

# 立法會

## *Legislative Council*

LC Paper No. CB(1)2308/03-04

Ref : CB1/PL/FA

### **Report of the Panel on Financial Affairs for submission to the Legislative Council**

#### **Purpose**

This report gives an account of the work of the Panel on Financial Affairs during the Legislative Council (LegCo) session 2003-04 from October 2003 to June 2004. It will be tabled at the meeting of the Council on 7 July 2004 in accordance with Rule 77(14) of the Rules of Procedure of the Council.

#### **The Panel**

2. The Panel was formed by a resolution passed by the Council on 8 July 1998 and as amended on 20 December 2000 for the purpose of monitoring and examining Government policies and issues of public concern relating to financial and finance matters. The terms of reference of the Panel are at **Appendix I**.

3. For the 2003-04 session, the Panel comprises 18 members, with the Hon Ambrose LAU Hon-chuen and the Hon Henry WU King-cheong elected as Chairman and Deputy Chairman respectively. The membership list of the Panel is at **Appendix II**.

#### **Major work**

##### Hong Kong's economic development

4. During the 2003-04 session, the Panel continued to provide a forum for all Members of LegCo to exchange views with the Financial Secretary (FS) on matters relating to macro economic issues. FS briefed Members periodically on Hong Kong's latest economic situation and new initiatives in managing public finances.

*Revival of Hong Kong's economy*

5. The Hong Kong economy suffered a severe setback caused by the outbreak of the Severe Acute Respiratory Syndrome (SARS) in the first half of 2003. Unemployment rate reached its record high at 8.7% in mid 2003. Fiscal deficit for 2003-04 which was estimated at \$68 billion in March 2003 was expected to reach \$78 billion at the end of the financial year. Public expenditure for 2003-04 was expected to reach \$250 billion after committing \$11.8 billion for the economic relief measures to relieve the hardship of the community and re-launching the economy.

6. Following the delivery of a statement on Hong Kong's economy and management of public finances at the Council meeting on 22 October 2003, the newly appointed FS, Mr Henry TANG, was invited to the Panel to brief Members on the blueprint for reviving the economy and tackling the budget deficit problem. FS reaffirmed the Government's commitment to tackle the deficit problem through revival of economy and controlling public expenditure. Members were aware that implementation of the Closer Economic Partnership Arrangement (CEPA) and allowing individual Mainland tourists to visit Hong Kong would help recovery of Hong Kong's economy. However, amidst rapid economic development in the Mainland, members saw the need for Hong Kong to maintain its overall competitiveness and to capitalize on the new opportunities opened to Hong Kong. FS emphasized the Government's determination to reach a balanced Operating Account by bringing down its operating expenditure to \$200 billion and attaining \$200 billion on the operating revenue by 2008-09. To achieve the target of restoring budget balance, there would be an accumulative reduction of 11% in operating expenditure from 2004-05 to 2008-09. Whilst members echoed the need to address the deficit problem, members reiterated the importance of attracting external investments, reviving the economy and addressing the high unemployment rate. Members were particularly concerned about the adverse impact of reducing public expenditure on the general public, in particular the less privileged class. Some members considered it more appropriate to set the time frame for achieving balance in the consolidated account in 2009-10 and urged the Government to refrain from cutting the expenditure on education, health and welfare services, as well as to ensure cost-effectiveness in utilizing limited public resources. FS took note of members' view and stressed that a pragmatic and measured approach was adopted in implementing expenditure cuts with due regard to community needs.

7. Following the dissipation of SARS, Hong Kong's economy rebounded distinctly since the third quarter of 2003 and gathered further growth momentum in the first quarter of 2004. In June 2004, FS advised the Panel that the Gross Domestic Product (GDP) leaped by 6.8% in real terms in the first quarter of 2004 as compared with 2003. Local consumption and investment spending recovered significantly coupled with strong growth in exports of

goods and services. The up-to-date forecast GDP growth rate for 2004 was 6%. Members noted that the economic support measures including further expansion in the “individual visit” scheme for Mainland visitors to Hong Kong, implementation of CEPA, as well as robust economic growth in the Mainland had benefited Hong Kong’s economy. According to the provisional financial results for the 2003-04 financial year announced by the Government on 28 April 2004, the expenditure for the financial year amounted to \$247.4 billion and revenue amounted to \$207.3 billion, resulting in a deficit of \$40.1 billion.

