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**Notes on the Briefing by the Financial Secretary
on Friday, 5 March 1999, at 10:45 am
in the Legislative Council Chamber**

Members present:

Hon Ronald ARCULLI, JP, Chairman of the Finance Committee (Convenor)
Hon CHAN Kam-lam, Deputy Chairman of the Finance Committee
Hon Kenneth TING Woo-shou, JP
Hon David CHU Yu-lin
Hon Cyd HO Sau-lan
Hon Edward HO Sing-tin, SBS, JP
Hon Albert HO Chun-yan
Ir Dr Hon Raymond HO Chung-tai, JP
Hon LEE Wing-tat
Hon Martin LEE Chu-ming, SC, JP
Hon Eric LI Ka-cheung, JP
Dr Hon LUI Ming-wah, JP
Hon NG Leung-sing
Hon Margaret NG
Hon Mrs Selina CHOW LIANG Shuk-ye, JP
Hon CHEUNG Man-kwong
Hon HUI Cheung-ching
Hon Christine LOH
Hon CHAN Yuen-han
Hon Bernard CHAN
Hon CHAN Wing-chan
Hon Gary CHENG Kai-nam, JP
Hon SIN Chung-kai
Hon WONG Yung-kan
Hon LAU Kong-wah
Hon Mrs Miriam LAU Kin-ye, JP
Hon Emily LAU Wai-hing, JP
Hon Andrew CHENG Kar-foo
Hon TAM Yiu-chung, GBS, JP
Dr Hon TANG Siu-tong, JP

Public officers attending:

Mr Donald TSANG Yam-kuen, JP	Financial Secretary
Miss Denise YUE, JP	Secretary for the Treasury
Mrs Carrie LAM, JP	Deputy Secretary for the Treasury
Mr Rafael HUI	Secretary for Financial Services
Mr Philip YUNG	Administrative Assistant to Financial Secretary

Staff in attendance:

Ms Pauline NG	Assistant Secretary General 1
Ms Anita SIT	Senior Assistant Secretary (1)8

The Convenor welcomed Mr Donald TSANG, the Financial Secretary (FS), and his colleagues to the briefing. He advised that the purpose of the briefing was to provide an opportunity for Members to ask questions on the 1999-2000 Budget announced by FS on 3 March 1999. Specific questions on the Draft Estimates of Expenditure would be dealt with at the Special Meetings of the Finance Committee scheduled for 16 to 19 March 1999.

Financial Secretary's introductory remark

2. FS said that despite the slowing down of the economy, the Government had budgeted an increase of 4.3% in total public expenditure, with the highest growth rates in the policy areas of social welfare, education and health. This reflected the commitment of the Government to helping the needy in the community. On the revenue side, the Government had tried to constrain its revenue raising measures in order to avoid causing undue negative impact on the economy which was expected to start to recover in 1999-2000. FS then stressed that his budget strategy was to maintain a fiscal balance over the medium term while seeking an early economic recovery in the short term.

The Cyberport Development

3. Mr Ronald ARCULLI, Convenor of this briefing, declared interest that he was a partner of a law firm which was acting as consultant to the consortium that might enter into a contract with the Government on the Cyberport project.

4. A number of Members pointed out that the Cyberport appeared to serve more or less the same purpose as other projects such as the Science Park and

Industrial Estates. Mr SIN Chung-kai cast doubt on whether there would be a demand for both the facilities of the Cyberport and the Science Park, and enquired how the Administration would balance the two projects in terms of resource allocation and marketing efforts. In reply, FS said that the Cyberport was an infrastructure project aimed at creating a strategic cluster of top information technology and services companies and a critical mass of professional talent in Hong Kong. The target clients of the Cyberport were corporations specializing in information technology and services, particularly those whose operation required broad band networks and multi-media facilities. On the other hand, the Science Park would accommodate a wider spectrum of companies engaged in various technological research and development including biochemical technology. He was confident that the demand for both types of facilities was strong and the two projects would be complementary to each other.

5. Mr LUI Ming-wah queried whether it would be more cost-effective to integrate the Cyberport into an expanded Science Park, instead of developing the Cyberport as a separate project. In response, FS said that the target clients of the Cyberport would require specific infrastructure facilities such as broad band networks and multi-media facilities and these facilities would not be available for common use at the Science Park. Moreover, proximity to the teleport at Chung Hom Kok was an important consideration for locating the Cyberport at Telegraph Bay. FS pointed out that given the good transportation network in Hong Kong and with advanced communication facilities, the exchange of expertise and information between the Science Park and the Cyberport would not be significantly affected by the physical distance between them. He said that in the United States, for example, there were several centres of high-tech industries in different parts of the country.

