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by the Administration and
cleared by the Chairman)

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**Notes on the Special Briefing for Finance Committee Members
on Monday, 5 June 2000, at 11:45 am
in the Chamber of the Legislative Council Building**

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 James TIEN Pei-chun, JP
Hon David CHU Yu-lin
Hon Albert HO Chun-yan
Hon LEE Wing-tat
Hon LEE Cheuk-yan
Hon LEE Kai-ming, SBS, JP
Hon Fred LI Wah-ming, JP
Dr Hon LUI Ming-wah, JP
Hon NG Leung-sing
Prof Hon NG Ching-fai
Hon CHEUNG Man-kwong
Hon Christine LOH
Hon CHAN Kwok-keung
Hon CHAN Yuen-han
Hon Bernard CHAN
Hon CHAN Wing-chan
Hon Mrs Sophie LEUNG LAU Yau-fun, JP
Hon LEUNG Yiu-chung
Hon SIN Chung-kai
Hon Jasper TSANG Yok-sing, JP
Dr Hon YEUNG Sum
Hon Ambrose LAU Hon-chuen, JP
Hon Emily LAU Wai-hing, JP
Hon FUNG Chi-kin

Public officers attending:

Mr Donald TSANG, JP	Financial Secretary
Mrs Carrie LAM, JP	Acting Secretary for the Treasury
Mr K Y TANG	Government Economist
Mr Philip YUNG	Administrative Assistant to Financial Secretary

Clerk in attendance:

Ms Pauline NG	Assistant Secretary General 1
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Staff in attendance:

Miss Polly YEUNG	Chief Assistant Secretary (1)3
Ms Anita SIT	Senior Assistant Secretary (1)8

The Convenor welcomed the Financial Secretary (FS), Mr Donald TSANG, and his colleagues to the briefing. The Convenor advised members that it had been a standing practice for FS to conduct two rounds of consultations with Members each year on the Budget. This briefing was the first part of his consultation on the 2001-02 Budget, focusing on expenditure proposals. FS would consult the newly elected Members of the Legislative Council (LegCo) again in October/November 2000 on the revenue side of the Budget.

2. Miss Emily LAU expressed dissatisfaction that Members were not given sufficient time to discuss the expenditure proposals of the 2001-02 Budget with FS. She questioned why this briefing and the meeting of the Financial Affairs (FA) Panel had been scheduled to be held consecutively within a single two-hour time slot. She recalled that FS had used to consult Members on the annual Budget in groups and each group was given about 45 minutes to one hour to express their views to FS. As this briefing would only last for about 40 minutes, she considered the present arrangement highly unsatisfactory. She also expressed dissatisfaction that the Government Economist had held a press conference on Hong Kong's economic performance in the first quarter of year 2000 some time ago, but LegCo Members were not briefed on this important matter until at the FA Panel meeting preceding this briefing.

3. The Convenor said that he had agreed to hold this briefing immediately after a short meeting of the FA Panel having regard to the availability of FS and Members. He was given to understand that there was no suitable alternative timing for this briefing.

4. FS said that he attached great importance to consulting LegCo Members in the Budget formulation process. Since the current term of LegCo would end by 30 June 2000, he had proposed to make use of this opportunity, amid competing priorities for his diary, to consult Members on the expenditure part of the 2001-02 Budget so that Members' views could be taken into account as early as possible when drawing up the Budget. He would consult LegCo Members again later in the year on the revenue side of the next Budget. He would also welcome any further views in writing from Members.

Guidelines for fiscal reserves

5. Miss Emily LAU noted from the Information Note "The 2001-02 Budget - Background information on the Financial Secretary's consultations with LegCo Members on expenditure proposals" (issued to Members vide FC125/99-00 dated 25 May 2000) that the guidelines set out in the 1998 Budget Speech were referred to when reporting on the fiscal reserves of \$444 billion at 31 March 2000. She queried the basis for using these guidelines in the absence of a community-wide consultation on how the fiscal reserves should be used. She opined that for the coming years, the Government should not refrain from spending on capital projects or initiatives for the purpose of improving the livelihood and eco-environment of the community, such as air quality improvement measures, noise mitigation measures, school improvement projects and urban renewal projects etc.

6. FS said that he had explained clearly how these guidelines were worked out in his Budget Speech in 1998. Feedback from the community on the guidelines had been favourable. He had always been prepared to listen to the views of LegCo Members and the general public and the formula for deciding on the fiscal reserves was also subject to discussion. The Government should of course set priorities for its spending. Education, environmental protection and urban renewal were the priority areas the Chief Executive highlighted in his Policy Address in 1999. Resources had been earmarked for initiatives related to these areas.