*Addressing the unemployment problem*

8. Notwithstanding continuous improvement in the overall labour market with the unemployment rate declining from the peak of 8.7% in mid 2003 to 7.1% for the period from February to April 2004, some members were concerned about the worsening structural unemployment problem. They strongly urged the Government to introduce concrete measures to create and increase employment opportunities for the low-income and low-education segments of the work force. In tackling the unemployment problem, FS stressed the role of the Government as the facilitator of the market while the private sector was the main provider of jobs. In addition to providing training and re-training opportunities for workers with low education attainment to improve their employability, the Government was committed to improving the economic and business environment through reviewing regulations and streamlining procedures and requirements with a view to attracting foreign investments and facilitating business operations.

*Management of Public Finances*

9. Noting that part of the Government’s plan to reduce the fiscal deficit was through the selling of Government assets, the Panel studied in detail the various proposals put before the Panel. On the proposal to securitize future revenue receivable from tolls on five tunnels and one bridge, members noted that the proposal aimed to raise \$6 billion to finance capital works projects rather than the Government’s recurrent expenditure. While indicating support for the proposal as a means to address the budget deficit problem, some members cautioned the Government of the constraints imposed on its future transport policy in light of its undertakings to investors. The Administration assured the Panel that relevant bureaux were actively developing a mechanism capable of providing flexibility to the Government in formulating and implementing future transport policy and protecting the interest of investors.

10. The Panel examined and supported the Administration’s proposal to transfer \$40 billion from the Land Fund (LF) to the General Revenue Account (GRA) with a view to meeting the latter’s anticipated shortfall in 2004-05. Members stressed the importance for the Administration to continue adhering to the principle of prudent management of public finances and stepping up its

efforts to address the deficit problem by implementing effective saving measures and exploring new sources of revenue. On the way forward for the LF, while some members considered it advisable to dissolve the fund and transfer the balance to the GRA, there was concern that the dissolution might undermine LegCo's function in monitoring the use of public fund. The Administration undertook to examine the proposal further taking into account members' views.

*Campaign to re-launch Hong Kong's economy and Hong Kong Harbour Fest*

11. Out of the \$11.8 billion economic relief package to help the community to tide over the difficulties arising from the outbreak of SARS, \$1 billion was earmarked for the "Campaign to re-launch Hong Kong's economy" (the Campaign). The Administration's intention was to undertake a comprehensive publicity and promotion campaign locally, internationally and in the Mainland to restore Hong Kong's reputation and get the economy moving again. For this purpose, two ad hoc bodies, including the Economic Relaunch Working Group (ERWG), were formed to provide advice and oversee the implementation of the activities of the Campaign. When the Panel was briefed on this subject on 29 May 2003, one day before the funding proposal was put to the Finance Committee for approval, members noted the wide range of initiatives to help bring various economic activities back to normal and the cultural, media, sports and community programmes to rebuild public confidence in Hong Kong. Members were dissatisfied with the lack of details on the individual projects under the Campaign but had given support to the proposal in view of the need for prompt actions to restore confidence in Hong Kong. Members were therefore gravely concerned when it was reported in the press in summer 2003 that the Government had undertaken to underwrite a revenue shortfall up to \$100 million for Hong Kong Harbour Fest (Harbour Fest). Besides, the high artist fees and confusing ticketing arrangements also aroused considerable public concern and affected Hong Kong's international image.

12. As soon as the new legislative session commenced in October 2003, the Panel reviewed with the Administration the cost-effectiveness of the Campaign. On the activities organized under the Campaign, members expressed serious doubt over the financial arrangements and the cost-effectiveness of some activities, in particular the Harbour Fest. The Panel was advised that among the total of 95 proposals received by ERWG under the Campaign, 84 projects were approved. The Panel was informed by the Administration after the meeting that ERWG had decided not to consider any further proposals under the Campaign. As in early April 2004, the total expenditure for the Campaign was estimated at \$660 million.

