

Observations of the Public Accounts Committee on the Report of the Director of Audit on the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 2009

The Committee noted the Report of the Director of Audit on the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 2009 ("the Government Accounts").

2. The Committee sought information on "Losses of cash and valuables due to theft, fraud or negligence" under the General Revenue Account, as reported in page 123 of the Government Accounts. The Committee's enquiries and the information provided by the **Secretary for Financial Services and the Treasury** vide the Secretary's letter of 25 January 2010, in *Appendix 8*, are set out in the ensuing paragraphs.

A. Cases brought forward from previous years

Government Logistics Department – Irrecoverable debt (\$17,025,082.44)

3. Regarding the irrecoverable debt amounting to \$17,025,082.44, the Committee enquired whether the Administration had carried out any review on the internal controls and about the improvement measures that would be/had been put in place.

4. The **Secretary for Financial Services and the Treasury** replied that:

- the irrecoverable debt amount of \$17,025,082.44 was the total of a judgement sum at \$10,742,838.17, cost of action at \$244,315.55, and interest calculated up to 5 September 2007 (the date on which a Bankruptcy Order was granted against the Managing Director of the Hong Kong Auctioneers and Estate Agency Ltd. ("HKAEAL")) at \$6,042,928.72 less a contract deposit of \$5,000;
- the debt in question was owed to the Government by the Managing Director of the HKAEAL hired by the former Government Supplies Department ("GSD") (now the Government Logistics Department) for the disposal of unserviceable or obsolete government stores and confiscated goods;
- to forestall recurrence of the situation of the Government not being able to recover auction proceeds from hired auctioneers, the GSD had taken various improvement measures between 1998 and 2002 to guard against late payments by hired auctioneers. No late payments by auctioneers had been found subsequently; and
- to further strengthen controls, the GSD changed the auction arrangement in November 2002. The auctions had since been held in-house with an auctioneer hired to provide the professional service of conducting the auction only. The auctioneer was no longer responsible for collecting any auction

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proceeds from the successful bidders who were required to pay the proceeds directly to the Government by 4:30 pm on the auction day. A release note would be issued to the successful bidders only upon confirmation of receipt of the proceeds or upon clearance of the cheque. The arrangements had worked well so far.

5. In response to the Committee's enquiry, the **Secretary for Financial Services and the Treasury** also provided in the letter of 25 January 2010 details of the recovery actions that had been taken so far.

Department of Health – Embezzlement by staff (\$13,710,000)

6. Regarding embezzlement by staff of the Department of Health ("DH"), the Committee enquired whether there were preventive controls and if there were, why the controls were not effective.

7. The **Secretary for Financial Services and the Treasury** replied that there were preventive controls clearly set out in various government-wide regulations and instructions for bureaux and departments to comply with. The occurrence of the embezzlement case was a calculated act by the perpetrator who made use of falsified documents, coupled with failure in upholding the above regulations and instructions by his supervisors.

8. The Committee also asked whether the Administration had reviewed the internal controls. The **Secretary for Financial Services and the Treasury** stated that:

- since discovery of the embezzlement case, the DH had taken immediate actions to strengthen the internal controls of the department's payment and accounting procedures and had implemented recommendations of the ICAC following a review of the case;
- the DH had reminded all staff in its Finance Office of the need to strictly comply with government regulations and instructions in processing payments. In particular, all officers involved in payment processing had been reminded to ensure that claims for payments were adequately supported, properly certified and correctly accounted. To this end, a comprehensive checklist on payment checking had been issued to provide practical assistance to staff in dealing with matters relating to authorisation of payment vouchers. A circular had also been issued to provide a summary of major points to be observed by budget holders and subject officers in arranging payments; and

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- as a further safeguard, the DH had introduced sample post-payment checking by budget holders on selected payments charged to their votes. The DH's Internal Audit Section had also revised its work plan to conduct more health checks on payment vouchers and procedures to ensure that the checks and balances are functioning as anticipated.

9. As regards the recovery actions that had been taken, the **Secretary for Financial Services and the Treasury** advised that according to information from the Police, there was no evidence to show that the perpetrator had any valuable assets. In order to exhaust all means in taking recovery actions against the perpetrator in respect of the embezzlement sum, the Department of Justice ("D of J") had been setting about proceeding with the civil procedures of instigating a civil action with the aim of successfully obtaining a judgment from the court against the perpetrator and, if so successfully obtained, would instigate bankruptcy.

