

28th March, 1940.

PRESENT:—

HIS EXCELLENCY THE GOVERNOR (SIR G. A. S. NORTHCOTE, K.C.M.G.).

HIS EXCELLENCY THE GENERAL OFFICER COMMANDING THE TROOPS, (MAJOR GENERAL A. E. GRASETT, D.S.O., M.C.).

THE COLONIAL SECRETARY (HON. MR. N. L. SMITH, C.M.G.).

THE ATTORNEY GENERAL (HON. MR. C. G. ALABASTER, O.B.E., K.C.).

THE SECRETARY FOR CHINESE AFFAIRS (HON. MR. R. A. C. NORTH).

THE FINANCIAL SECRETARY (HON. MR. H. R. BUTTERS, *Acting*).

HON. COMMANDER G. F. HOLE, R.N. (Retired), (Harbour Master).

HON. MR. T. H. KING (Commissioner of Police).

HON. DR. P. S. SELWYN-CLARKE, M.C., (Director of Medical Services).

HON. MR. A. B. PURVES (Director of Public Works).

HON. SIR HENRY POLLOCK, KT., K.C., LL.D.

HON. MR. J. J. PATERSON.

HON. MR. LO MAN-KAM.

HON. DR. LI SHU-FAN.

HON. MR. A. L. SHIELDS.

HON. MR. W. N. T. TAM.

MR. C. B. BURGESS (Deputy Clerk of Councils).

ABSENT:—

HON. MR. S. H. DODWELL.

HON. MR. LEO D'ALMADA E CASTRO, JNR.

MINUTES.

The Minutes of the previous meeting of the Council were confirmed.

ANNOUNCEMENT.

THE COLONIAL SECRETARY.—Sir, in order that the telegrams exchanged on the subject of the Colony's war contribution, the text of which has already been published in the local press, may have a place on the records of this Council, I am commanded by Your Excellency to recite the following:—

From Governor, Hong Kong, to Secretary of State, dated 14th March, 1940.

"I have the honour on behalf of the Colony of Hong Kong to offer to His Majesty's Government as contributions towards the prosecution of the war the following amounts.

- (a) \$5,000,000 towards the construction and equipment of two mine-sweeping vessels, four harbour defence vessels and two ferry tenders
- (b) a gift of £100,000 in cash.

These amounts were unanimously voted in the Legislature to-day."

From Secretary of State, to Governor, Hong Kong dated 15th March, 1940.

"Please convey to the Legislative Council of Hong Kong the sincere thanks of His Majesty's Government for their exceedingly generous decision to offer an immediate gift to His Majesty's Government of £100,000 towards the prosecution of the war and to provide for the construction of naval vessels from the proceeds of special war taxation. His Majesty's Government deeply appreciate these very practical contributions by the people of Hong Kong towards the successful prosecution of the war."

PAPERS.

THE COLONIAL SECRETARY.—By Your Excellency's command, I lay upon the table certain papers, copies of which are in the hands of Honourable Members.

The Papers laid were as follows:—

Amendment made by the Governor in Council under section 3 of the Importation and Exportation Ordinance, 1915, Ordinance No. 32 of 1915, to the prohibitory order relating to the importation of certain merchandise from Macao, dated 14th March, 1940.

Order made by the Controller of Trade under the Defence Regulations, 1939, with the consent of the Governor, prohibiting the export, except by licence, of Nickle Coins, dated 15th March, 1940.

Copy of Secretary of State's Despatch No. 82 of 29th February, 1940, with enclosures, relative to Hong Kong Military Contribution.

Administration Reports, 1939:—

Part II.—Law and Order:—

Report of the Commissioner of Prisons.

FINANCE COMMITTEE'S REPORT.

THE COLONIAL SECRETARY, by command of H.E. The Governor, laid upon the table the Report of the Finance Committee (No. 2), dated 14th March, 1940, and moved that it be adopted.

THE FINANCIAL SECRETARY seconded, and this was agreed to.

TELEPHONE AMENDMENT BILL, 1940.

THE FINANCIAL SECRETARY moved the first reading of a Bill intituled "An Ordinance to amend the Telephone Ordinance, 1925, as amended by the Telephone Amendment Ordinance, 1930, and the Telephone Amendment Ordinance, 1933." He said: Your Excellency,—The Taxation Committee which you, Sir, appointed in 1938 "to consider and report what methods of taxation could best be adopted in the Colony, should it be necessary to raise additional revenue, having regard to the Colony's general economic position and the importance of distributing any additional burden in the most equitable manner in relation to the incidence of existing taxation" among its minor recommendations under the heading Utility Companies stated, in connection with the Telephone Company, "We are informed that the present franchise of this Company is unsatisfactory in various ways both to the Company and to Government and we recommend that the possibility of revision in such a manner as to secure higher royalties for Government, while removing the features which are at present objectionable to the Company, should be investigated in collaboration with the Company".

