OFFICIAL REPORT OF PROCEEDINGS

Wednesday, 22nd January 1975

The Council met at half past two o'clock

PRESENT

HIS EXCELLENCY THE GOVERNOR (*PRESIDENT*)
SIR CRAWFORD MURRAY MACLEHOSE, KCMG, MBE
THE HONOURABLE THE COLONIAL SECRETARY
MR DENYS TUDOR EMIL ROBERTS, CBE, QC, JP
THE HONOURABLE THE FINANCIAL SECRETARY
MR CHARLES PHILIP HADDON-CAVE, CMG, JP
THE HONOURABLE THE ATTORNEY GENERAL
MR JOHN WILLIAM DIXON HOBLEY, QC, JP
THE HONOURABLE THE SECRETARY FOR HOME AFFAIRS
MR DENIS CAMPBELL BRAY, JP
DR THE HONOURABLE GERALD HUGH CHOA, CBE, JP
DIRECTOR OF MEDICAL AND HEALTH SERVICES
THE HONOURABLE IAN MACDONALD LIGHTBODY, CMG, JP
SECRETARY FOR HOUSING
THE HONOURABLE DAVID HAROLD JORDAN, MBE, JP
DIRECTOR OF COMMERCE AND INDUSTRY
THE HONOURABLE LI FOOK-KOW, CMG, JP
SECRETARY FOR SOCIAL SERVICES
THE HONOURABLE DAVID AKERS-JONES, JP
SECRETARY FOR THE NEW TERRITORIES
THE HONOURABLE LEWIS MERVYN DAVIES, CMG, OBE, JP
SECRETARY FOR SECURITY
THE HONOURABLE DAVID WYLIE McDONALD, JP
DIRECTOR OF PUBLIC WORKS
THE HONOURABLE KENNETH WALLIS JOSEPH TOPLEY, JP
DIRECTOR OF EDUCATION
THE HONOURABLE IAN ROBERT PRICE, TD, JP
COMMISSIONER FOR LABOUR
DR THE HONOURABLE CHUNG SZE-YUEN, CBE, JP
THE HONOURABLE WILSON WANG TZE-SAM, OBE, JP
THE HONOURABLE LEE QUO-WEI, OBE, JP
THE HONOURABLE OSWALD VICTOR CHEUNG, OBE, QC, JP
THE HONOURABLE ROGERIO HYNDMAN LOBO, OBE, JP
THE HONOURABLE MRS CATHERINE JOYCE SYMONS, OBE, JP
THE HONOURABLE PETER GORDON WILLIAMS, OBE, JP
THE HONOURABLE JAMES WU MAN-HON, OBE, JP
THE HONOURABLE JOHN HENRY BREMRIDGE, JP
DR THE HONOURABLE HARRY FANG SIN-YANG, OBE, JP
THE HONOURABLE MRS KWAN KO SIU-WAH, MBE, JP
THE HONOURABLE LO TAK-SHING, JP
THE HONOURABLE FRANCIS YUAN-HAO TIEN, OBE, JP
THE HONOURABLE ALEX WU SHU-CHIH, OBE, JP

ABSENT

THE HONOURABLE JAMES JEAVONS ROBSON, CBE, JP
SECRETARY FOR THE ENVIRONMENT
THE HONOURABLE LI FOOK-WO, OBE, JP

IN ATTENDAN

THE CLERK TO THE LEGISLATIVE COUNCIL
MR KENNETH HARRY WHEELER

Affirmation

MR Alex WU made the Affirmation of Allegiance and assumed his seat as a Member of the Council.

HIS EXCELLENCY THE PRESIDENT: —I would like to welcome Mr WU to this Council.