Home Affairs Bureau – Embezzlement by staff (\$409,100.80)

10. Regarding embezzlement by staff of the Home Affairs Bureau ("HAB"), the Committee enquired whether the Administration had carried out any review on the internal controls and about the improvement measures that would be/had been put in place.

11. The **Secretary for Financial Services and the Treasury** replied that the HAB had reviewed the relevant accounting procedures and control mechanism. A circular had been issued and measures such as imposing requirements for maintaining detailed transaction records and conducting more surprise checks had been put in place to tighten up controls to prevent recurrence of similar incidents.

12. As for the recovery actions, the **Secretary for Financial Services and the Treasury** stated that:

- the HAB was taking legal action to recover the loss. The Final and Interlocutory Judgment had been obtained and the next step was for the D of J to apply to the Court for an assessment of damages. In order to serve the relevant notice and court documents relating to the assessment of damages application on the Defendant, the Administration was in the process of ascertaining the latest whereabouts and correspondence address of the Defendant; and

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- once the damages were assessed and a final judgment entered, enforcement action for recovery of the loss could then commence. The D of J would consider every possible means of enforcement with a view to recovering the embezzlement sum and relevant loss from the perpetrator, including initiating garnishee proceedings, charging order application, writ of *fifa*, and bankruptcy petition.

B. Cases in 2008-2009

Leisure and Cultural Services Department – two cases of overpaid housing allowances (\$1,735,749.09)

13. Referring to the two cases of overpaid housing allowances, the Committee asked whether the recipients of the housing allowances were responsible for reporting the overpayments.

14. The **Secretary for Financial Services and the Treasury** replied that the recipients of the housing allowances, who were contract staff of the two Municipal Councils (Ex-Council Contract ("ECC") staff) before their dissolution, were not aware of the housing allowances being overpaid until they were informed by the Leisure and Cultural Services Department ("LCSD").

15. The Committee further asked:

- whether there were loopholes in the internal procedures which caused the overpayments and whether there were preventive controls;
- whether the Administration had reviewed the internal controls and what improvement measures had been taken; and
- about the progress of recovering the outstanding amount of \$1,235,749.09, i.e. \$1,735,749.09 less the \$500,000 recovered.

16. The **Secretary for Financial Services and the Treasury** replied that:

- at the material time, the LCSD had put in place an established mechanism for processing applications for housing benefits of ECC staff. The cases were discovered by the LCSD during the course of an internal review of the housing benefits for staff. The LCSD had conducted a detailed review of the mechanism upon the discovery of the cases;

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- to ensure that all relevant applications would be processed in full compliance with the terms and conditions of the contracts and the established mechanism, the LCSD had implemented measures such as centralising the vetting of the applications and escalating the level of approving authority for housing benefits of ECC staff; and
- the Administration was considering the extent of liability of each of the officers involved and whether surcharges should be imposed as a result. When the above was completed, the Administration would take appropriate follow-up action to deal with the outstanding amount according to the laid-down procedures, including seeking the approval of the Finance Committee for writing off any irrecoverable amount as necessary.

Water Supplies Department – Embezzlement by Staff (\$4,392)

17. Regarding embezzlement by staff of the Water Supplies Department ("WSD"), the Committee enquired whether the Administration had reviewed the internal controls and whether improvement measures would be/had been put in place. The Committee also asked whether the embezzlement sum had been recovered.

18. The **Secretary for Financial Services and the Treasury** replied that:

- the WSD had reviewed the procedures on sub-impresst claims immediately following the incident and issued instructions to enhance the control, including not allowing a sub-impresst holder to incur cash expenditure and claim reimbursement from the sub-impresst held by him/her and requiring the certified payment amount be stated in words in the claim form. In addition, the Internal Audit Section of the WSD conducted independent checks regularly to ensure compliance of the procedures; and
- the amount of \$4,392 had been fully recovered in September 2009.

C. Note 1: Cases less than \$1,000

19. Referring to Note 1 which stated that cases less than \$1,000 each were excluded. The Committee asked about the numbers of cases involving less than \$1,000 each in each of the past five years.

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20. The **Secretary for Financial Services and the Treasury** advised that the accounts relating to cases less than \$1,000 each in the past five years were all settled within the financial year in question. The statistics were as follows:

<u>Financial Year</u>	<u>Number of cases</u>
2004-2005	7
2005-2006	6
2006-2007	4
2007-2008	5
2008-2009	2