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**Notes on the Special Briefing for Finance Committee Members  
on Thursday, 11 March 2004, at 10:30 am  
in the Chamber of the Legislative Council Building**

**Members present:**

Dr Hon Philip WONG Yu-hong, Chairman of the Finance Committee (Convenor)  
Hon Kenneth TING Woo-shou, JP  
Hon James TIEN Pei-chun, GBS, JP  
Dr Hon David CHU Yu-lin, JP  
Hon Cyd HO Sau-lan  
Hon Albert HO Chun-yan  
Hon LEE Cheuk-yan  
Dr Hon Eric LI Ka-cheung, GBS, JP  
Hon Fred LI Wah-ming, JP  
Hon Margaret NG  
Hon Mrs Selina CHOW LIANG Shuk-ye, GBS, JP  
Hon HUI Cheung-ching, JP  
Hon CHAN Yuen-han, JP  
Hon Bernard CHAN, JP  
Hon Jasper TSANG Yok-sing, GBS, JP  
Hon Howard YOUNG, SBS, JP  
Hon LAU Chin-shek, JP  
Hon LAU Kong-wah, JP  
Hon Miriam LAU Kin-ye, JP  
Hon Emily LAU Wai-hing, JP  
Hon CHOY So-yuk  
Hon Andrew CHENG Kar-foo  
Hon Timothy FOK Tsun-ting, SBS, JP  
Dr Hon LAW Chi-kwong, JP  
Hon TAM Yiu-chung, GBS, JP  
Hon Abraham SHEK Lai-him, JP  
Hon LI Fung-ying, JP  
Hon Henry WU King-cheong, BBS, JP

Hon Michael MAK Kwok-fung  
Hon LEUNG Fu-wah, MH, JP  
Dr Hon LO Wing-lok, JP  
Hon Frederick FUNG Kin-kee  
Hon LAU Ping-cheung  
Hon Audrey EU Yuet-mee, SC, JP

**Public officers attending:**

Mr Henry TANG Ying-yen, GBS, JP	Financial Secretary
Mr Frederick MA Si-hang, JP	Secretary for Financial Services and the Treasury
Mr Alan LAI Nin, GBS, JP	Permanent Secretary for Financial Services and the Treasury (Treasury)
Mr TANG Kwong-yiu	Government Economist
Miss Elizabeth TSE, JP	Deputy Secretary for Financial Services and the Treasury (Treasury)
Ms Rhoda CHAN	Principal Assistant Secretary for Financial Services and the Treasury (Treasury)
Mr K K LAM	Principal Executive Officer (General), Financial Services and the Treasury Bureau (Treasury)
Ms Shirley YUEN	Administrative Assistant to Financial Secretary
Mrs Avia LAI	Administrative Assistant to Secretary for Financial Services and the Treasury

**Staff in attendance:**

Ms Pauline NG	Assistant Secretary General 1
Miss Becky YU	Chief Council Secretary (1)1
Mrs Mary TANG	Senior Council Secretary (1)2
Ms Caris CHAN	Senior Legislative Assistant 1
Mr Frankie WOO	Legislative Assistant 2

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Action

The Convenor welcomed Mr Frederick MA Si-hang, Secretary for Financial Services and the Treasury (SFST) and his colleagues to the briefing. He also informed members that Mr Henry TANG Ying-yen, Financial Secretary (FS), who had to attend a radio programme in the morning, would arrive later.

2. SFST gave a power-point presentation on Hong Kong's economic performance in 2003-04, the 2004 medium range forecast (MRF), expenditure initiatives, and revenue raising measures. The Government Economist also briefed members on the current economic situation. Details were set out in charts 9 to 23 of the information booklet attached at the Annex. FS joined the meeting at 11:30 am.

**General economy**

3. Mr James TIEN said that Members of the Liberal Party would support in general the 2004-05 Budget as proposed. Referring to operating revenue, he opined that Government's forecasts of \$170.7 billion for 2005-06 and \$165.6 billion for 2004-05, which were based on the actual figures for 2003-04, were overly conservative having regard to the rapid rebound of the economy following the recovery from the outbreak of Severe Acute Respiratory Syndrome (SARS). The fiscal reserves for 2008-09 which were estimated at \$158.4 billion after bond issuance should also include proceeds from the sale of Government assets and the repayment of Government bonds. Given the revitalization of the economy and the anticipated increase in revenue, Mr TIEN held the view that the 0.5% increase in salaries tax as proposed in last year's Budget should not be implemented to allow the middle class group, which was hardest hit by the economy in the past year, an opportunity of respite.