Before the Telephone Ordinance No. 9 of 1925, which it is now proposed further to amend, was introduced into this Council a Resolution moved by the then Colonial Secretary, Sir Claud Severn, was passed. That Resolution described the negotiations which led up to the determination under the Ordinance of the franchise to operate telephones which had been granted in 1905 by the Government to the China and Japan Telephone and Electric Company, Limited and the

creation of its successor, the present Hong Kong Telephone Company. The main objects of Government in 1925 were to secure that the Company should in future be domiciled in Hong Kong and work on a dollar basis and to provide an improved telephone service in the Colony. The first object was realised by requirements in respect of the registration and articles of the Company and the number and residence of its directors. They must all be *bona fide* resident in Hong Kong. The present Bill merely increases their number. There can be no doubt, I think, that the second object also has been achieved and that the achievement is due to the efficiency of this Hong Kong Company working within the scheme of an ordinance which places the ultimate control of its activities in the hands of the Governor-in-Council and of this Council.

In framing an Ordinance governing a public utility company the interests of three parties have to be considered, though in a final analysis these may be reduced to two: the public generally, and that part of the public which subscribes for the services rendered by the Company, and the shareholders of the Company. The 1925 Ordinance, therefore, in addition to making provision for a royalty, controlled both dividends and subscription rates.

The net profits of the Company were dealt with in the Resolution as follows:—

They were to be used firstly in payment to Government, as the representative of the public, of a royalty of \$4 in respect of each direct exchange line telephone; secondly in payment to the shareholders of the Company of a minimum dividend of 8 per cent. per annum rising to 12 per cent. per annum; thirdly in the event of the net profits exceeding 12 per cent. per annum then as to the difference between 12 per cent. and 18 per cent., half thereof was to be distributed in further dividends and the remaining half employed in the reduction of the subscription rates; the dividend payable to shareholders being limited to a maximum rate of 15 per cent. Any additional surplus was to be used solely for the reduction of subscription rates.

Effect was given to these proposals by the Telephone Ordinance, 1925. According to the schedule of that Ordinance the annual rate to be paid by subscribers per exchange line within Victoria, Kowloon and the Peak district was \$108, subject to revision upwards if the rate was found to be insufficient to make provision for an efficient service and for the payment of the minimum dividend of 8 per cent. per annum. In this connection it will be remembered that the dollar in 1925 was the equivalent of 2s. 4d.

In 1930 the annual rate was increased, with the approval of this Council to \$117 per exchange line, at which figure it has remained. With the flat rate basis, by which subscribers in Hong Kong may have unlimited calls for the standard rate of subscription, it is difficult to make accurate comparison, yet it may safely be said that the Hong Kong

telephone subscription rate compares favourably with the lowest to be found elsewhere and that the modern service provided is of a high standard notwithstanding the exacting climatic conditions. The interests of the subscriber have, therefore, been well served. I would remark in passing that the Telephone Committee, 1922, appointed to report on the telephone service in Hong Kong recommended an annual rate of \$120 for the year 1926 under the old manual system and expected that the cost of a modernised system would necessitate a further substantial increase in that figure. That the charges had been kept down to the present rate has been due to a combination of two factors: the good fortune and the good guidance of the Hong Kong Telephone Company. The Company was fortunate in that its equipment was purchased during a period of keen competition among manufacturers at about one-third of what it would cost to-day, and it has shown its foresight in providing a large margin of plant for future growth at the favourable prices which then prevailed. The Company has been run economically and the premium at which its shares were issued was utilised to write off old plant, while no bonus shares have been issued at any time.

As the Taxation Committee remarked, however, there are certain features in the Ordinance under which the Company functions which are not satisfactory to the Company; for instance, it is argued that the absolute limit of 15 per cent. dividend is inequitable because the high rate of profits is due largely to the efficiency of the Company and to the Canton line which was not in existence when the original arrangement was made. An absolute maximum gives the Company no incentive to earn further profits by greater efficiency and economy after that point has been reached.

Moreover, the present system of contributing to a reserve fund for the redemption of the Company's capital is not entirely satisfactory. A fixed sum of \$170,482 is put aside yearly, which is sufficient to amortise the whole capital by 1975, but interest on investments of that fund goes into general profit and loss account, while there is no provision for dealing with depreciation of these investments.