13. Regarding organizing and financing the Harbour Fest, members were disappointed to note that the Government had not played an effective role in

monitoring the implementation of the event. The Panel questioned the appropriateness of the Government to underwrite the shortfall of the event and to give a complete free hand to the American Chamber of Commerce in Hong Kong (AmCham) to organize such a large-scale event through a private company, Red Canvas Limited, owned by the then Chairman of AmCham. Given the low attendance rate of 125 900 for the 16 concerts, members further questioned if the objectives of boosting the local economy and promoting tourism had been achieved. In the light of the concern expressed by the Panel and the general public, the Audit Commission commenced a review on the Harbour Fest in late October 2003. In December 2003, the Chief Executive appointed a two-member independent panel of inquiry to investigate into the event.

14. Following the publication of the reports by the Audit Commission and the Independent Panel of Inquiry on the Harbour Fest, the Public Accounts Committee of LegCo and the Panel separately examined the various aspects of issues highlighted in the reports. On 14 June 2004, the Panel invited FS, the Director-General of Investment Promotion (DGIP) who was the Controlling Officer responsible for administering the \$1 billion commitment for the Campaign, and Mr James THOMPSON, former Chairman of AmCham, to explain on the cost benefits of the Harbour Fest, in particular the low viewing rate of the TV special broadcast in USA. While Mr THOMPSON maintained that the event was successfully held, members reiterated that where public funds were involved, it was of paramount importance that all parties should be vigilant in exercising control over the use of tax-payers' money and in achieving the objectives of the project. The Panel noted that in the light of the observations and recommendations of the two reports, the Administration would strengthen measures to improve the process for committing government funds on specific projects and would consider providing training on crisis communication for senior officials. The Panel also noted that investigations on the Harbour Fest were being undertaken by the Police and the Independent Commission Against Corruption.

#### Accrual-based consolidated accounts of the Government

15. The Panel was briefed in January 2004 on the Government's Accrual-based Consolidated Accounts for 2002-03, which was the first set of accrual-based accounts published by the Government. The Panel welcomed the Administration's initiative in publishing the accrual-based accounts in addition to the existing cash-based accounts with a view to enhancing transparency of Government's financial position and performance. Some members expressed concern about the Government's huge liabilities of over \$320 billion for the provision of pensions and untaken leave balance of civil servants, and considered that such liabilities would become a financial burden of Hong Kong. Members requested the Administration to assess Government's pension liability and consider long term strategies in tackling the liability. On the way

forward, the Panel took note of the Administration's undertaking to provide more financial and non-financial information in the accrual accounts for subsequent years, and to conduct a review in 2006-07 taking into account members' views and latest international standards on accrual accounting for the public sector.

### Corporate Governance

16. Recognizing the importance of enhancing corporate governance of companies for upgrading the quality of financial market and reinforcing Hong Kong's status as an international financial centre, the Panel continued to monitor the progress of the implementation of the Corporate Governance Action Plan drawn up by the Administration, the Securities and Futures Commission (SFC), and the Hong Kong Exchanges and Clearing Limited (HKEx) in early 2003. Given the important role played by company directors in enhancing corporate governance of companies, the Panel welcomed the initiative in strengthening the training for directors of listed companies through phased implementation of the Code on Corporate Governance Practices. On tightening the regulation of Initial Public Offering intermediaries including sponsors and financial advisers, the Panel appreciated the initiative of the Hong Kong Society of Accountants (HKSA) in improving the self-regulatory regime of the accountancy profession to enhance the effectiveness and transparency of the regime through introduction of the Professional Accountants (Amendment) Bill 2004, a private Member's bill sponsored by Dr Hon Eric LI. The Panel examined in detail the policy aspects of the Bill and its implications on the accountancy profession and the investing public. The Panel was of the view that as the Bill covered a wide range of proposals, it was more prudent for LegCo to form a Bills Committee to study the Bill. Following the Panel's submission of a report to the House Committee, a Bills Committee was formed to scrutinize the Bill.