7. FS further explained that the public sector had accounted for over 20% of the Gross Domestic Product (GDP) since 1998-99 and this trend would likely continue for the coming few years. For a service-oriented economy like Hong Kong, this level of public expenditure was slightly on the high side and the Government had to ensure that the public sector would not take up a disproportionate part of the community's resources. As regards the existing

arrangements relating to the investment income on fiscal reserves, FS invited Members to refer to the information note the Administration had provided in response to Members' queries raised at the briefing on 10 March 2000.

(*Note:* The information note was issued to members vide LC Paper No. FC96/99-00 dated 31 March 2000.)

8. The Convenor invited Members to follow up the Government's targets on the priority areas of the 1999 Policy Address at the appropriate Panels, including how the Administration would prioritize these targets, the timetable for implementation and the proposed expenditure for achieving these targets.

9. On the application of the guidelines on the fiscal reserves as set out in the 1998-99 Budget Speech, Mr SIN Chung-kai asked whether FS would cut expenditure or raise revenue just for the sake of maintaining the fiscal reserves within the guidelines. FS said that in line with the objectives of the guidelines, the Administration would always seek to maintain public investment and expenditure programmes even during economic downturns to facilitate economic development.

Fiscal deficit

10. Referring to the Government's projection of consolidated operating deficits from 1998-99 to 2002-03, Mr YEUNG Sum enquired how far the deficits were of a structural nature. He considered that budget deficits should not be a cause for alarm when drawing up expenditure proposals.

11. FS said that he could not take a definitive view at this stage as the extent and nature of the operating deficits was being studied by the Task Force headed by the Secretary for the Treasury. The Task Force would take about one year to complete its work, but would first submit a progress report to him in November 2000.

12. FS recalled that he had explained in detail the Government's fiscal principles in this year's Budget Speech. While he agreed that a deficit budget was necessary and well justified under certain circumstances, structural deficits were an entirely different matter which the Administration had to address seriously. In an open economy like Hong Kong's, structural deficits would seriously undermine Hong Kong's competitiveness. Nor did the Basic Law allow prolonged fiscal deficits. FS stressed that Hong Kong would go against its constitution if the Administration did not adhere to prudent principles in managing public finances.

13. Mr LEE Wing-tat pointed out that over the past four years, a fiscal deficit was only recorded in 1998-99. Even in the case of 1999-2000, the original estimate was that there would be a deficit in this year, but the provisional 1999-2000 outturn had now indicated a fiscal surplus. He expressed concern about the Administration's strategy in using a deficit projection to curtail new initiatives in expenditure when drawing up the 2001-02 Budget. He was worried that some important policy areas such as employees retraining and education would not be given adequate resources. He also cautioned that if FS was too conservative in mapping out his expenditure strategies, the latest economic rebound would not be sustainable.

14. FS invited Members to refer to Charts 5 and 6 of the background information note and to consider these two charts in conjunction. He drew Members' attention to the need to look closely at successive years of operating deficits rather than occasional occurrence. Indeed, certain items of revenue or expenditure of a special or one-off nature could affect the final outturn of a particular year. For example, the level of fiscal surplus/deficit in 2000-01 and 2001-02 could be affected by the proceeds from the partial privatization of the Mass Transit Railway Corporation. Any sizeable reduction in the forecast income of \$15 billion from the flotation in 2000-01 could increase the forecast deficit considerably. Operating deficits could only be tolerable in the short term but FS said that the Administration must not allow them to continue over the medium and long terms. Despite the better than expected fiscal outturn in 1999-2000, the Administration was obliged to remain vigilant and examine carefully any hidden problems in public finances. It was therefore the Government's intention to restrict the growth of Government expenditure to 2.5%, as he had made clear in the 2000-01 Budget.

New money for new initiatives

15. Mr LEE Cheuk-yan referred to Chart 9 of the background information note and enquired about the amount of uncommitted new money for 2001-02. As there was a fiscal surplus of \$9.9 billion in 1999-2000, he asked whether FS would make available more new money and consider relaxing the cap of 2.5% growth in recurrent expenditure. Specifically, Mr LEE considered that more funds should be injected to the Employees Retraining Board (ERB), which he understood would be running out of its financial reserves in one or two years, and financial incentives should be provided to employers for releasing their employees to attend vocational training courses.

16. FS responded that to restrict to 2.5% in the medium term was a strategy to restore the balance between the growth in Government spending and that of the economy in the medium term. The community had by and large expressed support for this strategy. A 2.5% growth in recurrent expenditure together with the savings resulting from the Enhanced Productivity Programme (EPP)

would provide quite substantial room for funding new initiatives. As such, he did not consider it appropriate to depart from that strategy at this stage.

