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Legislative Council

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Legislative Council
Panel on Financial Affairs

Minutes of special meeting held on
Friday, 20 April 2001 at 8:30 am
in the Chamber of the Legislative Council Building

Members present : Hon Ambrose LAU Hon-chuen, JP (Chairman)
Hon Henry WU King-cheong, BBS (Deputy Chairman)
Hon James TIEN Pei-chun, JP
Hon Albert HO Chun-yan
Dr Hon David LI Kwok-po, JP
Hon NG Leung-sing
Hon Bernard CHAN
Hon CHAN Kam-lam
Hon SIN Chung-kai
Dr Hon Philip WONG Yu-hong
Hon Jasper TSANG Yok-sing, JP
Hon Emily LAU Wai-hing, JP

Non-Panel Member attending : Hon Tommy CHEUNG Yu-yan, JP

Members absent : Hon LEE Cheuk-yan
Hon Eric LI Ka-cheung, JP
Hon James TO Kun-sun

Public officers attending : Hong Kong Monetary Authority

Mr Joseph YAM, JP
Chief Executive

Mr Raymond LI, JP
Executive Director (Corporate Services)

Mr Stefan GANNON, JP
General Counsel

Financial Services Bureau

Mr Stanley WONG
Deputy Secretary for Financial Services

Clerk in attendance : Mrs Florence LAM
Chief Assistant Secretary (1)4

Staff in attendance : Mr Jimmy MA
Legal Adviser

Ms Pauline NG
Assistant Secretary General 1

Ms Connie SZETO
Senior Assistant Secretary (1)1

I Permanent accommodation for the Hong Kong Monetary Authority
(LC Paper Nos. CB(1) 905/00-01, 994/00-01, 1022/00-01(01) & (02), 1038/00-01(01) & (02), and 1051/00-01(01) & (02))

The Chairman informed members that the purpose of the meeting was for the Administration to brief the Legislative Council (LegCo) Members on the proposed acquisition of premises at Two International Finance Centre (IFC II) as the permanent accommodation for the Hong Kong Monetary Authority (HKMA). He referred members to letter of 12 April 2001 from the Financial Secretary (FS) (LC Paper No. CB(1) 1022/00-01(01)) setting out FS' position on the matter and the reasons for declining the Panel's invitation to attend the meeting.

2. Members noted that HKMA intended to acquire an area of 280,000 sq. ft. as office for the Authority (i.e. 80,000 sq. ft. in excess of the size of its current accommodation at Citibank Tower) and an additional of 60,000 sq. ft. to provide for conference facilities and public access. The cost of the purchase, which was estimated by the market to reach HK$4 billion, would be charged to the Exchange Fund (EF).

3. The Chief Executive, Hong Kong Monetary Authority (CE/HKMA) said that he was aware that some LegCo Members had expressed serious concern over the proposed acquisition of the permanent accommodation. He responded to the three major issues relating to the concern as follows :

(a) Arguments for the acquisition of the new accommodation

HKMA's financial analyses had suggested that it would be more economical to purchase rather than to lease offices for HKMA in the long run. The provision of permanent accommodation would enable HKMA to enhance its security arrangements.

(b) Legal basis for using EF for the proposed acquisition

The decision to purchase the premises was made by FS after seeking the advice of the Exchange Fund Advisory Committee (EFAC). FS was the controller of EF and was responsible for the management and operation of the Fund as provided under section 3 of the Exchange Fund Ordinance (EFO) (Cap. 66). Section 6(a) of EFO provided that "the emoluments payable to, and other staff costs relating to, the persons employed in connection with the purposes of the Fund" shall be charged to the Fund. As the office accommodation of HKMA staff was clearly a "staff cost" in the context, the use of EF to purchase the premises was intra vires EFO.

(c) Transparency and public accountability of HKMA's operations

HKMA was committed to enhancing its openness and accessibility to the public and LegCo. Apart from explaining to the public and briefing LegCo Members on its work on a regular basis, HKMA was subject to scrutiny of EFAC and the Director of Audit whose staff members had a continuous presence in HKMA. As for transparency of the proposal, the Panel on Financial Affairs was informed of the proposed acquisition in January 2001. An information paper was issued in March 2001 to provide members with details on the proposal.