17. On the other hand, the Administration conducted public consultation in September 2003 on HKSA's proposal to set up an Independent Investigation Board (IIB) to consider complaints of alleged accounting, auditing and/or ethics irregularities committed by professional auditors involving listed companies, and a proposal initiated by the Standing Committee on Company Law Reform's Phase 1 Corporate Governance Review to establish a Financial Reporting Review Panel (FRRP) to enquire into apparent departures from the law and accounting standards in the annual accounts of companies. While members in general welcomed the two proposals to enhance the public oversight of the auditing profession, members had divergent views on the funding arrangements for the independent governing board overseeing both bodies. While some members considered that the accountancy profession, SFC, HKEx and listed companies should be responsible for the costs involved, some opined that the Government should contribute to the costs, as enhancement of market quality would also help reinforce Hong Kong's

position as an international financial centre. There was also a suggestion that the Administration should recover the costs from fines imposed on parties found responsible for the irregularities. The Panel noted the Administration's view that adoption of the cost-sharing approach would facilitate discussion and achieving a consensus among the parties concerned so as to expedite the formation of IIB and FRRP. Members also noted the Administration's undertaking to continue discussing with the parties concerned on the institutional and funding arrangements before introducing the relevant legislative proposals into LegCo.

18. As regards the improvements to the regulation of listing, the Panel continued to monitor the consultation conducted by the Administration in October 2003. The Administration further consulted the Panel in April 2004 on its recommendations and implementation roadmap on its package of proposals to enhance the regulation of listing. The Panel noted that the Administration had decided to provide more important listing requirements with statutory backing and expand the existing dual filing system. Under the new arrangements, both SFC and HKEx would have a role in administering the listing functions. SFC would be responsible for enforcing the statutory listing requirements and HKEx would continue to enforce the non-statutory listing rules. The Stock Exchange of Hong Kong (SEHK), a subsidiary of HKEx, would continue to receive listing applications at the frontline and all applications remained to be approved by its Listing Committee. Members also noted that the market had indicated support for the proposals. Recognizing that the recommendations would increase the duties of SFC and confer more power on it, some members saw the need to strengthen the existing monitoring system over SFC to ensure the cost-effective deployment of SFC's resources and to enhance checks on its powers.

19. On the enhancement of the transparency of the operation of SFC, the Panel noted that SFC's annual audit reports on HKEx's performance of listing functions would be submitted to FS who would cause the reports to be published, and that SFC's oversight of HKEx's performance of listing functions would be subject to regular review by the Process Review Panel (PRP). In this regard, the Administration also undertook to consider a member's suggestion to expand the membership of PRP. In respect of public concern over possible conflict of interests on the part of the members of SEHK Listing Committee, the Administration agreed to convey to SFC and HKEx a member's suggestion about the need to review the existing system for appointing members to the Listing Committee.

Briefing on the Report of the Securities and Futures Commission on the Recommendations made by the Working Group on Review of the Financial Regulatory Framework for Licensed Corporations

20. With a view to addressing default risks in the securities industry to enhance investor protection, the Panel supported early implementation of enhanced regulatory measures on securities margin finance (SMF) providers. Pointing out that segregation of clients' collateral was the norm for major international financial centres, some members called on SFC to expedite requirement on SMF providers to provide complete segregation of non-borrowing margin clients' collateral. However, some members were aware of industry's concern that the suggestion might impose financial burden on SMF providers. The Panel noted that it remained the long-term goal of SFC to achieve complete segregation of non-borrowing margin clients' collateral so as to meet international standards. SFC also undertook to explore with the market the possible means to improve the present infrastructure to facilitate segregation of clients' collateral.

Hong Kong Monetary Authority

*Work of the Hong Kong Monetary Authority*

21. During the session, the Panel continued to receive briefing from the Chief Executive of the Hong Kong Monetary Authority (CE/HKMA) on the work of HKMA.

22. In the light of the public concern over the case of the Bank of China (Hong Kong) Limited (BOCHK) involving the New Nongkai loan, the Panel examined the regulation of the banking sector, in particular HKMA's approach in supervising authorized institutions (AIs) and its response to the incidents of this nature. Members noted that in the BOCHK case, HKMA had relied on the institution to undertake its own investigation and review on the bank's high level control and credit approval process. Some members were concerned that the lack of representation by the person concerned in the investigation/review and the passive role played by HKMA in this particular case might compromise Hong Kong's position as an international banking centre. HKMA reassured members that in following up the BOCHK case, it discussed with the bank the implementation of the recommendations in the special report and cooperated with the law enforcement authorities in Hong Kong in relation to their investigation. In response to some members' concern over HKMA's capability in supervising AIs based outside Hong Kong, HKMA stressed that it had not encountered any problem in seeking assistance from overseas banking regulators on supervisory matters.



