

立法會

Legislative Council

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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 from October 2004 to June 2005. It will be tabled at the meeting of the Legislative Council (LegCo) on 6 July 2005 in accordance with Rule 77(14) of the Rules of Procedure of LegCo.

The Panel

2. The Panel was formed by a resolution passed by LegCo 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 in **Appendix I**.

3. For the 2004-05 session, the Panel comprises 17 members, with Hon Bernard CHAN and Hon Ronny TONG Ka-wah elected as Chairman and Deputy Chairman respectively. The membership list of the Panel is in **Appendix II**.

Major work

4. During the 2004-05 session, the Panel continued to provide a forum for Members of LegCo to exchange views with the Financial Secretary (FS) on matters relating to macro economic issues. FS briefed the Panel periodically on Hong Kong's latest overall economic situation. The Panel also received regular briefings from the Chief Executive of the Hong Kong Monetary Authority (CE/HKMA) on the work of HKMA, including banking regulation and monetary issues. Moreover, the Panel examined issues relating to corporate governance and investor protection, and a number of other issues.

Hong Kong's economic development

Hong Kong's latest overall economic situation

5. The Panel was pleased to note that the Hong Kong economy was back on an upswing and the Government's fiscal position had improved. The activity upturn was marked by thriving exports and offshore trade, vibrant inbound tourism, strong pick-up in consumer spending, and robust growth in investment. The negative equity problem had eased along with the rise in property prices. The number of residential mortgage loans in negative equity reduced from the peak of around 106 000 cases in June 2003 to around 14 000 cases in March 2005, representing a reduction of 87%. As regards the forecast for 2005, FS advised the Panel in June 2005 that in overall terms, the Hong Kong economy was expected to achieve further growth, with GDP forecast to grow by 4.5% to 5.5%.

Combating poverty and addressing the unemployment problem

6. Despite the economic recovery, the Panel was concerned that the majority of the people in Hong Kong were not able to benefit from the economic recovery. Given the acute widening of the gap between the rich and the poor, members urged the Administration to address the problem. In this respect, FS advised members that the establishment of the Commission on Poverty had reflected the Government's determination to help the poor and address their needs. The Commission agreed that it should use multiple means and channels and actively involve the community to provide the poor with more opportunities, so that they could realize their potential, regain dignity and self-confidence, and move up the social ladder to live a more fulfilled and happier life.

7. The Panel noted that the labour market had improved visibly with the seasonally adjusted unemployment rate falling from the record high of 8.6% in mid 2003 to 6.1% in the first quarter of 2005. Nevertheless, aged workers and workers with low education attainment continued to have great difficulty in getting employed, and even if they were employed, they were paid very low wages. FS pointed out that the Economic and Employment Council had been collaborating with the business community and the labour sector to actively pursue measures to assist the unemployed to find jobs. He stressed that it was the Government's role to facilitate the market, while the private sector was the main provider of jobs. To facilitate workers with low education attainment or low level of skills to find jobs, the Administration would continue to develop the tourism industry to promote employment in the sector. In this connection, FS undertook to consider some members' suggestion that suitable places be identified for the development of hotel resort areas in Hong Kong. As regards the unemployment problem in the construction sector, FS envisaged that the economic upturn would contribute to further revival of the property market and

would therefore help alleviate the problem in the long run. Some members urged that the Administration should capitalize on the large-scale infrastructural projects, such as Hong Kong-Zhuhai-Macau Bridge, cross-border railway network, and development of Lantau Island, to create employment opportunities for local construction workers.

Use of the accumulated surplus of the Exchange Fund

8. Given that the accumulated surplus of the Exchange Fund (EF) amounted to \$420.7 billion as at 31 March 2005, the Panel considered that it was high time for the Administration to review how the accumulated surplus should be used. Noting that section 8 of the Exchange Fund Ordinance (Cap. 66) provided a mechanism for transfer of funds from EF to the general revenue, members requested FS to consider deploying part of the accumulated surplus to meet government expenditure and to finance new initiatives for improving the livelihood of the general public, such as the programmes for combating poverty. In this connection, some members suggested that a fixed rate or fixed sum be transferred from the accumulated surplus to the general revenue. FS however stressed the need for the Government to adopt a prudent approach in setting the appropriate level of EF to be maintained and to boost the financial position of EF for the purposes of maintaining the stability of Hong Kong dollar and the monetary and financial systems in Hong Kong. Given the unpredictability of the international monetary environment, Hong Kong must maintain adequate levels of foreign reserves to ensure the stability of Hong Kong dollar and preserve both local and overseas confidence in the currency. Moreover, the investment income of EF was volatile and unpredictable and was not a stable source of income. FS therefore considered it unnecessary to contemplate making the transfer arrangements as suggested by members. Members urged FS to reconsider the issue, taking into account the motion passed by LegCo on 1 June 2005 urging the Government to, among other things, review the existing methodology for sharing the EF's investment income between the Government and HKMA and allocate more investment income of EF to the Government.