6. On Dr Raymond HO's question why the Government would jointly develop the Cyberport with a private company instead of implementing it as a purely private development project, FS said that generally speaking, the Government would not actively take part in development projects. The Government should restrict its role to the provision of the essential infrastructure to facilitate development. Only when there was a clear consensus in the community on the need for a development project and it was clear that the resources available from interested private companies were inadequate to take forward such a project successfully would the Government consider greater participation in the project. The Government's overriding principle was always maximum support and minimum intervention.

7. On Dr Raymond HO's concern about the co-ordination among the management bodies of the existing industrial estates, the Science Park and the Cyberport in marketing the respective developments, FS said that these developments provided different facilities and targeted different types of

companies. It would be up to prospective tenants to decide which development was suitable for setting up their operations in Hong Kong, having regard to the differences in location, tenancy terms, infrastructure facilities etc.

8. On whether the Administration would consider offering the development right of the Science Park to the private sector as in the case of the Cyberport, FS pointed out that funds required for the construction of the Science Park had already been approved by the Finance Committee. Nevertheless, the Administration would be willing to consider alternative modes of development which would bring about greater benefits to the community.

Disney theme park

9. In response to Mr CHAN Kam-lam's question on the progress of negotiation for construction of a Disney theme park in Hong Kong, FS said that both the Government and the company were interested in the project and a series of meetings had been held. The two sides had exchanged a letter of understanding recently and agreed on the target schedule of reaching a binding agreement by the end of June this year, after which a funding proposal would be put to the Finance Committee. Both sides would be engaged in intensive talks in the coming few months. The Administration would report to Members the outcome of the negotiation at an appropriate time.

Forecast GDP growth

10. Miss Emily LAU questioned the Administration's forecast of a 0.5% growth in Gross Domestic Product (GDP) in real terms for 1999-2000. She considered this forecast too optimistic and enquired about the basis for the forecast. In reply, FS advised that the downward movement of various economic indicators had begun to slow down since the last quarter of 1998, and there were signs that the economy would reach the bottom and begin to pick up in 1999. Based on recent trends and relevant projections, the Government Economist forecast a 0.5% growth in GDP for 1999-2000. The main factors contributing to a positive GDP growth included the projected growth in private consumption expenditure, Government consumption expenditure, and exports and imports of services, details of which had been set out in the Economic Report and other reference material attached to the Budget Speech. The Administration would update its economic forecasts in its quarterly economic reports. FS remarked that the Government's GDP forecast was consistent with those of renowned financial analysts who gave a range from -1% to 1%. He did not agree that the Government's GDP forecast was too optimistic and pointed out that an annual GDP growth of 3.5% from 1998-99 to 2002-03, as assumed for the medium range forecast, would bring the economy

only back to the same GDP level as that of 1997-98 in real terms. The International Monetary Fund indeed projected an annual 4% GDP growth for Hong Kong for the same period.

11. Pointing out that the property sector and the financial sector had been the main driving forces of Hong Kong's economy over the past 10 to 20 years, Mr NG Leung-sing enquired about which sector(s) or industries would drive the momentum for the economy in the next five years. In response, FS said that the Government played only a facilitating, rather than a leading, role in economic development. It had no intention to maneuver and decide which sector(s) should lead the economy. Based on recent trends, he believed exports and service industries would continue to contribute the largest shares of GDP. He added that hopefully, high-tech industries would increase their share in economic output and provide new strengths for the economy.

Tax rebate

12. Miss Margaret NG enquired about the rationale for the tax rebate proposal which apparently would not benefit those outside the tax net but would substantially reduce the Government's revenue. FS replied that about 40% of the working population had to pay salaries tax. He pointed out that the needy in the community could be taken care of directly through the Comprehensive Social Security Assistance Scheme and the public housing programme, and indirectly through infrastructure projects, the implementation of which provided job opportunities. The proposed tax rebate was aimed at providing a relief for the middle class and the small and medium enterprises hard hit by the economic downturn. FS agreed to provide Miss NG with information on the total amount of tax rebate in respect of each category of taxpayers listed in page (1) of the supplement to the Budget Speech, and the highest amount of tax rebate for individual taxpayers under each category. He also took note of Miss Christine LOH's request for a copy of the information.

