

立法會
Legislative Council

LC Paper No. CB(1)2350/06-07

(These minutes have been seen
by the Administration)

Ref : CB1/PL/FA/1

Panel on Financial Affairs

**Minutes of special meeting
held on Friday, 20 July 2007 at 9:00 am
in Conference Room A of the Legislative Council Building**

- Members present** : Hon CHAN Kam-lam, SBS, JP (Chairman)
Hon Bernard CHAN, GBS, JP (Deputy Chairman)
Hon James TO Kun-sun
Hon SIN Chung-kai, SBS, JP
Hon Emily LAU Wai-hing, JP
Hon Abraham SHEK Lai-him, SBS, JP
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon WONG Ting-kwong, BBS
Hon TAM Heung-man
- Members absent** : Hon James TIEN Pei-chun, GBS, JP
Hon Albert HO Chun-yan
Ir Dr Hon Raymond HO Chung-tai, SBS, S.B.St.J., JP
Dr Hon David LI Kwok-po, GBM, GBS, JP
Hon Andrew LEUNG Kwan-yuen, SBS, JP
Hon Ronny TONG Ka-wah, SC
Hon CHIM Pui-chung
- Public officers attending** : Agenda Item I

Professor K C CHAN
Secretary for Financial Services and the Treasury

Mr Kevin HO
Permanent Secretary for Financial Services and the
Treasury (Financial Services)

Mr Alan LAI
Permanent Secretary for Financial Services and the
Treasury (Treasury)

Miss Alice CHEUNG
Administrative Assistant to Secretary for Financial
Services and the Treasury

Clerk in attendance: Miss Polly YEUNG
Chief Council Secretary (1)5

Staff in attendance : Ms Annette LAM
Senior Council Secretary (1)3

Ms Sharon CHAN
Legislative Assistant (1)8

Action

I. Briefing by Secretary for Financial Services and the Treasury

(LC Paper No. CB(1)2137/06-07(01) — Paper provided by the
Administration)

Briefing by the Secretary for Financial Services and the Treasury

At the invitation of the Chairman, the Secretary for Financial Services and the Treasury (SFST) briefed members on the major policy initiatives under his purview. On the area of financial services, SFST advised that the Administration would continue with its work towards the goal of building Hong Kong as China's international financial centre (IFC). He highlighted the progress and upcoming plans under two major policy directions, as follows:

- (a) Facilitating market development
- (i) The action agenda proposed by the Focus Group on Financial Services established under the Economic Summit on "China's 11th Five-Year Plan and the Development of Hong Kong" in January 2007 comprised 80 recommendations on how the Hong Kong Special Administrative Region (HKSAR) could contribute to the economic development and financial reform of the Mainland through strengthening its status as China's IFC. Action had been initiated for 30 of the recommendations, and the Administration would continue to

follow up the other proposals in collaboration with the financial services industry and relevant authorities.

- (ii) Strengthening financial cooperation between Hong Kong and the Mainland through developing a complementary, cooperative and interactive relationship between the financial systems of Hong Kong and the Mainland.
 - (iii) Consolidating Hong Kong's position as Asia's leading asset management centre. In this connection, following the abolition of estate duty and the exemption of offshore funds from profits tax, there had been significant growth in Hong Kong's asset management business, with an increase of 36% in the size of Hong Kong's combined fund management business in 2006 compared with 2005. The expansion of the Qualified Domestic Institutional Investors Scheme and the further implementation of the Closer Economic Partnership Arrangement with the Mainland would open up ample business opportunities for the financial services industry of Hong Kong.
 - (iv) Broadening the source of listed companies to facilitate listing of overseas companies in Hong Kong.
 - (v) Enhancing the development of the bond market through measures such as providing the necessary financial infrastructure.
 - (vi) Expanding renminbi (RMB) business in Hong Kong, including the issue of RMB bond in end June 2007. The Administration was also in discussion with the Mainland authorities on the proposal of allowing Hong Kong importers to settle direct import trade from the Mainland in RMB.
 - (vii) Promoting Hong Kong as an IFC in the Mainland and overseas. In this connection, preparation for the Asian Financial Forum scheduled on 21 September 2007 was underway.
- (b) Improving market quality
- (i) On enhancing corporate governance and financial reporting, the new Financial Reporting Council, which had recently commenced operation, would help to upgrade the regulation of the accounting profession and the quality of financial reporting of locally listed companies.