Management of public finance

9. FS, in his Budget Speech delivered on 16 March 2005, pledged that the Government would continue to maintain fiscal discipline and ensure effective use of resources. The Government planned to achieve fiscal balance in the Operating Account by 2008-09 as scheduled, and in the Consolidated Account by 2007-08, one year ahead of the target set in the last budget. The Panel noted that as at end of March 2005, public expenditure for 2004-05 amounted to \$242.2 billion and revenue to \$263.6 billion, resulting in a surplus of \$21.4 billion. The balance of fiscal reserves was \$296 billion.

10. Given that detailed information on government investment incomes was not readily available in the public domain, the Panel was concerned how far such incomes were ploughed back to the General Revenue Account. The Panel therefore invited the Research and Library Services Division of the LegCo Secretariat to conduct a research on the management of government investment incomes. Having examined the research report, members considered that the Administration should put in place a proper mechanism to govern the dividend payout policy of public corporations. The mechanism should cover the circumstances under which the dividends payable to the Government should be paid or waived. Moreover, the Administration should strengthen the role of public officers appointed to public corporations in ensuring the protection of government investment interests.

11. In examining the research report mentioned above, the Panel also expressed concern on related issues, in particular the impact of land grant policy on government revenue, and the principle adopted in the assessment of land premium. Given that land and revenue generated from its sale were important sources of income for the Government, members were of the view that the Administration should ensure the effective use of the limited land resources and that its land grant policy was able to safeguard public interest and maximize financial gains for the community. In this connection, members considered that the policy of subsidizing commercially operated infrastructural projects in the form of land, which was a remnant of the colonial era, no longer suited the present day circumstances. In particular, it was unjustified for the Government to apply the policy to the Mass Transit Railway Corporation Limited since the listing of the corporation in October 2000. Members also shared the Hong Kong Institute of Surveyors' concern that the application of the "green field site" principle in the premium assessment for the two railway corporations imposed an important assumption (i.e. no railway development) into the valuation process and thus would have significant implications for the premium assessment. Other things being equal, the availability of railway development would normally enhance accessibility and thus land values. In other words, the application of the "green field site" principle in the premium assessment for the two railway corporations had resulted in the loss of revenue. The Administration was requested to address these concerns.

Budget-related proposals

12. The Panel followed up on two initiatives mentioned by FS in his 2004-05 Budget Speech, namely, the proposed introduction of the new Personalized Vehicle Registration Marks (PVRM) Scheme to raise revenue for the Government, and the study conducted by an internal committee of the Government on the implementation of a goods and services tax (GST) in Hong Kong to broaden the tax base.

13. On the proposed PVRM Scheme, members expressed various concerns about the proposed scheme, particularly about its cost-effectiveness, and its impact on the income of the Lotteries Fund, law enforcement and intellectual property rights. Some members stated objection to the proposed scheme, and some doubted the effectiveness of the scheme in raising revenue and whether the proposal was worth supporting. The Panel therefore urged the Administration to review its proposal. The Administration subsequently reviewed the features of the proposed scheme in the light of members' views and incorporated the proposal in the Revenue (Personalized Vehicle Registration Marks) Bill 2005 presented to LegCo on 4 May 2005. The Bill was being scrutinized by a bills committee formed by LegCo.

14. As regards the study on the implementation of GST in Hong Kong, the Panel noted that the Government's internal committee had completed the study. Whilst agreeing that the Government should explore means to broaden the tax base, some members expressed reservation on whether GST was a suitable measure to tackle the fiscal deficit problem. Some members did not support the introduction of GST. The Panel was assured by FS that given the far-reaching impacts of GST on the local tax regime and Government's financial health, the Government would listen carefully to the views of the public. It would conduct a public consultation on the subject later this year.