4. In response, SFST said that given the substantial fiscal deficit, the Administration was more inclined to be conservative in preparing the 2004-05 Budget. He confirmed that the projected fiscal reserves for 2008-09 had included proceeds from the sale of Government assets. In 2003-04, Government had secured \$15.5 billion from the sale of housing loans to the Hong Kong Mortgage Corporation (HKMC). In 2004-05, Government planned to realize \$17 billion from the sale of assets or through securitization of revenues. These included \$6 billion each from the return of capital from the Airport Authority and the securitization of revenues from government toll tunnels and bridges as well as \$5 billion from sale of student loans. It was estimated that Government would sell or securitize assets of a total value of about \$112 billion from 2003-04 to 2008-09. This estimate was the same as that of last year except that the implementation period had been lengthened to allow sufficient time to realize the proceeds from the sale of assets and securitization. He added that raising funds through issuance of bonds had the advantage of increasing the flexibility of the Government's asset sale and securitization programme, thereby obviating the need to sell Government assets at low prices under unfavourable market conditions. As for the repayment of Government bonds, SFST said that details of the repayment arrangements had yet to be worked out and would be provided to Members in due course. The amount of repayment to be made by Government would be reflected clearly in the estimates of the corresponding years.

5. Mr Henry WU indicated support for the 2004-05 Budget, including the proposal to issue bonds to finance infrastructural projects. He hoped that the bonds would be successfully issued with participation of the financial services sector. Mr HUI Cheung-ching asked if Government bonds could be sold to retail investors. SFST said that channels would be provided for retail investors to buy Government bonds in the market through financial intermediaries, similar to the existing arrangements for bonds issued by HKMC. The issuance of Government bonds would also help promote the development of bond market.

6. Despite the package of measures to reduce public expenditure, Mr Eric LI noted that some of the international rating agencies were still criticizing the Administration for taking years to balance the budget. He asked how the Government could restore confidence in the 2004-05 Budget. FS said that the 2004-05 Budget was prepared in accordance with prudent financial principles. It had sought to balance the competing demands of improving the livelihood of the community, restoring fiscal balance, providing respite and revitalizing the economy. The International Monetary Fund had commented that the Budget, though conservative, had upside gain potential. FS further pointed out that the Administration respected the views of rating agencies and sought to exchange views with them where appropriate. Nevertheless, rating agencies' rating might not always accurately reflect the market sentiments. For instance, the Mainland Government's overseas bond launched last year was traded at a price similar to that of a higher-rated bond.

7. At Mr Howard YOUNG's request, the Administration undertook to provide further information on the drastic drop in overall investment spending in the first quarter of 2002.

### **Goods and service tax**

8. While supporting the 2004-05 Budget, Mr Eric LI expressed concern that the proceeds from the sale of government assets and bonds might not be of much help to reduce the huge fiscal deficit which might in turn have impact on the fiscal reserves. He also questioned if it was right timing to implement the goods and service tax (GST) in three years' time given that the economic situation would be quite different then. FS advised that Government had set up an internal working group to conduct a detailed and comprehensive study on the implementation of GST in Hong Kong. It would draw on practical overseas experience and come up with a proposed GST framework suitable for Hong Kong and an implementation timetable for further discussion.

9. Mrs Selina CHOW welcomed the provision of additional funding of \$95 million for various tourism promotion and training activities. She however expressed disappointment over the Government's plan to introduce GST despite the strong objection from the business and service sectors as well as academics. Although GST would broaden the tax base and provide a steady revenue, it would have the undesirable effect of complicating the simple tax system in Hong Kong and adding financial burden to low-income families. GST would also have impact on the business and service sectors as well as the tourist industry. While tourists could be given tax refund, they still had to bear the administrative costs for the refund. She opined that extensive consultation on the introduction of GST should be conducted.

10. Miss Margaret NG was also concerned about the impact of GST on the service industries, particularly on the legal profession. She said that due to keen competition, the legal sector had been providing value-added service to their clients. Profit margin had decreased substantially because of the need to adhere to insurance requirements. The introduction of GST would further aggravate the problem as this would incur additional accounting and administrative procedures, resulting in higher legal costs. She agreed that extensive public consultation on the introduction of GST was essential.