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Priority accorded to the policy area of Environment in the Budget

13. Miss Christine LOH said that while she supported the Budget at large, she was disappointed that "environment" was not given much attention in the Budget Speech. She remarked that the business sector and visitors to Hong Kong were very disturbed by the rapidly deteriorating environment and she queried the priority accorded to environmental protection in the allocation of public funds.

14. In response, FS stressed that the Budget was not meant to cover all policy areas. He reiterated the Administration's determination to continue to

accord high priority to environmental protection. He pointed out that about \$3.4 billion, representing a 3.7% increase over 1998-99, had been allocated to cover the recurrent expenditure on environment in 1999-2000. As an incentive for taxis and car owners to switch to liquefied petroleum gas (LPG), the Administration was prepared to exempt auto-LPG from the payment of duty. Miss LOH commented that despite the assurance of not imposing duty on LPG, financial and other forms of support from the Government to improve the environment was grossly inadequate.

Unemployment

15. Mr CHENG Ka-foo said that although some measures proposed in the Budget would help create new jobs in the medium and long term, he was disappointed that there was no specific measure to alleviate the unemployment problem in the short term. Referring to the difficulties encountered by university graduates in finding jobs, Mr CHENG suggested that the Administration should consider improving the ratios of teachers to students and social workers to students through creating more teaching and social work posts for university graduates.

16. FS said that unemployment and economic performance were closely related. The Government should not seek to create jobs simply for the sake of reducing unemployment. In order not to aggravate the current economic recession, he had proposed not to cut public expenditure in the coming year. For example, the proposed provisions for education and welfare in the recurrent expenditure for 1999-2000 were already 5.1% and 13.6% higher than the respective spending on these two areas in 1998-1999 in real terms. The Administration estimated that the committed infrastructure projects could bring about 120 000 new jobs, and more importantly, would help stimulate private investment. To control public expenditure without causing undue impact on the economy, the Administration would rigorously restrain the creation of new permanent civil service posts, whilst bureaux/departments would be allowed to offer appointments on contract terms to meet short-term needs.

17. Miss CHAN Yuen-han considered that although the budget initiatives might help strengthen Hong Kong's economy in the long run, they could not provide short term relief to the grassroot sector. She was particularly concerned that the unemployment problem would be aggravated by the inflow of immigrants from the Mainland following the recent ruling by the Court of Final Appeal on the right of abode. In this connection, she enquired whether the Administration had reviewed the effectiveness of the existing Task Force on Employment in easing unemployment.

18. FS reiterated that the Government should not and could not play a leading role in job creation as the unemployment problem could only be solved

when there was improvement in the overall economy. The Task Force on Employment had formulated a wide range of measures to ease unemployment and help job creation, and would welcome suggestions from Members. Miss CHAN Yuen-han commented that the Task Force had not been able to address the problem and she considered it necessary for all relevant government departments to re-examine the unemployment problem afresh having regard to suggestions made by labour unions and related associations.

19. Miss Cyd HO expressed concern about the unemployment problem of women workers and pointed out that jobs created by the implementation of public infrastructure projects were mostly open to male workers. She suggested that the Government should formulate short-term measures to facilitate the recovery of the manufacturing sector, which would help create jobs for unemployed female workers.

20. FS said in response that one objective of the proposed tax rebate was to provide relief to small and medium enterprises, which in turn would benefit their employees. While he fully appreciated Members' grave concern about unemployment, he stressed that under the existing policy of maintaining a small government and low tax rates, the Government could not be expected to put in a disproportionate amount of public resources to create jobs in the public sector.

21. On Miss Cyd HO's reference to the suggestion by Members of the Frontier to abolish the textile quota system which some people believed had led to speculation and higher costs for textile manufacturers, FS responded that the textile quota system was beyond Hong Kong's control as textile quotas were imposed by importing countries. For years, the Government had been negotiating for the abolition of textile quotas with the importing countries. He hoped that all textile quotas would be abolished through agreements of the World Trade Organization within the next eight to nine years. In this regard, Miss HO opined that the Administration should curb speculation on textile quotas by administrative measures in order to reduce the cost to local textile manufacturers.

22. Referring to the unemployment problem faced by young people, Mr TAM Yiu-chung said that the number of apprentice training vacancies offered by employers had decreased in 1998/99. He urged the Administration to consider providing some form of financial incentives to encourage employers to offer apprentice training to young people. FS agreed that vocational training was a priority area. He added that the funding provided to the Vocational Training Council (VTC) and the Employee Retraining Board had increased considerably over the past two years. For example, over \$2 billion would be provided for VTC in 1999-2000. FS agreed to convey the view of Mr TAM to VTC for further consideration.