23. On the development of financial infrastructure, CE/HKMA briefed the Panel at an informal meeting in late December 2003 on the proposal of providing personal renminbi (RMB) business in Hong Kong. The Panel welcomed the proposal and considered it a milestone for consolidating Hong Kong's status as an international financial centre. Members further noted that since commencement of the business in January 2004, there had been a steady increase in the use of RMB debit and credit cards by Mainland tourists in Hong Kong. The total outstanding RMB deposits in Hong Kong amounted to about RMB \$6 billion by the end of April 2004.

*Governance of the Hong Kong Monetary Authority*

24. The purchase of permanent accommodation for HKMA using \$3.7 billion from the Exchange Fund (EF) in 2001 aroused public concern about the governance of HKMA, in particular over the lack of public scrutiny of its expenditure. The Panel continued to deliberate on the subject during the current session with FS and CE/HKMA. Although some members considered the present arrangements suitable and effective in ensuring checks and controls over operation of HKMA, some other members requested FS to consider measures to define the powers and functions of HKMA by legislation and to enhance its public accountability, in particular in relation to its remuneration policy for senior staff. In response to members, FS reiterated that it was not appropriate to compare governance arrangements and remuneration across different central banking institutions as they operated in different economies and the situations in their job markets varied considerably. FS emphasized that under the current governing arrangements, the operation of HKMA were subject to the provisions of the Exchange Fund Ordinance (Cap. 66) and the Banking Ordinance (Cap. 155).

25. In monitoring the work and operation of HKMA, the Panel examined HKMA's Annual Report 2003 and sought detailed information on HKMA's operating expenses in performing its functions in relation to EF and its other banking duties. In response to a member's request for more information, CE/HKMA stated that the information provided to the Panel had been endorsed by the Exchange Fund Advisory Committee (EFAC) with due regard to the current policy governing disclosure of information and international standards. CE/HKMA however undertook to convey the request to the Governance Subcommittee of EFAC, which would make recommendations to FS.

*Division of functions and responsibilities between the Financial Secretary and the Monetary Authority in monetary and financial affairs*

26. Following the publication of an Exchange of Letters in June 2003 between FS and the Monetary Authority (MA), the Panel invited FS and CE/HKMA to discuss the details on the division of functions and responsibilities between FS and MA. Members expressed support for the

clear delineation of responsibilities in order to enhance transparency and credibility of policies and efficiency of operations in monetary and financial affairs. As regards safeguards for ensuring the proper discharge of power by FS to override MA's decisions, members noted that such decisions by FS were subject to public disclosure unless they were considered prejudicial to the stability and integrity of the monetary and financial systems of Hong Kong. In respect of a member's suggestion to stipulate in the Exchange of Letters for FS to consult EFAC before excluding such decisions from public disclosure, the Panel noted FS' assurance to consult EFAC on matters relating to exercise of the overriding power. CE/HKMA further explained that the Exchange of Letters had clearly stipulated the role of EFAC in the management of EF.

#### Development in the insurance and mandatory provident sectors

27. The Administration consulted the Panel on the proposal of turning the Insurance Authority (IA) into an independent regulator in the light of international regulatory trends in the insurance industry, recommendations of the International Monetary Fund and the results of a relevant Government's study conducted in 2002. The Panel noted that non-market participants generally found the proposal worth supporting, but there were market concerns over the powers and governance of an independent IA, the funding and cost implication on the insurance industry, as well as the impact on the level of insurance premiums. The Administration assured the Panel that details on the structure, supervisory, reporting and funding arrangements of an independent IA would be specified in relevant legislative amendments if the proposal was to be pursued. It also undertook to consult the Panel again with more detailed information after holding further discussions with the industry.

28. In the wake of the insolvency of three insurers of the HIH Group in 2001, the Administration conducted a feasibility study on establishing insurance policyholders' protection funds (PPFs) in Hong Kong in late 2002 and published a public consultation paper to invite views on related proposals. The Panel noted that while the insurance industry supported establishing PPFs in Hong Kong, there were concerns over problem of moral hazards and the impact on insurance premiums. The Administration undertook to consult the Panel on the way forward after the consultation exercise.