17. In this connection, the Acting Secretary for the Treasury (Atg S for Tsy) pointed out that in recognition of the importance of the work of ERB, the Administration had provided capital grants to it on four occasions totalling some \$1.6 billion over the past few years. She assured members that ERB had adequate financial resources to implement its planned programmes up to the fourth quarter of 2001. Having regard to members' view expressed at a Special Finance Committee meeting to provide a stable source of funding for ERB, the Finance Bureau (FB) and the Education and Manpower Bureau were actively examining the matter.

18. As regards the amount of uncommitted new money for new initiatives in 2001-02, Atg S for Tsy advised that capping the increase in recurrent expenditure to 2.5% would bring about new money in the region of \$4.8 billion. Assuming a 2% savings in baseline expenditure under the EPP, an additional \$2 billion would be available as new money. As the earmarked growth (i.e. the resources needed to meet committed growth in activities) in a year would usually require some 80% of the new money for the year, the uncommitted new money available in 2001-02 would be in the order of \$1 billion to \$2 billion. She added that the Administration was reviewing the resource allocation for existing services and committed new/increased services to see whether they could be delivered in a more cost-effective manner. If so, more uncommitted new money would be made available to finance new initiatives.

Enhanced Productivity Programme

19. Mr CHAN Kam-lam pointed out that not all the bureaux, departments and agencies had the same potential for productivity enhancement. It was noticed that currently, many bureaux and departments had achieved their saving targets by simply outsourcing their services. This way of cost-saving might not be the most effective and he therefore enquired whether the Administration would consider setting up a committee to review the capability or potential for productivity enhancement of individual departments and to recommend appropriate EPP target and measures for each bureau, department and agency.

20. Atg S for Tsy responded that in view of the continual expansion of the public sector in the past and the advancement in technology, the Administration considered that there was room for all Government bureaux and departments to achieve at least 5% savings in operating expenditure over a three-year period. In fact, the requirement to achieve a cumulative 5% savings in operating expenditure by 2002-03 was only a short-term target. The Administration was committed to striving for sustained long-term improvement in public sector

productivity. Nevertheless, Atg S for Tsy pointed out that for policy reasons and on account of service needs, certain departments and agencies such as public sector schools and certain welfare services had been exempted from the requirement to achieve 5% savings. She assured Members that although there was no designated committee to oversee the EPP, implementation of the EPP had all along been closely monitored by the Administration to ensure that it was heading in the right direction.

21. Mr HO Chun-yan questioned the earlier pledges made by the Administration that despite the EPP, there would not be any reduction in the provision of services. He quoted the example of a youth centre in his constituency, which had to be closed down, and the plan for the setting-up of an elderly centre, which had been shelved because of EPP. He pointed out that he had no difficulty in providing a list of services being scaled down or terminated in his constituency since the implementation of EPP. He further commented that even the public had already got an impression that many public services including those of the Police had been adversely affected by the EPP.

22. FS advised that implementation of the EPP would inevitably involve the rationalization and re-prioritization of certain services to enable more effective deployment of resources. The bureaux and departments concerned would be prepared to discuss with Mr HO the circumstances of the changes to the services he mentioned. As far as the Police was concerned, FS stressed that he had been assured that there would be no reduction in frontline operation under the EPP. The Force had been provided with adequate resources on upgrading the use of technology.

23. Atg S for Tsy further clarified that when implementing EPP, the Administration had pledged to maintain service quality and to deliver quality services. However, there might be a need to rationalize, streamline or terminate certain services where there was duplication or under-utilization of services or when the services had become obsolete. Regarding youth centres, Atg S for Tsy advised that the current plan was not to close youth centres but to cease those services provided in existing youth centres which no longer met the present needs of young people. The Administration and the subvented sector had agreed to make use of the savings thus achieved to enhance school social work services. She acknowledged that in this process, there might be some mis-matching in manpower and FB was working closely with the Social Welfare Department to identify ways to facilitate the process to avoid staff redundancies. She assured Members that in the process of resource redeployment, the Administration would ensure that the interest of existing staff would be duly considered.

The lower-income sector

24. Mr LEUNG Yiu-chung pointed out that the Administration was not entirely successful in enhancing productivity through the EPP. Instead, through contracting out public services, the Administration had changed civil service jobs into low-paid jobs in the private sector with long working hours. He stressed that the unemployment rate still stood high, but he had not found any concrete measures mentioned by FS to ease the unemployment problem in his 2000-01 Budget Speech. Mr LEUNG asked whether FS would respond to calls from the community for creating more job opportunities by facilitating the development of industries on environmental protection.