11. In response, FS said that the implementation of GST would not give rise to unfair competition on the legal sector as it would be levied on all legal services. He agreed that GST was a controversial issue. As the report on introduction of GST would be submitted at the end of year, it was too early to comment on any tax concessions at this stage. He assured members that public consultation would be conducted on the introduction of GST. It was hoped that the matter would be fully debated by all sectors of the community with a view to finding common grounds. If the outcome of consultation revealed that the whole community was totally against the introduction of GST, the Administration would not push ahead with the proposal. Mrs CHOW welcomed the undertaking made by FS that the Administration would take into account the public views before proceeding further with the proposal.

12. Miss CHOY So-yuk said that Members of the Democratic Alliance for Betterment of Hong Kong agreed that the Budget would provide the community with the needed respite, but they had reservations about the introduction of GST.

### **Tax concessions**

13. Referring to the recent statistics which indicated an increased disparity of wealth since the return of sovereignty, Mr Frederick FUNG enquired about the measures to be put in place to reduce the disparity. FS said that the issue raised by Mr FUNG was a fundamental one and would involve the introduction of various measures, including taxation, to redistribute wealth. Given that the economy had just started to recover, there was a need to allow the community some form of respite. As such, he did not wish to introduce fundamental changes to the existing tax system at this stage but would give due consideration when the situation warranted.

14. While appreciating the extension of the duty concession for ultra low sulphur diesel which would alleviate the hardship faced by the transport trade, Ms Miriam LAU noted that the concession would expire in end-2004 and asked if this was due to the anticipated recovery of the economy by then. She said that although the economy had started to recover, the transport trade was still facing a lot of hardship. To this end, the trade had repeatedly requested that diesel duty be reduced to an affordable level. She also questioned the anomaly in the existing tax

policy on diesel whereby industrial diesel was non-taxable while diesel used by certain categories of vehicles such as public light buses and heavy vehicles was taxable but this was not applicable to ferries and franchised buses. FS explained that the duty on ultra low sulphur diesel was a steady source of revenue. The Administration would further review the concession after its expiry in end-2004. Meanwhile, the Secretary for the Environment, Transport and Works had been requested to review tax and fee concessions in line with the "polluter-pays" principle.

15. In response to Mr LAU Ping-cheung's question on profits tax deduction for design-related research and development expenses, FS confirmed that this would apply to planning and engineering projects undertaken by building professionals, and that such an arrangement had been agreed with the Inland Revenue Department.

### **Revenue-raising measures**

16. Given that smoking was hazardous to health, and that the \$2.2 billion duty from cigarettes was not enough to cover the health cost associated with smoking, Mr Michael MAK opined that there was a need to increase the duty on cigarettes which was in line with the polluter-pays principle on the one hand and would support the Anti-smoking Campaign on the other. Consideration should also be given to banning smoking in all public places. While sharing Mr MAK's concern on the impact of smoking on the health of the community, FS said that he had decided not to increase the duty on cigarettes because the current level of duty was already very high. Besides, the Administration did not wish to rely on increasing duty as a deterrent against smoking since this might intensify the problem associated with the sale of illicit cigarettes. To tackle the problem, the Administration had stepped up enforcement against the sale of illicit cigarettes. A package of measures, which included publicity and educational programmes as well as legislative control such as designation of more no-smoking areas, were introduced to deter smoking.

17. Dr LO Wing-lok did not agree that the increase in duty would intensify the problem associated with the sale of illicit cigarettes. He said that the sale of illicit cigarettes should be curbed through enhanced enforcement actions. Some statistics from other countries suggested that increases in duty on cigarettes were effective in deterring smoking, and he would be glad to share these statistics with the Administration. He supported that the duty on cigarettes be increased at the rate of 5% plus inflation.

### **Export of goods and services**

18. Mr Henry WU noted that the total exports of goods and services had benefited from the weakening of the US dollar. He expressed concern about the impact on the economy of Hong Kong in the event of strengthening of the US dollar. GE explained that while the US dollar trend was not predictable, it was expected

that Hong Kong could still benefit from the performance of the US dollar in the earlier part of the year, but the total export of goods for 2004-05 would be less than that for 2003-04. Notwithstanding, as the positive overall economic prospect, particularly that for the local economy, he was confident that the estimated growth of Gross Domestic Product (GDP) of 6% could be achieved for 2004-05. In response to Mr WU's further enquiry about the stamp duty for stocks transactions, FS said that the Administration had no intention to repeal the stamp duty for stocks transactions within the 2004-05 Budget, but would keep the revenue income under constant review.