15. FS, in his 2005-06 Budget Speech, highlighted the on-going initiatives of the Administration to build on Hong Kong's strength as an international financial centre and the premier capital formation centre for the Mainland, and to further promote the development of Hong Kong as an international asset management centre. In this connection, FS put forward two proposals: abolition of estate duty and exemption of offshore funds from profits tax. Some members were concerned that these two proposals would only benefit the middle and wealthy classes. On the former proposal, some members considered it not justified to abolish the estate duty, and that the abolition was inconsistent with the Administration's objective of broadening the tax base. The proposal was subsequently incorporated in the Revenue (Abolition of Estate Duty) Bill 2005 presented to LegCo on 11 May 2005. The Bill was being scrutinized by a bills committee formed by LegCo.

16. As regards the proposal of exempting offshore funds from profits tax, the Panel requested the Administration to quantify the economic benefits of the proposal and set out the financial implications of the proposal, including the estimated amount of tax revenue foregone. On the Administration's proposal to apply the proposed exemption with retrospective effect to the year of assessment commencing on 1 April 1996, members were concerned about the impact of the proposal on tax revenue and whether the Government would be required to refund the profits tax collected from offshore funds since 1 April 1996. Members considered that as a matter of principle, legislative provisions should take effect from the enactment of the legislation and should not have

retrospective effect. The Administration undertook to take into account members' views in finalizing the details of the proposal.

Corporate governance

17. Recognizing the importance of enhancing corporate governance of companies for upgrading the quality of the financial market and reinforcing Hong Kong's status as an international financial centre, the Panel continued to monitor the progress of various initiatives put forward by the Administration for the purpose. On the initiative to enhance the regulation of listing, the Panel supported the Administration's proposal to amend the Securities and Futures Ordinance (SFO) (Cap. 571) to give statutory backing to major listing requirements, including those relating to financial reporting and other periodic disclosure (such as annual and interim reports), disclosure of price-sensitive information, and shareholders' approval for notifiable transactions. However, the Panel noted that while a vast majority of the submissions received by the Administration during the public consultation exercise expressed support for the proposal for empowering the Market Misconduct Tribunal to impose civil fines on issuers and directors for breaches of the statutory listing rules made by the Securities and Futures Commission (SFC), there were different views on whether SFC should be given such power. Some members of the Panel also had reservation on the need and merits of the proposal of giving SFC such power, and some considered it necessary to enhance the checks and balances on SFC's power in the regulation of listing. The Administration undertook to consider the views and concerns expressed by the Panel and various parties carefully before making a decision on the matter.

18. The Panel also examined the Administration's proposal of splitting the chairman post of SFC into a non-executive chairman post and a chief executive officer (CEO) post to improve SFC's governance structure. The Panel noted that while all SFC Board members agreed to the split in principle, they were concerned how the actual functions could be split between the chairman and CEO posts, and the current chairman of SFC considered that the new chairman post should be executive. Some members of the Panel expressed similar views. They were also concerned that the splitting arrangement, though applied to some public bodies in Hong Kong, might not be suitable for SFC which was a statutory regulator. In this connection, overseas experience did not show that the splitting arrangement was a global practice commonly adopted by securities and futures regulators. Changing the chairman post of SFC to a non-executive post might have negative impact on SFC's international status. Moreover, there was no major problem identified in the existing governance structure of SFC which would justify the implementation of such a significant change to its governance structure shortly after the commencement of SFO in 2003. However, other members supported the splitting proposal in principle for enhancing the governance structure of SFC. The Panel finally passed a motion by a majority vote supporting the proposal in principle. The

proposal was subsequently incorporated in the Securities and Futures (Amendment) Bill 2005 presented to LegCo on 6 April 2005. The Bill was being scrutinized by a bills committee formed by LegCo.

19. On the Administration's proposal of establishing the Financial Reporting Council (FRC), a great majority of members indicated their support for the proposal in principle for enhancing the oversight of the public interest activities of auditors and the transparency of the self-regulatory regime of the accounting profession, and speeding up the investigation of suspected cases of accounting irregularities. Some members however expressed concern about the proposal, in particular, the possible overlap of investigatory functions of the FRC, the Hong Kong Institute of Certified Public Accountants (HKICPA) and SFC, and whether the function of the FRC should be purely investigatory. The Panel requested the Administration to explore, in consultation with HKICPA, how the concerns could be addressed.