23. Mrs Selina CHOW said that Members of the Liberal Party (LP) supported the 1999-2000 Budget as they considered that the proposed fiscal measures could help stimulate the economy. She reiterated the view of Members of LP all along that the Government should focus its effort on encouraging and facilitating economic activities which would in turn create job opportunities and ease the unemployment problem.

Earnings from the investment of the fiscal reserves with the Exchange Fund

24. Mr Eric LI noted from the Budget Speech that the forecast fiscal deficit in 1998-99 was \$32.3 billion, which had taken into account the forecast yield of \$36 billion from the investment of the fiscal reserves with the Exchange Fund in 1998-99. According to paragraph 122 of the Budget Speech, this enhanced yield (\$9.3 billion higher than originally estimated) was a by-product of the Government's incursion into the stock market in August 1998 and the subsequent rise in the Hang Seng Index. Mr LI sought clarification on the accounting approach for the said yield of the fiscal reserves.

25. The Secretary for the Treasury (S for Tsy) explained that the estimated earnings from the investment of the fiscal reserves were accounted for under Subhead 040 "Investment earnings and interests" of Head 7 of the General Revenue Account. The said earnings of \$36 billion for the year 1998-99 were projected on the basis of the rate of investment return of the Exchange Fund as at the end of December 1998. S for Tsy agreed to provide a breakdown of the estimated earnings of \$36 billion after the briefing.

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26. Mr Eric LI further enquired about the reason for regarding the "earnings" resulting from the rise in market value of the securities held by the Government as part of the revenue in 1998-99, and queried whether the Administration had adopted an "accrual basis" accounting approach for the revenue part of the Budget while adopting the "cash basis" approach for the expenditure part. FS clarified that from the Treasury's perspective, these earnings would be realized by the end of the financial year when they were transferred to the General Revenue Account from the Exchange Fund. The Exchange Fund acted like a "deposit taking bank" for the Government's fiscal reserves, while the earnings on the fiscal reserves were similar to dividend payments by the Exchange Fund. Any sale of assets by the Exchange Fund to realize profits might have an impact on the return on the investment of the Exchange Fund as a whole, not directly on the fiscal reserves. He also confirmed that the cash basis accounting approach was used for both the revenue and the expenditure parts of the Budget.

Fees and charges of Government services

27. As to why the Administration had decided to extend the freeze on government fees and charges by only six months instead of one year, FS explained that the decision was made having regard to the forecast that the economy would reach the bottom and begin to pick up by mid 1999. A review of the fees and charges would then be necessary as the Government was facing fiscal deficits and the user pays principle should be upheld. He said that the Administration would seek Members' views on the level of increase and the priority for adjusting different fees and charges in the near future.

28. Mrs Selina CHOW commented that the Administration should implement rigorous changes to streamline procedures and trim costs whenever there was such an opportunity, as these changes might result in considerable cost reduction and ultimately benefit the clients of government services comprising mainly small and medium enterprises. In this connection, she expressed support for the proposal to issue a three-year business registration certificate as an option in addition to the present annual certificate. She however considered that the cost reduction for a three-year certificate should warrant a lower registration fee than the \$5,200 announced in the Budget, given that the registration fee for an annual certificate was \$2,000.

29. In response, FS re-affirmed the principle that the Government would not regulate business activities unless necessary. He clarified that the business registration fee was one of the few items of government fees consisting of a tax element in addition to a charge set to recover cost. This tax element was the main reason for the less than proportionate reduction in the registration fee for a three-year business certificate.

Promoting investment

30. Mr Kenneth TING expressed support for the Budget on behalf of the Federation of Hong Kong Industries. As one of the driving forces of economic recovery was inflow of overseas investment, he asked whether the Administration would consider providing tax concessions for overseas investment. FS replied that the Government would not provide such tax concessions as this would inevitably complicate the tax system and expand the discretionary powers of tax officials. The trend in many developed countries was to abolish progressively various kinds of tax concessions for overseas investment. Instead, the Government would strive to provide a favourable business environment in terms of infrastructure facilities, and a simple tax system which would be conducive to foreign investment. FS added that the Government was well aware of the need to sharpen Hong Kong's competitive edges.