### **Public expenditure**

19. Ms Emily LAU remarked that there had been general consensus that public expenditure should be kept at 20% of GDP. She failed to see why this should be reduced to 16.9% in 2008-09. FS explained that if the economic growth could meet the medium-range forecast, public expenditure would be down to 20% of GDP by 2006-07. Public expenditure as a percentage of GDP for 2008-09 would have to be reviewed every year in the light of the prevailing economy. With the revitalization in the economy and the increase in revenue, there was a possibility that a balanced budget could be restored earlier than expected.

20. Mr LEE Cheuk-yan expressed grave concern about the adverse impact of the proposed drastic funding cuts on the health, welfare and education aspects, which were closely linked to the underprivileged of the community. Given the vast reserve of the Exchange Fund, and the fact that the economy had experienced a V-shaped rebound, he queried why it was necessary to impose such drastic funding cuts. FS said that the Administration was committed to achieving fiscal balance and to maintaining a healthy budget for future generations. He stressed that funding cuts did not apply across the board and the needs of individual departments were taken into account in the allocation of funding. By way of illustration, the Hospital Authority (HA) was allowed to make up for the funding cuts by retaining part of the revenue generated from medical services to finance its operation. Funding for the Police and the Immigration Department had also been increased to cope with the additional workload arising from influx of visitors from the Mainland.

### Welfare

21. Referring to Government's commitment to invest in education and provide for the disadvantaged, Mr Fred LI pointed out that the increase in funding for the welfare sector was mainly attributed to the surge in provision for Comprehensive Social Security Assistance (CSSA). The welfare sector, including non-government welfare organizations, faced financial reduction. While these welfare organizations were prepared to accept funding cut of 2.5%, it appeared that the actual reduction was far more drastic, amounting to as much as 5% in some cases. FS explained that the 2004-05 Budget was formulated on a people-oriented approach aiming at

improving the livelihood of the community. He had met with Members of the Democratic Party as well as representatives of the welfare sector and had reached to a mutual understanding on the funding provisions for the welfare sector for 2004-05, details of which had been set out in the Budget. He appreciated the efforts made by the welfare organizations in serving the community and hoped that they could do more with less.

22. Referring to Mr LEUNG Fu-wah's enquiry about the assistance given to the disadvantaged. FS said that efforts would be made to promote the development of a tripartite social partnership comprising the Government, the business community and the welfare sector to encourage corporations to take part in helping the disadvantaged. In fact, under the "Caring Company" campaign launched by the Hong Kong Council of Social Service, business organizations had demonstrated their concern for the society in a number of ways, including the provision of outreaching services to the disadvantaged. Consideration was being given to introducing a matching grant scheme to encourage greater corporate participation.

23. While acknowledging that the Government would be investing \$200 million in setting up the tripartite social partnership, Ms Cyd HO noted that this would mainly target at the youth. She pointed out that with the aging population, there was a need for increased spending on welfare, particularly on the provisions for CSSA. FS said that one of the major difficulties in preparing the Budget was to achieve a balance of interest. The Administration was well aware of the needs of the aging population and was prepared to review the public expenditure based on a people-oriented approach taking into account changing circumstances.

### Health

24. Noting that HA was allowed to retain part of the revenue generated from medical services to finance its operation, Dr LO Wing-lok enquired about the basis upon which the decision was arrived at and its applicability to other public organizations. FS said that such an arrangement was worked out with the Secretary for Health, Welfare and Food so that HA could keep an agreed percentage of its revenue generated from medical services to finance its operation. The estimated amount of revenue which HA could deploy on top of the subvention amount was about \$1.5 billion. He added that this was a special arrangement applicable to HA only.

### Security

25. Mr Howard YOUNG also expressed concern on the reduction in recurrent expenditure for both the health and the security sectors in 2004-05. While funding cut in the health sector could be met by increase in fees, the reduction in the security sector might have impact on security control, particularly on cross-border immigration control. The Permanent Secretary for Financial Services and the Treasury (Treasury) explained that funding for the security sector had taken into



account the needs of individual departments under the Security Bureau. Although funding for the security sector had been reduced for 2004-05, funding for the Immigration Department had in fact been increased having regard to the need for more resources in dealing with the influx of visitors from the Mainland.