- (ii) On enhancing investor protection and education, the Securities and Futures Commission (SFC) would strive to strengthen its regulatory and enforcement work having regard to public concern about the investigation process. SFC would also explore ways of utilizing part of its levy income to enhance investor protection and education.
- (iii) On improving market efficiency, various initiatives such as streamlining the licensing procedures for overseas fund managers had been implemented.
- (iv) On improving the operation of the Mandatory Provident Fund (MPF) System, the Mandatory Provident Fund Schemes Authority (MPFA) was consulting the industry and relevant stakeholders on the feasibility of allowing employees to choose their MPF trustees and would submit a proposal to the Administration. In addition, the Administration was considering the MPFA's proposal to increase the penalty against employers who had failed to register their employees on MPF schemes or who had defaulted MPF contributions in order to put the penalty on a par with that for wage defaults under the Employment Ordinance (Cap. 57). Members' views on MPFA's proposal were welcome.
- (v) On providing statutory backing for major listing requirements, the Administration intended to conduct further market consultation on the details of the legislative proposal.
- (vi) On the implementation of Basel II since January 2007, the Hong Kong Monetary Authority (HKMA) would continue to monitor the progress of implementation.
- (vii) On the Companies Ordinance (Cap. 32) (CO) rewrite exercise, work had commenced in mid-2006 and was progressing according to schedule.

2. SFST also gave a brief account of the work on the management of public finance. He recapped the policy objective of maintaining a sound and healthy public finance for Hong Kong guided by three major principles, i.e. maintaining strict fiscal discipline; efficient use of public finance and adhering to a low and simple tax regime. Nevertheless, he highlighted the need to give consideration to options for broadening the tax base so as to meet the challenges posed by a rapidly ageing population and rising medical costs in the long run. During the nine-month public consultation ended in March 2007, the community had a general recognition of the problem of a narrow tax base in Hong Kong, although no consensus had been reached on the measures to be adopted to broaden the tax base. The Administration would further examine the propriety and implications of different tax options having regard to public views collected.

Discussion

Declaration of interests by Principal Officials

3. Ms Emily LAU thanked SFST for attending the meeting and sharing his visions and plans with the Panel. She also hoped that SFST would make the best endeavour to attend future meetings of the Panel. Ms LAU referred to the existing requirements on declaration of investments and interests by Principal Officials and recapped that the subject would be further discussed at the coming meeting of the Panel on Constitutional Affairs. Noting media reports that the spouse of SFST held a senior position in a private investment firm, Ms LAU sought SFST's view on the adequacy or otherwise of the prevailing requirements and whether they should be further strengthened to safeguard against conflict of interests arising from the work of the Principal Officials and that of their close family members such as spouse.

4. In reply, SFST said that Principal Officials were subject to very stringent declaration requirements under the existing declaration regime, which had been working effectively all along. As to his personal circumstances, SFST pointed out that there was an effective "firewall" in place under the current system to safeguard against conflict of interests between his family or personal affairs and his public office.

5. In this regard, Ms Emily LAU opined that senior officials should be sensitive and take heed of any real or perceived conflict of interests arising from their official capacity. She urged SFST to note her concern and pay special attention to such matters as a new Principal Official under the accountability system. SFST noted Ms Emily LAU's view and concern.

Hong Kong's position as an international financial centre and asset management centre

6. Referring to the Strategic Economic Dialogue (SED) between the United States (US) and China to map out their bilateral economic relationship, Mr Bernard CHAN was concerned whether and how the financial services sector of Hong Kong could make the best use of the opportunities under SED in the near future. In reply, SFST highlighted that the said SED would provide ample opportunities as well as challenges for the financial services industry of Hong Kong. To maintain its position as an IFC, Hong Kong had to enhance its competitiveness and facilitate the development of a more globalized economy in the Mainland.

7. The Chairman opined that an important initiative to enhance Hong Kong's IFC status was the development of a futures market for commodities, such as petroleum futures. In response, SFST advised that the development of the futures market was included in the 11th Five-Year Plan. The Administration had noted the proposal from the Democratic Alliance for the Betterment and Progress of Hong

Kong on the development of a petroleum futures market in Hong Kong, as well as the views of the financial services industry. As a first step, the Hong Kong Exchanges and Clearing Limited had appointed consultants to study the feasibility of developing a commodities futures market in Hong Kong.

8. Noting that the abolition of estate duty in 2006 had attracted foreign funds into the Hong Kong market, Mr Jeffrey LAM enquired whether there were other measures to further strengthen Hong Kong's position as an asset management centre. Mr LAM opined that measures to facilitate market development should be formulated having regard to the uniqueness of the Hong Kong market instead of merely replicating the practices of overseas jurisdictions.