Arguments for the proposed acquisition

4. Mr David LI, Mr NG Leung-sing, and Mr Philip WONG supported the proposal. They considered it appropriate to provide HKMA with separate and clearly identifiable premises. The practice was in line with other premier international financial centres which also housed their central banking institutions and regulatory authorities in separate and dedicated office premises.

5. Some members questioned the need to acquire an extra of 140,000 sq. ft. in the new premises and urged HKMA to provide details on the usage of the space.

6. CE/HKMA explained that 80,000 sq. ft. of the extra space would cater for possible future needs of HKMA. Possible new duties for HKMA included consumer protection for bank customers, supervision of the deposit insurance system and the Credit Reference Agency, etc. Given the long term nature of these activities, it would be difficult to specify their requirements in detail. Moreover, a number of international financial institutions, such as the Bank for International Settlements, the World Bank and the International Monetary Fund, had expressed an interest to expand and establish offices in Hong Kong. The HKMA should also cater for such needs. Any space in the new accommodation which was not used immediately would be let to suitable tenants at market rate. It was estimated that letting of the space could secure a reasonable return of 6% to 7% for EF. Therefore, it would be cost effective and prudent planning to cater for such future needs at the outset. The remaining 60,000 sq. ft. would be used mainly to provide purpose-built conferencing facilities to enable HKMA to provide high quality venue for international conferences and seminars for the international financial community and to provide public access facilities to enhance the public's understanding of the financial system and the works of HKMA. The HKMA saw the latter as an important step in enhancing the transparency and accountability of its operations.

7. Given that the financial investments of EF had achieved good returns for the Fund over the past years, Mr James TIEN was of the view if the cost for acquiring the premises was invested in the financial market, it might give a better yield for EF. Miss Emily LAU was concerned that the premises might become a negative asset in view of the slack performance of the property market. Mr Albert HO considered that using EF to make the purchase would change the asset composition of the Fund and could affect its liquidity adversely.

8. In response, CE/HKMA emphasized that the proposed acquisition was cost effective. According to HKMA's analyses, it would take less than 20 years to recoup the cost of purchasing the premises from rental savings. As the transaction was still under negotiation, commercially sensitive information

could not be disclosed at the moment. HKMA would provide details on the financial analyses when such information could be disclosed. CE/HKMA stressed that the main purpose of the acquisition was to provide permanent accommodation for HKMA. The purchase would represent a profitable investment of EF. There were guidelines on asset composition of EF. The purchase would not breach any of the guidelines. The cost for purchasing the premises was insignificant when compared with the huge size of EF which currently exceeded HK$ 1 trillion. HKMA did not envisage that the liquidity of EF would be adversely affected.

HKMA

(*Post-meeting note:* The results of the financial analyses were disclosed in connection with the signing of a memorandum of agreement by the FS on 28 April 2001.)

9. Mr James TIEN commented that in order to request the property developers of IFC II to provide HKMA with customized security arrangements and access facilities to suit its unique requirements, HKMA could consider the alternative of negotiating with the developers to arrange a rental contract of over 30 years. CE/HKMA replied that as IFC II was under construction, the acquisition would enable HKMA to ensure that the design of the building would meet its operational requirements. These included the introduction of enhanced and customized security arrangements to meet its special needs and the provision of a separate lift lobby for the offices. HKMA received a significant number of distinguished guests, such as governors of central banks and finance chiefs from the Mainland and overseas. There had been comments that the security arrangements at HKMA's present accommodation would need to be improved. Currently, a substantial quantity of confidential and market sensitive information was stored electronically at HKMA's office premises. The acquisition of the new premises would enable HKMA's cabling and telephone lines to be laid in dedicated trunkings, thus ensuring the security of HKMA's market operations.