25. FS emphasized that the EPP was an important service-wide exercise to achieve operating savings. There should be no doubt that it was worth pursuing. To improve the unemployment situation, it was necessary to strengthen the economy and upgrade the skills and knowledge of the workforce. He assured Members that the Administration was fully aware of the hardship brought about by unemployment and was actively exploring ways to address the problem. On the suggestion of facilitating the development of industries on environmental protection to provide more job opportunities, FS said that the initiative to establish these industries should come from the private sector while the Government would consider providing the necessary support.

26. Miss CHAN Yuen-han criticized the Administration for being insensitive to the hardship suffered by the lower-income sector and for driving wages further down by contracting out public services and lowering the remuneration for new appointees to the civil service. She cautioned that if the Administration did not take appropriate measures to address the problem, social instability would result. She therefore urged the Administration to critically review the EPP and the provision of financial assistance and services to the lower-income sector.

27. FS reiterated that the Chief Executive, himself and his colleagues were deeply concerned about the difficulties faced by different sectors of the community. The Administration would spare no efforts in strengthening the economy and tackling the unemployment problem. He remarked that the economy was in the course of recovery but it would take some time before the public at large could benefit from the economic growth.

Spending on welfare

28. Mr Fred LI noted that since the implementation of the Support for Self-Reliance Scheme in June 1999, the growth in caseload of the Comprehensive Social Security Assistance Scheme (CSSA) and in the expenditure on CSSA payments had stabilized. As such, he urged the Administration to consider

restoring the special grant for spectacles which was abolished in 1998 following a review of CSSA. He pointed out that children of CSSA households now had to use their meal money to buy spectacles which was an essential item. He added that there was no possibility of abuse as the grant was paid on a reimbursement basis.

29. In response, Atg S for Tsy clarified that in the past, the CSSA covered a range of special grant items. This itemized mode of payment was considered not appropriate and thus, the CSSA payment system had been revised accordingly. Nevertheless, the Administration would always try to provide more support to the needy. For example, the approval of FC was sought in May 2000 for a financial commitment of over \$100 million to raise the subsidies payable under various student financial assistance schemes for children of needy families. FS said that the Support for Self-Reliance Scheme aimed at encouraging and assisting the able-bodied CSSA recipients to rejoin the workforce. The Government was committed to ensuring that CSSA households should be provided with the means for basic necessities.

Spending on education

30. Mr CHEUNG Man-kwong recalled that the Administration had earmarked \$800 million for taking forward various education reform measures in 2000-01. As the uncommitted new money available in 2001-02 was estimated to be \$1 billion to \$2 billion only, he was concerned whether adequate funds would be available for implementing reform measures in 2001-02. FS reiterated that education was a priority area as highlighted by the Chief Executive in his Policy Addresses. Indeed, spending on education accounted for over 20% of the total public expenditure for the current year. He added that while proposals on education reform were still under consultation, the Administration would allocate sufficient funds for implementing new measures which were necessary and cost-effective.

Spending on economic services

31. Noting that the recurrent expenditure for the policy area of economic services had only accounted for about 4% of the total Government recurrent expenditure, Mr James TIEN enquired whether the Administration would allocate more resources to this policy area in 2001-02 to help the local business sector to capitalize on the business opportunities arising from the imminent accession of China to the World Trade Organization. In reply, FS confirmed that the Administration would take positive steps in this regard and was already discussing with the Central People's Government on how Hong Kong's business sector could contribute to and capitalize on this development. He also welcomed suggestions from Members as to what measures the

Administration might take in this regard.

32. Mr Kenneth TING pointed out that due to the linked exchange rate system, the interest rate in Hong Kong remained high. On the other hand, the Special Finance Scheme for Small and Medium Enterprises (SMEs) had ceased accepting new applications in April 2000. In view of the financing difficulties faced by SMEs at this early stage of economic recovery, he enquired whether the Administration would explore other measures to assist SMEs. FS recapitulated that the main purpose of the scheme was a relief measure for SMEs when they faced severe credit stringency. As there had been marked improvement in the liquidity of the banking sector, the Administration considered that there were no longer compelling grounds to continue with the scheme. He however reiterated that the Government would continue to provide appropriate support for SMEs on various fronts.

33. The Convenor said that Members were at liberty to forward their views in writing to FS on the 2001-02 Budget. FS added that he would welcome further suggestions and views from Members, verbally or in writing.

34. The briefing ended at 12:35 pm.

Legislative Council Secretariat
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