Monetary issues

20. Given the increasing acceptance of Renminbi (RMB) for retail transactions in Hong Kong and the growing economic integration between the Mainland and Hong Kong, the Panel was concerned whether Hong Kong dollar would be pegged with RMB and in this connection, whether the Administration would review the Linked Exchange Rate (LER) System. The Panel was advised by CE/HKMA that in view of the small size and external-oriented nature of Hong Kong's economy, a stable currency maintained under the LER System was vital for Hong Kong to withstand external volatility. As US dollar was a strong and powerful currency in the global financial market and RMB exchange rate was linked to US dollar to some extent, the increasing use of RMB in Hong Kong and the increase in the flexibility of RMB exchange rate should not undermine the Administration's determination to maintain the LER System.

21. On 18 May 2005, HKMA announced the introduction of three refinements to the operation of the LER System. The refinements aimed at removing uncertainty about the extent to which the exchange rate might strengthen under the LER System and promoting the smooth functioning of the money and foreign exchange markets in accordance with the Currency Board arrangements. HKMA was invited to brief the Panel in July 2005 on the details and impact of the three refinements.

Regulation of the banking sector

22. The Panel supported the implementation of the New Basel Capital Accord (i.e. Basel II) in Hong Kong for improving risk management of banks and keeping in pace with international developments. On the proposal to provide the Monetary Authority (MA) with the statutory power to raise the

upper end of the minimum capital adequacy ratio (CAR) for individual licensed banks from 12% to 16%, members were concerned under what circumstances the MA would exercise such power. The Panel was advised that at present, the MA was able to require licensed banks to raise their minimum CARs above the 12% ceiling by mutual agreement under special circumstances, such as the Asian Financial Crisis, to reflect the risks they faced. HKMA considered it necessary to provide the MA with the statutory power to raise the minimum CARs to address risks in the banking industry should circumstances warranted. Whilst members had no objection to this proposal, they stressed the importance for the MA to exercise its statutory power in a fair and consistent manner. The relevant proposals about the implementation of Basel II were subsequently incorporated in the Banking (Amendment) Bill 2005 presented to LegCo on 6 April 2005. The bills committee formed to study the Bill supported the Bill (with some proposed Committee Stage amendments) and the Administration's proposal that the Second Reading debate on the Bill be resumed on 6 July 2005.

23. In examining the policy issues arising from the destruction of rented safe deposit boxes by DBS Bank (Hong Kong) Limited (DBS) in October 2004, the Panel noted that banks providing safe deposit box service generally included an exemption of liability clause in their contract with customers. Some of these clauses purported to exclude or restrict a bank's liability even in the case of loss or damages caused by negligence of the bank or its staff. However, under section 7(2) of the Control of Exemption Clauses Ordinance (CECO) (Cap. 71), a party to a contract could not by reference to any contract term excluded or restricted his liability for negligence except in so far as the term or notice satisfied the requirement of reasonableness. Section 5.5 of the Code of Banking Practice (the Code) also provided that, in drawing up their terms and conditions for banking services, AIs should have due regard to applicable laws in Hong Kong, including the CECO. Members therefore queried whether the exemption of liability clause had breached the Code. The Panel was advised that HKMA had requested all AIs to undertake a comprehensive review of terms and conditions for safe deposit service and other banking services so as to ensure that they were consistent with the Code. Upon review, of the 27 authorized institutions (AIs) providing safe deposit box service, 24 were required to amend their safe deposit box agreements to comply with the Code. 22 of the 24 AIs had amended their exemption of liability clauses such that they would not seek to exclude or restrict their liability in cases where the damage was caused by AIs' own negligence, and the remaining two AIs had decided to terminate their safe deposit box service shortly.

Investor protection

24. In the last session, with a view to addressing default risks in the securities industry to enhance investor protection, the Panel expressed its support for the early implementation of the enhanced regulatory measures on

securities margin finance providers. In the current session, the Panel followed up on the outcome of the public consultation exercise conducted by SFC. The Panel was advised by SFC that all respondents generally accepted the rationale that the proposed reforms would enhance investor protection. However, as the respondents had different views on the proposals of imposing a re-pledging limit and increasing Financial Resources Rules haircut percentages, SFC would continue dialogue with the industry to identify the most suitable measures for reducing risks and give the industry a reasonable transitional period for accommodating changes to the existing practice. Pointing out that the practice of pooling and re-pledging of non-borrowing clients' collateral was unfair to clients and infringed their rights, members urged that the Administration and SFC should work out a concrete timetable for abolishing such a practice and achieving complete segregation of borrowing and non-borrowing margin clients' collateral. The Administration and SFC were invited to report progress to the Panel before the end of 2005.