### **Promoting employment**

26. Miss CHOY So-yuk noted with concern the lack of concrete proposals for promoting employment and reviving the economy. She opined that the provision of \$200 million for promoting tripartite social partnership with the business sector should also apply to the promotion of social and environmental responsibilities. In reply, FS said that he was fully committed to the guiding principle of “market leads and government facilitates” in fostering economic development. The establishment of Mainland/Hong Kong Closer Economic Partnership Arrangement (CEPA) had brought about unprecedented opportunities to all sectors of the community and had enabled rapid recovery of the economy. Over \$150 million worth of tariff free goods had since been exported to the Mainland. Apart from CEPA, the Administration had also increased the quota under the Admission of Mainland Talents and Professional Scheme to facilitate the exchange of expertise between the two sides. There were also a number of proposals aiming at promoting employment and reviving the economy and a committee comprising LegCo Members, representatives from the trades and industries had been set up for the purpose. As regard environmental responsibilities, FS said that it might be more appropriate to hold discussions on the subject with the Secretary for the Environment, Transport and Works.

27. While agreeing to the need for respite, Miss CHAN Yuen-han held the view that the Administration had not made good use the opportunities offered by CEPA and the Individual Visit Scheme to promote employment. The setting up of a committee was far from enough to address the concerns of labour unions on the need to improve the present unemployment situation, which would be further aggravated if a large number of civil servants had been laid off. She was also concerned about the lack of minimum wage for workers of outsourced projects. FS took note of Miss CHAN’s views.

28. Mr LEUNG Fu-wah noted that the provision of \$1.2 billion for extending 11 000 temporary jobs was much less than that in 2003-04. He was also disappointed that only 105 out of the 2 000 youths employed as Tourism Development Assistants (TDAs) last year were offered extension of temporary employment despite their successful efforts in promoting tourism. He opined that the expenditure on tourism promotion and training activities was a worthwhile investment as this would not only create employment opportunities but also generate income for Hong Kong in the long run. FS said that the creation of a large number of temporary jobs in 2003-04 was meant to provide job opportunities for the unemployed following the outbreak of SARS. It had also equipped the

unemployed with the necessary skills to find alternative employment. With the improvement in economy, more employment opportunities were made available in the job market. As such, the Administration had to review the need for extending temporary jobs, bearing in mind that its role was to promote employment instead of creating jobs, which should be reliant on the private sector. The decision to invest \$1.2 billion to extend these jobs had been made after taking into account the operational needs of individual departments and after consultation with relevant parties. Further details on the job extension would be provided by the Secretary for Economic Development and Labour at the special FC meetings.

### **Article 107 of the Basic Law**

29. Ms Emily LAU said that she would support FS on the need to foster a business-friendly environment but more needed to be done in promoting fair competition. Referring to Article 107 of the Basic Law (BL 107) which stated that the Government should “keep the budget commensurate with the growth rate of its gross domestic product”, she enquired about how the Administration had interpreted this provision in preparing the Budget. As the expenditure targets of the Budget did not commensurate with the growth rates of GDP, she questioned if there was contravention of BL 107. FS said that under the Basic Law, the authority for interpretation rested with the Standing Committee of National People’s Congress (NPCSC). The Budget was worked out in accordance with prudent financial principles based on a people-oriented approach. Hong Kong had been suffering from negative growth in GDP over the past few years. Despite the cumulative deflation rate of 20%, operating expenditure had increased by 12%. In order to recover the 32% difference and in an attempt to balance the budget, there was a need for forward planning which would be kept under constant review in the light of changing circumstances.

30. While acknowledging that the authority to interpret the Basic Law rested with NPCSC, Ms Audrey EU opined that the Administration must have its own understanding on BL 107 in preparing the Budget since it was required to “follow the principle of keeping expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the budget commensurate with the growth rate of its gross domestic product”. She therefore asked how BL 107 was applied in preparing the Budget. FS said that he agreed to the principles set out in BL 107 and had prepared the Budget in accordance with the principle of keeping expenditure within the limits of revenues. However, it might not be possible to keep the budget commensurate with the growth rate of GDP at all times and some deviations would have to be allowed. The Chairman said that he would not allow any further deliberation on BL 107 as it was quite beyond the scope of discussion of the briefing.

31. The Chairman thanked FS and his colleagues for attending the meeting. He reminded members that the special FC meetings to examine the Estimates for Expenditure 2004-05 would be held from 29 March to 1 April 2004, and that the deadline for submitting questions on the Estimates was midnight of 17 March 2004.

32. The briefing ended at 1:05 pm.

Council Business Division 1  
Legislative Council Secretariat  
10 June 2004