29. The Panel welcomed the proposed issuance of the Code on Disclosure for Mandatory Provident Fund (MPF) Investment Funds (the Code) in June 2004 for compliance by the industry to enhance the disclosure requirements/standards for MPF investment funds in relation to information on fees, charges and performance of MPF funds with a view to facilitating scheme members in making informed MPF investment decisions. To address some members' concern about complaints on the high level of fees charged by scheme trustees in the market, the MPF Schemes Authority agreed to include the issue in the on-going reviews of the MPF system. As regards the concern

about the lack of direct sanctions on trustees for breaching the Code, MPF Schemes Authority undertook to review the need of providing statutory backing for the Code and introducing direct sanctions for breaching the Code in the light of experience in implementing the Code.

Other issues

30. During the 2003-04 legislative session, the Panel also studied other issues such as the comprehensive agreement between the Hong Kong Special Administrative Region of the People's Republic of China and the Kingdom of Belgium for avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income and on capital, which was the first agreement of this kind concluded by Hong Kong with other economies. Moreover, the Panel also examined the policy aspects of a number of private Member's bills, including the Standard Chartered [Bank] (Hong Kong) Limited (Merger) Bill and the Wing Hang Bank Limited (Merger) Bill, before they were introduced into LegCo.

31. The Panel held a total of 13 meetings from October 2003 to June 2004 to examine and monitor the above issues.

Council Business Division 1  
Legislative Council Secretariat  
2 July 2004

**Legislative Council  
Panel on Financial Affairs**

**Terms of Reference**

1. To monitor and examine Government policies and issues of public concern relating to financial and finance matters.
2. To provide a forum for the exchange and dissemination of views on the above policy matters.
3. To receive briefings and to formulate views on any major legislative or financial proposals in respect of the above policy areas prior to their formal introduction to the Council or Finance Committee.
4. To monitor and examine, to the extent it considers necessary, the above policy matters referred to it by a member of the Panel or by the House Committee.
5. To make reports to the Council or to the House Committee as required by the Rules of Procedure.

**立法會  
財經事務委員會  
Legislative Council  
Panel on Financial Affairs**

**2003 至 2004 年度委員名單  
Membership list for 2003 - 2004 session**

<b>主席 Chairman</b>	劉漢銓議員, GBS, JP	Hon Ambrose LAU Hon-chuen, GBS, JP
<b>副主席 Deputy Chairman</b>	胡經昌議員, BBS, JP	Hon Henry WU King-cheong, BBS, JP
<b>委員 Members</b>	丁午壽議員, JP	Hon Kenneth TING Woo-shou, JP
	田北俊議員, GBS, JP	Hon James TIEN Pei-chun, GBS, JP
	朱幼麟議員, JP	Dr Hon David CHU Yu-lin, JP
	何俊仁議員	Hon Albert HO Chun-yan
	李卓人議員	Hon LEE Cheuk-yan
	李家祥議員, GBS, JP	Dr Hon Eric LI Ka-cheung, GBS, JP
	李國寶議員, GBS, JP	Dr Hon David LI Kwok-po, GBS, JP
	吳亮星議員, JP	Hon NG Leung-sing, JP
	涂謹申議員	Hon James TO Kun-sun
	陳智思議員, JP	Hon Bernard CHAN, JP
	陳鑑林議員, JP	Hon CHAN Kam-lam, JP
	單仲偕議員	Hon SIN Chung-kai
	黃宜弘議員, GBS	Dr Hon Philip WONG Yu-hong, GBS
	曾鈺成議員, GBS, JP	Hon Jasper TSANG Yok-sing, GBS, JP
	劉慧卿議員, JP	Hon Emily LAU Wai-hing, JP
	石禮謙議員, JP	Hon Abraham SHEK Lai-him, JP
	(合共： 18 位委員) (Total： 18 members)	
<b>秘書 Clerk</b>	陳美卿小姐	Miss Salumi CHAN Mei-hing
<b>法律顧問 Legal Adviser</b>	顧建華先生	Mr KAU Kin-wah
<b>日期 Date</b>	2003 年 10 月 9 日 9 October 2003	