10. Responding to Mr Henry WU's enquiry as to whether HKMA had considered other locations for its permanent office, such as the proposed Central Government Offices at Admiralty, CE/HKMA said that as the final decision on the use of the site at Admiralty was still outstanding, FS had instructed that other locations should be considered. Given the Government policy of housing all major financial regulators under one roof, and the fact that the Mandatory Provident Fund Schemes Authority (MPFA) and the Hong Kong Exchanges and Clearing Limited (HKEx) had already moved into IFC in 1999 and 2000 respectively, the Government considered IFC II to be a suitable location for the permanent office of HKMA.

11. Miss Emily LAU doubted whether LegCo had been consulted on the government policy of housing all major financial regulators in one strategic location. Noting that MPFA and HKEx were accommodated in rented

premises at IFC, Miss LAU questioned the rationale for HKMA to acquire its offices at the building. She also expressed concern that housing all financial regulators in the same building could pose a risk. The Deputy Secretary for Financial Services replied that the government policy was announced in 1997. The main objectives were to enhance communication among the regulatory bodies and to facilitate sharing of common market infrastructure. However, individual financial institutions had their own considerations as to whether they should acquire or rent their offices at IFC.

12. Some members expressed concern that the announcement of the "one-roof" policy in 1997 might have put HKMA in a disadvantaged position when negotiating with the developers. CE/HKMA assured members that HKMA had engaged property consultants to handle the purchase to ensure that the price for the accommodation was reasonable. According to the analysis of the Government Property Agency, the price for the premises was below the prevailing market price.

Legality of using the Exchange Fund to purchase the premises

13. Mr Albert HO pointed out that section 3(1) of EFO had clearly stipulated that the primary purpose of EF was to maintain the stability of Hong Kong dollar. However, the acquisition of the HKMA's permanent accommodation was unrelated to this purpose. Mr HO and Miss Emily LAU considered that the cost of purchasing the accommodation should be charged to the general revenue and should be subject to the approval of the Finance Committee of LegCo. They expressed serious doubt over the argument put forward by HKMA's legal adviser that "other staff costs" under section 6(a) of EFO should include "cost for accommodation of staff" and hence the cost for the purchase could be met by EF. They cautioned that if such a wide interpretation of section 6(a) was accepted, the provision could be easily abused and EF could be used to meet any expenses incurred by HKMA. Their views were shared by Mr TSANG Yok-sing and Mr Henry WU.

14. CE/HKMA explained that sections 3(1) and (1A) of EFO provided FS with the power to use EF for purposes either directly or indirectly affecting the exchange value of Hong Kong dollar, and to maintain the stability and integrity of its monetary and financial systems, with a view to maintaining Hong Kong as an international financial centre. HKMA was delegated the authority to achieve these purposes. Providing HKMA with accommodation and systems for its operation would be consistent with these purposes. CE/HKMA assured members that HKMA would not abuse its power in using EF to meet its expenses. All expenditure incurred by HKMA was reasonable and had been made in good faith.

15. Members noted that the LegCo Legal Adviser (LA) had written to HKMA to seek clarification on the legal bases for charging the cost of the purchase to EF and that HKMA's legal adviser had responded reiterating his previous position. Mr Albert HO and Miss Emily LAU suggested that FS should be asked to seek the advice of the Department of Justice on the matter. In order to facilitate further discussion by the Panel, Mr Albert HO requested LA to provide a paper setting out the legal issues relating to the subject.

(*Post meeting note*: LA's paper was circulated to members vide LC Paper No. CB(1) 1120/00-01 on 2 May 2001.)

16. Mr Albert HO pointed out that FS' decision to use EF for purchasing the accommodation was inconsistent with the position which he took at the debate on the 2001-02 Budget, where he had repeatedly stressed the need for the Government to retain sufficient reserves under EF for defending the Hong Kong dollar and hence had refused the demand of the public to use the sizable reserves accumulated to fund new initiatives to relieve the hardship suffered by the community. He urged the Administration to explain its fiscal policy and what it considered to be the appropriate level of EF.

17. As regards the relationship between the Government's fiscal reserves and EF, CE/HKMA said that they were two separate and distinct entities. The fiscal reserves, which currently stood at over HK$430 billion, had been accumulated from the budget surpluses over the years. He recognized that there had been strong public demand for the Government to use the substantial reserves to address the needs of the community. If this was considered appropriate, the necessary amount could, at any time, be withdrawn from EF. Furthermore, Section 8 of EF provided a mechanism for FS, after satisfying certain conditions, to transfer the accumulated surplus of the EF to the general revenue. One condition was that FS should be satisfied that such transfer would not adversely affect the purposes of EF as stipulated in section 3(1) or (1A) of EFO.

