Response to questions raised by Hon Sin Chung-kai on the Business Review of Hongkong Post Certification Authority (HKPCA)

1. Please provide the breakdown of HKPCA's annual revenue and operating expenditure. What are the five major expenditure items? What percentage of the total operating cost does the cost of systems and facilities maintenance constitute?

The main sources of revenue of HKPCA in 2004-05 are as follows:

	Items	Revenue (HK$ '000)	%
1.	Subscription fees for various types of e-Certs	4,953	52
2.	Fees for backup floppy disks issued to holders of e-Certs embedded in Smart ID Cards	4,418	46
3.	Other revenue, such as revenue from the sale of smart card readers and e-Cert-related products	218	2
	Total	**9,589**	**100**

The main expenditure items of HKPCA in 2004-05 are as follows:

	Items	Expenditure (HK$ '000)	%
1.	Staff cost	18,295[#]	74
2.	Systems and facilities maintenance	2,509	10
3.	General operational expenses	2,044	8
4.	Rental and management charges	1,341	5
5.	Audit, legal and insurance fees	627	3
	Total expenditure before depreciation is included	**24,816**	**100**

[#] $5 million of the staff cost is salary payment to staff working at the e-Cert service counters at the nine smart ID card centres.

2. **If HKPCA continues to provide e-Cert services until the services are contracted out to a private sector operator (e.g. in 2010-11), what will be HKPCA's estimated annual revenue, operating expenditure and other relevant investment required taking into account its annual revenue and expenditure in the past?**

If HKPCA continues its current mode of operation (i.e. without private sector participation), it is estimated that its annual operating expenditure (if depreciation is not included) and revenue will be about $25 million and $5 million respectively. Assuming that HKPCA will not launch any more promotional activities and will maintain only the most basic services, it is estimated that its annual operating expenditure (if depreciation is not included) will be at least $16 million and its annual revenue will be about $1.7 million.

We estimate that HKPCA's systems will remain in operation until 2010-11 and replacement will not be required before then.

3. **Did the Government look into ways to reduce HKPCA's annual operating expenditure, for example, by using IT facilities whose maintenance costs are lower? Please give details if the answer is in the affirmative; and explain why if the answer is negative.**

Hongkong Post (HKP) has already adopted various measures to reduce HKPCA's operating expenditure. These measures include:

- Strict control of expenditure – HKPCA's annual operating expenditure has been reduced by 14% from about $28 million in 2000-01 to about $24 million in 2004-05. The $24 million operating expenditure incurred in 2004-05 already covered the additional cost arising from the e-Cert embedded in smart identity (ID) card scheme launched in June 2003 (which includes the annual expenditure of $5 million for maintaining the e-Cert service counters at the nine smart ID card centres).

- Strict control of staff size – HKPCA has always kept the number of

staff at the minimum level required for meeting operational needs. It currently employs 83 staff, and about 60 of them are contract staff supporting the e-Cert service counters at the smart ID card centres.

- Contracting out – HKPCA has contracted out its work as appropriate (e.g. hotline enquiry service) in order to enhance cost effectiveness.

HKPCA is a recognized certification authority (CA) under the Electronic Transactions Ordinance (ETO) (Cap. 553). Accordingly, its systems, facilities and operational procedures have to meet the strict requirements of the ETO and the Code of Practice for Recognized CAs issued by the Government. The IT systems currently used by HKPCA were procured through open tendering in 1999 and 2002 respectively, and in making the procurements, HKPCA has struck a reasonable balance between meeting the technology and security requirements under the ETO and the Code of Practice and achieving cost effectiveness. Given that a complete replacement of HKPCA's IT systems will not be required before 2010-11, the Government would have to make additional investment to replace HKPCA's IT systems even if lower maintenance costs would be incurred. Hence, the proposal may not enhance the overall cost effectiveness of HKPCA.

4. **Regarding the Government's proposal to invite the private sector to run HKPCA's e-Cert operation:**

(a) **If the Government decides to let a private contractor run the e-Cert operation, will the Government provide any financial support to the private contractor? For example, will the Government be responsible for part of the operating expenditure or make any investment in the e-Cert services?**

Our ultimate goal in inviting the private sector to participate in running the e-Cert services is to engender a self-financing e-Cert operation. To this end, bidders may propose to offer new value-added services or e-commerce applications under separate brands, in addition to running the HKPCA operation, in order to generate income from other sources.

We are now drafting the conditions and detailed provisions of the Request for Proposal document, which will be announced early next year.

(b) **Has the Government assessed the implications of the proposal for the wider adoption of the e-Cert by the public in future? For example, will the operation of e-Cert services by the private sector affect the public's interest in using the e-Cert? Will the public have confidence in the private sector operator?**

Past experience indicates that the introduction of "killer applications" is key to the wide adoption of e-Cert by the public. When compared with HKP, a private sector operator should have greater flexibility in providing value-added services and e-commerce applications. We consider that private sector participation in the HKPCA operation should have positive impact on the promotion of e-Cert services and its utilization rate.

The Postmaster General (PMG) is a recognized CA under the ETO. Even if e-Cert services are run by a private sector operator, PMG will still be responsible for monitoring the performance of the contractor to ensure that HKPCA's standards of operation and security fully meet the Government's requirements. This is very important for maintaining users' confidence in the e-Cert.

The ETO provides for a voluntary recognition scheme to ensure the trustworthiness of recognized CAs and the digital certificates issued by them, and enhance public confidence in recognized CAs. There are at present two commercial recognized CAs in Hong Kong, and the digital certificates issued by them enjoy the same status as e-Certs. This shows that commercial recognized CAs are also capable of meeting the standards of operation and security set by the Government.

5. **Apart from the two proposals outlined in the paper (i.e. having the private sector operate the e-Cert services or terminating HKPCA's operation), will the Government consider other solutions to maintain HKPCA's e-Cert services?**

Apart from the above two proposals, the only way to maintain the e-Cert services is to continue to subsidize the operation of HKPCA using public funds (i.e. to provide an annual subsidy of at least $15 million). With two commercial recognized CAs operating in Hong Kong that are capable of issuing recognized digital certificates to both organizations and members of the public, it will be difficult for the Government to justify financing the HKPCA indefinitely. In view of the above, we hope to identify a suitable private sector operator to help operate the e-Cert services so as to engender a self-financing operation.

6. **If the Government decides to gradually wind down HKPCA's operation, what will be the focus of HKPCA's future operation? After the termination of HKPCA's operation, what initiatives will be launched by the Government to promote the use of the e-Cert and an environment where the importance of security of electronic transactions and information security will be recognized?**

In the event a suitable private sector operator cannot be identified and the HKPCA has to terminate its operation by end March 2008, HKPCA will stop issuing new e-Certs in or before the third quarter of 2007. During the 20-month transitional period from mid-2006 to end March 2008, HKPCA will assist the existing subscribers of e-Cert and its business partners to complete the necessary transitional arrangements. After March 2008, HKPCA will, in accordance with the requirements of the ETO and the Code of Practice issued by the Government Chief Information Officer (GCIO), submit a termination plan to GCIO. The termination plan will specify the arrangements for the termination of HKPCA's service, including the arrangement for its records to be archived for not less than seven years in order to protect the interests of persons concerned.

Even if HKPCA has to terminate its operation, it does not mean the Government will stop promoting the importance of information security and security of electronic transactions in the community. Indeed, the Office of the Government Chief Information Officer will continue to promote to different sectors the importance of information security and the application of digital certificates, as well as to explore in consultation with

Government departments and other sectors the development of digital certificate applications that can better meet the needs of the Government and the business sector.