyed the same rate of investment return achieved by the entire EF in a year. The decision to place the fiscal reserves with the EF for investment purpose rested entirely with the Government. S for Tsy further explained that the use of the EF was governed by the EFO which stipulated FS as the controller of the Fund. The annual investment income of the EF and the accumulated surpluses were not treated as recurrent income of the Government.

31. Referring to paragraph 14 of the Administration's paper, Ms CHAN Yuen-han considered that the practice of some jurisdictions of setting up stabilization funds to build up the reserves through accumulating budget surpluses to pay for government spending when there was a shortfall in government revenue was more flexible than maintaining the fiscal reserves at a level according to some unscientific guidelines. She opined that such a practice would help adjust government spending in response to changes in the economic situation and fluctuations in the level of revenue.

32. In response, S for Tsy said that published information on practices of overseas jurisdictions in maintaining their fiscal reserves was rather scanty. According to published information, many countries had accumulated fiscal deficits rather than fiscal reserves. As regards Ms CHAN's comment on the stabilization funds, S for Tsy said that it was a common practice for economies with unstable sources of revenue to set up such funds to pay for government spending. According to the observation of the IMF, while the stabilization funds in most cases had contributed to enhancing the effectiveness of fiscal policy by making budget expenditure less susceptible to fluctuations in revenues, it was clear that such funds could not be a substitute for sound fiscal management.

VI Any other business

33. There being no other business, the meeting ended at 1:05 pm.