25. The Panel also followed up on SFC's review of the level and funding of the Investor Compensation Fund (ICF), and review of the major broker defaults since 1998. On the review of the ICF, some members expressed support for the proposal to introduce an automatic levy triggering mechanism in order to increase transparency of the operation of the ICF, and the proposal to suspend the levies if the net asset value of the ICF exceeded \$1.4 billion. The Panel noted that the Administration would consult the public on these proposals. The relevant rule amendments were subsequently gazetted on 30 June 2005 and would be tabled at LegCo on 6 July 2005. As regards the review of the major broker defaults since 1998, some members were concerned whether SFC would introduce legislative amendments concerning clients' proprietary rights in shares. The Panel was advised that the case law in Hong Kong had established that clients had individual proprietary rights in the securities held on their behalf by their brokers. In the six broker defaults since 1998, the courts had held that shares should be allocated and distributed to clients as far as possible based on the principle of individual proprietary rights in shares. However, the Financial Markets Law Committee in the United Kingdom (UK) had recently issued a consultation paper on the analysis of the need for and nature of legislation relating to property interests in indirectly held investment securities. The paper recommended that unless otherwise agreed, investors in a particular issue of securities held by an intermediary in a common pool had co-proprietary interests in the pool. SFC would closely monitor the development of the issue in the UK. Should the above mentioned recommendation be adopted, SFC would re-consider its position on whether the existing law in Hong Kong should be changed.

Other issues

26. During the 2004-05 session, the Panel also studied and indicated its support for the following financial or legislative proposals:

- (a) Proposal for Hong Kong to contribute US\$19.19 million to the 8th replenishment of the Asian Development Fund (ADF IX) of the Asian Development Bank (ADB) over a ten-year period;
- (b) Proposed revision of 35 items of fees and charges for certain public services under the purview of the Treasury Branch of Financial Services and the Treasury Bureau which did not directly affect people's livelihood or general business activities;
- (c) Proposal of re-structuring the filing fees for non-Hong Kong companies; and
- (d) Proposal of improving the disclosure of interests regime under Part XV of SFO.

27. Moreover, the Panel also examined the policy aspects of a number of private Member's bills, including the Citibank (Hong Kong) Limited (Merger) Bill and the Industrial and Commercial Bank of China (Asia) Limited (Merger) Bill, before they were presented to LegCo.

28. The Panel held a total of 13 meetings from October 2004 to June 2005, including one held jointly with Panel on Planning, Lands and Works, to examine and monitor the above issues.

**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**

**2004 至 2005 年度委員名單
Membership list for 2004 - 2005 session**

主席 Chairman	陳智思議員, JP	Hon Bernard CHAN, JP
副主席 Deputy Chairman	湯家驊議員, SC	Hon Ronny TONG Ka-wah, SC
委員 Members	田北俊議員, GBS, JP	Hon James TIEN Pei-chun, GBS, JP
	何俊仁議員	Hon Albert HO Chun-yan
	李卓人議員	Hon LEE Cheuk-yan
	李國寶議員, GBS, JP	Dr Hon David LI Kwok-po, GBS, JP
	涂謹申議員	Hon James TO Kun-sun
	陳鑑林議員, JP	Hon CHAN Kam-lam, JP
	單仲偕議員, JP	Hon SIN Chung-kai, 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
	林健鋒議員, SBS, JP	Hon Jeffrey LAM Kin-fung, SBS, JP
	梁君彥議員, SBS, JP	Hon Andrew LEUNG Kwan-yuen, SBS, JP
	黃定光議員, BBS	Hon WONG Ting-kwong, BBS
	詹培忠議員	Hon CHIM Pui-chung
	鄭經翰議員	Hon Albert Jinghan CHENG
	譚香文議員	Hon TAM Heung-man
	(合共： 17 位委員)	
	(Total： 17 members)	
秘書 Clerk	陳美卿小姐	Miss Salumi CHAN Mei-hing
法律顧問 Legal Adviser	顧建華先生	Mr KAU Kin-wah
日期 Date	2004 年 10 月 12 日 12 October 2004	