9. In response, SFST pointed out that the effectiveness of the policy initiatives in consolidating the position of Hong Kong as Asia's leading asset management centre was evident in the growth of the capital market in the past few years. Looking ahead, Hong Kong could further expand the scale of its asset management business in the light of the abundant inflow of capital from the Mainland. To cater for the needs of the local market, he assured members that the Administration would seek the views of the financial services industry when formulating suitable measures to facilitate the development of the asset management business.

10. Mr SIN Chung-kai was concerned whether Hong Kong had achieved an actual increase in asset management activities, or whether it was merely functioning as the marketing and sales centre of fund management firms based in overseas financial centres such as London and New York. He was concerned about the prospect of consolidating Hong Kong's development into an important asset management centre in the region.

11. In reply, SFST advised that the rapid growth in Hong Kong's fund management business was attributable to the globalization of financial services, under which many international institutional investors had chosen Asia as their platform for investment. Hong Kong possessed a number of unique advantages (including financial infrastructure and free flow of investment information) to attract overseas fund management firms to set up headquarters or regional offices to develop their business in Asia and the Mainland. He confirmed that there had been an actual increase in fund management activities in Hong Kong in recent years and assured members that the Administration would continue its efforts to facilitate the development of asset management business in Hong Kong.

Operation of the Mandatory Provident Fund System

12. Mr Jeffrey LAM expressed concern about the high management fees charged by MPF service providers in general and considered that the Administration should work closely with MPFA to devise suitable measures for ensuring that the investment return for the MPF schemes should be commensurate with the level of management fees charged by trustees.

13. In reply, SFST said that he shared Mr Jeffrey LAM's observation that the management fees of MPF schemes were generally on the high side. He pointed out that the higher fees might be attributable to the set up costs during the first few years of operation of the MPF schemes. Now that the MPF System had been in operation for some seven years since 2000, the MPF market was more competitive. Market forces and greater choices for MPF scheme members would help lower the level of management fees charged.

14. Referring to members' majority view expressed at the first meeting of the Bills Committee on Mandatory Provident Fund Schemes (Amendment) Bill 2007 that employees should be given the right to choose their MPF service providers, Mr SIN Chung-kai called on the Administration to expedite preparation of the relevant bill so that its scrutiny could be completed within the remaining session (i.e. 2007-2008 session) of the current term. Miss TAM Heung-man expressed similar concern and enquired about the timeframe for introducing the bill.

15. Mr Bernard CHAN declared that his company was a MPF service provider. While he had no objection in principle to the proposal of allowing employees to choose their own service providers, he cautioned that higher administrative costs might be incurred for employers to make MPF contributions to different service providers of their employees' choices. Mr CHAN considered it important to work out details of the proposal with the stakeholders, notably MPFA and representatives of employers and employees. He further pointed out that under the existing arrangements, although employees could not choose their own MPF service providers, they could choose from the investment funds operated by the service providers.

16. SFST said that he was well aware of the concern of Members of the Legislative Council (LegCo) and the community about measures to enhance the operation of the MPF System. He assured members that the Administration attached importance to this subject and that the MPFA was examining in conjunction with the industry the feasibility of allowing employees the choice of MPF service providers. SFST however pointed out that given the complexity involved, the Administration had not set a timetable for introducing the relevant legislative amendments to this effect. He advised that apart from introducing legislative amendments, the interests of scheme members could also be enhanced through non-legislative means such as by increasing market competition and transparency, as well as encouraging MPF service providers to provide greater choices to scheme members. He believed that MPFA was continuing its effort in this regard.

Rewrite of the Companies Ordinance

17. Noting the Administration's plan to introduce the new legislation into the LegCo in 2010, Miss TAM Heung-man expressed concern about the slow progress

of the CO rewrite exercise and doubted whether Hong Kong's competitiveness would be undermined as it had lagged behind other jurisdictions in the region (such as Singapore) in modernizing the company law. Mr Jeffrey LAM also expressed concern about the CO rewrite exercise and called on the Administration to give due consideration to the views and concerns of operators of small and medium enterprises in taking forward the exercise.