Revenue raising measures

31. Mr LEE Wing-tat concurred that in view of the expected drop in revenue from certain sources such as the stamp duty on property transactions and Rates, it was necessary to find new revenue sources to address budget deficits in the medium term. He however noted that FS had mentioned the possible introduction of land and sea departure tax in his Budget Speech, but had not mentioned other new tax sources such as sales tax. He urged the Administration to adopt an open attitude and actively solicit views from the public on various new tax options.

32. In response, FS stressed that in view of the present economic climate and the projected deficits in the next two years, it was necessary to identify new tax sources. He nevertheless affirmed that a low tax policy would be upheld and any new tax measures must be simple and easy to enforce and should not have an undue impact on taxpayers. He assured members that the Administration was open to views of the public on the subject. In this connection, FS said that the Administration had no intention to introduce sales tax in 1999-2000.

33. Mrs Selina CHOW said that although the Government would not introduce sales tax in the coming financial year, Members of LP were worried that sales tax would be introduced in future. She reiterated the view of Members of LP that sales tax should not be introduced in Hong Kong.

34. On the proposal for introducing land and sea departure taxes, FS said that this proposal could be further explored as the tax net would be wide and the amount required to be paid by each taxpayer would be small. LAU Kong-wah however commented that in considering the introduction of land departure tax, the Administration had apparently overlooked the additional charge of about \$20 for a single trip payable by passengers taking the Kowloon Canton Railway to Lo Wu. In response, FS pointed out that the land departure tax had little to do with the train fares charged by the Kowloon Canton Railway Corporation (KCRC) as the latter was determined purely on commercial considerations of the KCRC.

35. In response to Mr LAU Kong-wah's and Mr CHEUNG Man-kwong's comments that car owners were targeted at by the revenue raising measures, FS advised that decisions on revenue raising measures had had regard to the number of people affected and to the question of affordability. To avoid increasing the operating costs of the transportation industry and related trades, the proposed increase in the Cross Harbour Tunnel tolls would apply to private cars and motorcycles only.

36. On the decision not to raise tobacco duty, FS remarked that having considered the relevant statistics, he was of the view that increasing tobacco duty would only provide further impetus to smuggling and illegal sale of cigarettes. This would be counter-productive in revenue terms and would

contribute little to furthering the anti-smoking policy. A new approach to combat smuggling and discourage smoking was required and he would take up the matter with the relevant bureaux/departments shortly. He also assured Members of the capability of law enforcement departments in combating smuggling and illegal sale. As regards the duty on alcohol, FS clarified that a mechanism to adjust the duty annually in line with inflation, which did not necessitate legislative amendments, was already in place.

Fixed penalties for traffic-related offences

37. Referring to the proposal to increase the fixed penalties for traffic-related offences by 26.5%, Mrs Miriam LAU expressed doubt on whether the measure would eventually bring about an increase in revenue as anticipated by FS since the deterrent effect of the increased penalties would prevail. Mrs LAU was also of the view that the penalties for traffic-related offences should be imposed primarily for deterrence, rather than for raising public revenue. She further pointed out that the decrease in the number of traffic-related offence orders issued over the past few years might be an indication that the existing level of fixed penalties was already high enough to achieve the intended deterrent effect.

38. In response, FS confirmed that the primary objective of the penalties was to deter traffic-related offences. The proposed adjustment by 26.5% was to keep the level of penalties in line with cumulative inflation since the last adjustment in 1994 in order to maintain the deterrent effect. In this connection, he also pointed out that the Government was less concerned about the outturn revenue than road users' compliance with traffic safety regulations.

Outsourcing of public services

39. Mr HO Chun-yan suggested that to help boost the economy and to improve the living environment, the Administration should consider contracting out some Government services which were not currently adequate due to the lack of in-house resources. For example, the Administration might engage contractors to demolish unauthorized structures which were posing a hazard to the public. Taking note of Mr HO's suggestion, FS clarified that the Buildings Department had been engaging private contractors to demolish unauthorized structures but he stressed that the Government would not contract out its statutory functions such as building safety inspections.

Urban renewal

40. Mr HO Chun-yan pointed out that given the present property market climate, it was opportune for the Government to expedite the urban renewal programme by playing a more active role in urban renewal. The Government should take this opportunity to enhance its land bank to prepare for a probable surge of population and an increase in housing needs in future. FS noted his view.

41. The briefing ended at 12:15 pm.

Legislative Council Secretariat
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