The present Bill gives effect to negotiations with the Company which were initiated and practically brought to conclusion by Mr. Caine, with a view to removing those objectionable features in the Ordinance and at the same time securing higher royalties and other advantages to Government. The arrangement incorporated in the present Bill is as follows:—

The Company provides Government free of charge with a telephone service for Government purposes up to 500 lines and arranges for the necessary branch exchange in a place sufficiently protected from possible air raid damage. This exchange has been constructed in the basement of the Hong Kong and Shanghai Bank Building.

The modernisation of the Government system, which is obsolescent, would involve considerable expenditure and on technical grounds it is desirable to amalgamate the Government with the Company's system.

The provision of this exchange represents a capital saving to Government of roughly one-quarter of a million dollars. Also a discount of 25 per cent. will be allowed Government on the standard rate of subscription in respect of any telephones or connections in excess of these 500 lines. Arrangements will be made later for the Company to take over other Government services when it is possible to obtain the necessary equipment, and until this matter has been further discussed from the technical angle it is difficult to estimate the ultimate saving to Government in respect of recurrent expenditure and personal emoluments, but an appreciable saving is anticipated in respect of both.

Also an additional royalty of one half of the surplus profits over and above the amount required to pay a 12 per cent. dividend on the paid-up capital shall be payable to Government. In order to avoid double taxation the Company is permitted to deduct any amount payable to Government by way of taxation on profits from the net annual profits of the Company before surplus profits are assessed for this purpose. This is based on the analogy of the treatment of such other utility companies as pay a royalty to Government which will be permitted to deduct the royalty from their profits before such are assessed for purposes of war taxation. It will be observed that the remaining half of the surplus profits remains at the disposal of the directors who need not necessarily employ it for the purpose of increasing dividends.

This arrangement will apply retrospectively to the year 1939, so that Government may anticipate a considerable addition to the royalty otherwise payable in respect of that year. It is felt that Government, as representative of the whole community, has a prior claim to a share of the surplus profits in preference to the subscribers who already enjoy a remarkably cheap rate of subscription.

The management of reserves has been varied by allowing depreciation of existing investments to be charged to the capital reserve at once and in respect of capital reserve in lieu of the appropriation of a sum not exceeding \$170,482 per annum there will be paid an appropriation not exceeding \$92,577 per annum, plus the total amount of interest and dividends received during the year from the investments made on account of this reserve. This sum is calculated as sufficient to accumulate the required amount in thirty-six years on a sinking fund basis of 3 per cent. Interest on investments made on behalf of the depreciation reserve will continue to be credited to profit and loss account. Depreciation of such investments will be debited against profits but any excess over their written down value on realisation will be credited.

The Bill is being introduced as a Government measure but its terms have been agreed to by the directors of the Company. In perusing the Hansard account of the first reading in this Council of the Telephone Ordinance, 1925, one meets frequent tributes to the ability and tact of Mr. Taggart who conducted the final negotiations

in connection with the foundation of the Telephone Company of which he was a promoter and is the managing director, and I should like to record that the Government representatives in the present negotiations with Mr. Taggart have again met the same high qualities of vision and breadth of judgment, to which testimony is borne by the success of the Company and the service it has rendered to the Colony.

THE COLONIAL SECRETARY seconded, and the Bill was read a first time.

Objects and Reasons.

The "Objects and Reasons" for the Bill were stated as follows:—

1. The terms of the concession granted to the Hong Kong Telephone Company Limited are contained in the Telephone Ordinance, No. 9 of 1925, as amended by the Telephone Amendment Ordinances, No. 9 of 1930 and No. 27 of 1933.

2. Under these Ordinances the company's dividend was restricted to 12 per cent. plus half of profits up to a further 6 per cent. the other half going to reduce subscription rates and in no case was the dividend payable to shareholders to exceed 15 per cent. (*See* Ordinance No. 9 of 1925, s. 36). Thus one half of the profits between 12 per cent. and 18 per cent. and all profits above 18 per cent. was to be devoted to reducing the rates payable by the subscribers.

3. The Company's directors have argued, in discussions with the Government's Financial Advisers during recent months, that the absolute limit of a 15 per cent. dividend is inequitable because the high rate of profits which the Company has been able to earn has been due largely to its efficiency and partly to the profits on the line to Canton which was not in existence when the original arrangement was made.

4. A reasonable objection to an absolute maximum is that it gives the company no incentive to earn profits by greater efficiency and economy after that maximum is reached.

5. Moreover the existing subscription rates are regarded as reasonably low and further contribution to the public revenue by way of royalty and a contribution of certain free lines for Government purposes has been considered a reasonable basis for settlement in existing circumstances.

6. The proposed amendments are shown in greater detail in the attached Table of Correspondence.

7. The Bill is to be introduced as a Government measure; but its terms have been agreed to by the directors of the company.

ADJOURNMENT.

H.E. THE GOVERNOR.—Council stands adjourned *sine die*.