18. In response, SFST advised that given the scope and complexity of the rewrite exercise, the Administration would take forward the exercise in a comprehensive manner to enhance corporate governance and compliance. He assured members that in the process, the Administration would conduct thorough consultation with stakeholders and would issue a White Bill in mid-2009 for public consultation. In this connection, the Permanent Secretary for Financial Services and the Treasury (Financial Services) (PS(FS)) supplemented that the Administration had set up a number of Advisory Groups to gauge the views of the relevant industries and stakeholders in the rewrite exercise. Moreover, several topical public consultation exercises would be conducted. The first topical consultation exercise on the proposals to improve the accounting and auditing provisions had been conducted according to schedule. PS(FS) further informed members that the rewrite exercise had been in smooth progress and the White Bill was expected to be issued in mid-2009 as planned.

Enforcement actions taken by securities regulators

19. Noting the lengthy investigation into cases of alleged market misconduct, Ms Emily LAU doubted whether the current procedures could provide adequate protection to the investors, in particular for cases involving insider dealings.

20. SFST said that as far as investigation of market misconduct was concerned, a set of established procedures was in place. However, completion of investigation would take time given the stringent thresholds in areas such as collection of evidence and the complexity of the issues involved in some cases of suspected breaches. The Administration was equally concerned about the investigation of suspected regulatory breaches and had engaged SFC in discussion of how the investigation procedures could be improved.

21. Mr James TO said that as far as he knew, cross-border mechanisms were in place in some overseas jurisdictions such as US, which enabled the securities regulator to follow up cases of regulatory breaches outside their jurisdiction. In this connection, Mr TO was concerned about the difficulties encountered by the enforcement agencies in Hong Kong in following up cases of suspected regulatory breaches across the border. As there were a large number of Mainland corporations listed in Hong Kong, Mr TO considered it necessary for the securities regulators in Hong Kong and the Mainland to establish an effective arrangement for cross-border cooperation in the investigation and enforcement of suspected regulatory breaches. He called on SFST to step up efforts at the top government level to strengthen financial cooperation between Hong Kong and the Mainland,

particularly in cross-border enforcement. Mr SIN Chung-kai shared Mr TO's concern about the need to step up cooperation in cross-border enforcement.

22. In response, SFST advised that locally listed companies, irrespective of whether they were incorporated in Hong Kong or in other places, were subject to the same regulatory requirements under the Securities and Futures Ordinance (Cap. 571) and the Listing Rules. The regulators would take appropriate actions to follow up cases of suspected regulatory breaches. In this regard, PS(FS) pointed out that while the enforcement agencies in Hong Kong would spare no effort in following up cases of suspected regulatory breaches both within and outside Hong Kong, they would have to rely on the assistance of the authorities in the places concerned in taking actions outside Hong Kong. SFST and PS(FS) noted the concern of Mr James TO and Mr SIN Chung-kai and confirmed that the HKSAR Government would continue to work with the relevant authorities in the Mainland with a view to strengthening cooperation.

Challenges in public finance management

23. Noting the three challenges faced by the Government in managing public finance, Miss TAM Heung-man was concerned whether the Administration would consider the introduction of new taxes such as the goods and services tax (GST) to broaden the tax base so as to balance recurrent public expenditure with government revenue. Whilst appreciating the need to broaden the tax base, Mr WONG Ting-kwong opined that it was necessary to identify the most appropriate tax option. Mr WONG also enquired whether SFST would plan to re-introduce GST as an option during his term of office and whether other options such as the capital gains tax would be considered. Ms Emily LAU considered that "affordability" or "ability-to-pay" should be the guiding principle in considering options to broaden the tax base. Pursuant to this principle, Ms LAU said that the Administration should consider progressive taxes such as capital gains tax or progressive rates of profits tax instead of regressive tax like GST which would only aggravate income disparity.

24. SFST confirmed that maintaining fiscal balance was the Government's clear policy objective in the management of public finance. Nevertheless, various challenges such as an ageing population had posed a challenge to public finance and demonstrated the need to address the problems arising from the current narrow tax base. SFST recalled that different views on the pros and cons of various tax options had been received during the public consultation on tax reform which ended in March 2007, but no consensus on the best option to broaden the tax base had been reached. For example, there were views against GST, as well as views that capital gains tax was not conducive to maintaining the position of Hong Kong as an IFC. Given the recent economic upturn, the problems associated with a narrow tax base might not be acute in the immediate term but as a responsible government, further examination of measures to address the problem was necessary with regard to relevant considerations such as the community's "ability-to-pay" and public acceptability.