18. On the question of adequacy of foreign reserves, CE/HKMA said that under the Linked Exchange Rate system and the currency board arrangements, theoretically it was only necessary for Hong Kong to maintain the level of foreign reserves at US$28 billion in order to provide full backing for the current monetary base of HK$220 billion. However, experience had suggested that Hong Kong needed considerably more in foreign reserves than this theoretical minimum to maintain currency stability. The amount of foreign reserves utilized for defending the Hong Kong dollar against manipulative attacks on the currency during the international financial crisis of 1997/98 was as much as US$38 billion. This was over three times of the theoretical minimum of US$12 billion for backing the then smaller monetary base of HK$95 billion. It was difficult, if not impossible, to derive a clear-cut and scientific formula for determining the appropriate level of foreign reserves.

Given that Hong Kong was a small economy with an entirely open market, it would be prudent to maintain a level of foreign reserves well above the theoretical minimum in order to strengthen the financial position of EF for meeting possible vulnerabilities and risks.

Issues about accountability and transparency

19. Mr Albert HO and Miss Emily LAU expressed strong dissatisfaction about the allegation of political interference by LegCo Members over the operations of EF as contained in FS' letter of 12 April 2001. They considered that it was the duty of LegCo to monitor the operations of EF and HKMA. Mr TSANG Yok-sing added that it was legitimate for LegCo to ask the Government questions on the management and control of EF, as this was one of the means for ensuring the Government's accountability. They considered that the Government should provide detailed information on the proposed acquisition in a timely manner to facilitate monitoring by LegCo.

20. CE/HKMA stressed that it was beyond doubt that LegCo had a legitimate interest in monitoring the use of public funds, regardless of whether it was the general revenue or EF. The Administration was vested with the power to control and manage EF and had been discharging this responsibility in a highly transparent manner. There was no adverse reaction from members of the Panel after the intention to purchase permanent accommodation for HKMA was disclosed in January 2001. An information paper was specifically prepared in March 2001 to update members on the progress. CE/HKMA also said that he had accepted members' invitation to attend the present meeting to brief them on further details on the subject. However, the success of Hong Kong's monetary management and the credibility of its monetary policy depended crucially on the independence of the monetary authority in discharging its responsibilities. Any indication from LegCo Members to halt the negotiation on the purchase using EF could be interpreted by the international financial community as fettering the independent and exclusive power of FS provided under EFO. This would undermine their confidence in Hong Kong's monetary and financial systems.

21. On the issue of public scrutiny, CE/HKMA fully agreed that the greater the independence in the control of EF the greater the need for arrangements to ensure that those exercising the authority were accountable. The degree of transparency in the operations of HKMA was already exceedingly high by international standards. The accountability arrangements mentioned in the above discussion were working effectively. HKMA welcomed advice from LegCo Members and the public on ways to further enhance it public accountability.

22. In this connection, Members were of the view that it was necessary to conduct a comprehensive review on the structure and operation of HKMA and EFO. In response, CE/HKMA advised members that the Administration, by its own initiative, had planned to further clarify the policy objectives, the mandates, the authority, and the governance and accountability arrangements of HKMA to ensure that it was able to discharge its functions effectively and professionally.

23. As regards Miss Emily LAU's comment that EFAC might be ineffective in monitoring the operations of HKMA, as majority of the members were from the banking sector whose business was regulated by HKMA, CE/HKMA stressed that EFAC comprised experts who were leading figures in the financial services sector with extensive knowledge and experience. He was confident that these members were able to provide objective advice on the management of EF and the operations of HKMA. He did not concur with Miss LAU's view that there would be role conflict on the part of members.

24. Members agreed that the Panel should follow up the subject. The development on the matter should be kept in view and further meetings would be convened when necessary.

II Any other business

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

Legislative Council Secretariat
9 July 2001