25. Referring to recent discussions in the community on introducing a mandatory medical insurance scheme in the light of an ageing population and rising medical costs, Mr WONG Ting-kwong opined that the contributions payable for medical insurance in addition to MPF contributions might add to the financial burden of employees. Ms Emily LAU also expressed concern about the proposed reform of the health care financing system in Hong Kong. Ms LAU recalled that during an earlier meeting between the Panel on Health Services and the Bauhinia Foundation Research Centre on the latter's report on "Development and financing of Hong Kong's future health care", she had noted that contrary to the general impression that health care services in Hong Kong were heavily subsidized by the Government, over 40% of the medical costs under the current system was in fact borne by the community.

26. In this connection, SFST said that the issue of health care financing was outside the purview of the Financial Services and the Treasury Bureau (FSTB). However, he was aware that the proposal of a mandatory medical insurance scheme had yet to be considered in the light of public views

27. Miss TAM Heung-man recalled that LegCo had passed a motion in the 2004-05 session urging the Government to examine specific issues relating to Hong Kong's taxation system and the implementation of the Inland Revenue Ordinance (Cap. 112) (IRO) so as to enhance the competitiveness of Hong Kong and to attract international investors. In this connection, Miss TAM expressed concern about whether and how FSTB had followed up the motion and reviewed IRO with a view to clarifying certain grey areas in the existing taxation regime.

28. SFST appreciated Miss TAM Heung-man's concern about the importance of a clear taxation regime in attracting international investors. He however pointed out that amendments to IRO and/or revision to the taxation system had to be taken forward in a cautious manner with full consideration of the possible far-reaching consequences on the economy of Hong Kong. The Permanent Secretary for Financial Services and the Treasury (Treasury) (PS(Tsy)) advised that the current provisions of IRO had enabled Hong Kong to maintain a relatively simple taxation system with which investors and the business community had become familiar. While the Administration would welcome suggestions and views on specific provisions of IRO, changes would not be introduced lightly unless it was certain that they would bring about overall benefits.

Investment management

29. Noting that investment guidelines were in place for bureaux/departments and subvented organizations to follow in the investment of funds under their management, Mr SIN Chung-kai enquired whether the Administration had kept these guidelines under periodic reviews to best balance the needs for risk management and investment return.

30. In response, PS(Tsy) advised that many of the funds managed by bureaux/departments/subvented organizations were governed by legislation and

their management might therefore be subject to certain statutory requirements. In the case of some funds, dedicated committees had been established to make investment decisions or advise on the investment strategies of the funds. Some of these committees were also required to submit proposals to the relevant bureaux/departments/subvented organizations on the investment portfolio to be adopted in order to ensure that there was a proper balance between investment return and risks. He assured members that the investment guidelines provided by the Administration would be subject to review from time to time having regard to changing circumstances including the introduction of new investment products.

31. Mr SIN Chung-kai stressed the importance of frequent updating of the investment guidelines and urged the Administration to engage the relevant committees and solicit their views on whether and how the guidelines should be revised. SFST noted Mr SIN's concern.

Income disparity in Hong Kong

32. Referring to SFST's reply to a question on the Gini Coefficient (GC) at the LegCo meeting on 4 July 2007, Ms Emily LAU noted with concern that SFST's analysis of the computation of GC seemed to suggest that Hong Kong was not facing a problem of income disparity. Pointing out that income disparity in Hong Kong had aggravated over the past decade, as manifested by the increasing GC value and the significant increase in the number of low-income households, Ms LAU was concerned about the Administration's plans and measures to tackle the problem.

33. In response, SFST clarified that his reply to the question at the LegCo meeting on 4 July 2007 provided an explanation on the definition and interpretation of GC. There was no intention to suggest that income disparity did not exist in Hong Kong, or was not a problem to be addressed. He assured members that the Administration attached great importance to combating poverty and income disparity and had devised various initiatives in this respect.

Requirement on note issuing banks

34. The Chairman noted that HKMA had recently announced an additional policy requirement relating to the continuing authorization of banks as note issuing banks (NIBs), which imposed restriction against the holding of 20% or more of the shares of NIBs by a foreign government or a foreign government controlled entity. He enquired about the rationale behind this additional requirement. In reply, SFST advised that as a NIB had a systemically significant status in Hong Kong in performing the public function of note issuance, the additional policy requirement of HKMA would be in Hong Kong's public interest to prevent any close association of a NIB with a foreign sovereign entity.

II. Any other business

35. There being no other business, the meeting ended at 10:27 am.

Council Business Division 1
Legislative Council Secretariat
13 September 2007