Papers

The following papers were laid pursuant to Standing Order 14(2): —

	Subject	*LN No*
Subsidiary Legislation:		
Miscellaneous Licences Ordinance.		
	Miscellaneous Licences (Amendment) Regulations 1975	2
Summary Offences Ordinance.		
	Summary Offences Ordinance (Exemption from Section 13) Order 1975	3
Road Traffic (Parking and Waiting) Regulations.		
	Road Traffic (Temporary Car Park) Regulations	8
Buildings Ordinance.		
	Building (Construction) Regulations 1975	9
Buildings Ordinance.		
	Building (Administration) (Amendment) Regulations 1975	10

Subject *LN No*

Buildings Ordinance.
Building (Escalators) (Amendment) Regulations 1975 11

Buildings Ordinance.
Building (Lifts) (Amendment) Regulations 1975 12

Buildings Ordinance.
Building (Planning) (Amendment) Regulations 1975 13

Public Health and Urban Services Ordinance.
Cremation and Gardens of Remembrance (New Territories) Regulations 1975 14

Merchant Shipping Ordinance.
Merchant Shipping (Hong Kong - Macau Ferry Terminals) (Amendment) Regulations 1975 15

Prisons Ordinance.
Pik Uk Prison Order 1975 16

Public Health and Urban Services (Amendment) Ordinance 1974.
Public Health and Urban Services (Amendment) Ordinance 1974 (Commencement) Notice 1975 17

Summary Offences Ordinance.
Summary Offences Ordinance (Exemption from section 13) Order 1975—Corrigendum 18

Sessional Papers 1974-75:

No 26—Annual Report of the Accountant General with the Accounts of Hong Kong 1973-74 (published on 22.1.75).

No 27—Report and Certificate on the Accounts of the Hong Kong Government for the year ended 31st March 1974 (published on 22.1.75).

No 28—Despatch dated 15th January 1975 to the Secretary of State on the Report by the Director of Audit for the year ended 31st March 1974 (published on 22.1.75).

Report:

First Annual Report of the Criminal and Law Enforcement Injuries Compensation Boards ended 31st March 1974 (published on 22.1.75).

Oral answers to questions

Clerical Assistant promotion examinations

1. MR WANG asked: —

Sir, what is the reason for the delay in the announcement of the results of the promotion examinations for clerical assistants taken in June 1974?

THE COLONIAL SECRETARY: —Sir, for some time it has been the practice, towards the end of each year, to announce the list of those clerical assistants who had succeeded as a result of the annual examination in gaining entry to the rank of clerical officer.

In November 1974, however, a joint committee of official and staff members was established to study the structure of the Clerical Class.

Until this committee has reported and the Government has reached a conclusion on its report, it will not be known how many clerical officer vacancies are available to be filled.

Hong Kong funds overseas

2. MR LOBO asked: —

Sir, (*a*) will Government state whether any Hong Kong funds are currently being managed by the Crown Agents;

(*b*) if so, what is the total involved?

THE FINANCIAL SECRETARY: —The answer to the first part of my honourable Friend's question, Sir, is: yes. But I am not able to provide a direct answer to the second part of the question because to do so would be a breach of customary commercial confidentiality.

However, honourable Members will be interested to know that, whereas in December 1971 all of our overseas funds and assets were deposited with or held by the Crown Agents, today they are only one of ten institutions which we employ as depositories and custodians for

our overseas funds and assets amounting at current market values to the equivalent of rather more than US$1,000 million. I should perhaps add that the ten institutions with whom we now have accounts include three central banks.

My honourable Friend's question, Sir, may have been prompted by doubts about the safety of the funds deposited with the Crown Agents. On this score, I do not think I can do better than repeat part of the statement made by the Minister for Overseas Development in the House of Commons on the 18th December 1974. The Minister said, in describing the financial arrangements which had been made to assist the Crown Agents:

> "These arrangements will demonstrate beyond all doubt that the Government stands behind the Crown Agents so that the position of all depositors is fully safeguarded."

I shall circulate, Sir, a copy of the Minister's statement so that honourable Members may read it in full.

Of course, to the extent that the Crown Agents act in a custodial and management role for part of our securities portfolio, their own financial position is not relevant I might add, in this connection, that this Government has no complaints about the way in which the Crown Agents have, over the years, carried out our instructions relating to the management of this portfolio. The bulk of our securities portfolio is owned by the Exchange Fund of course and as honourable Members are aware the investment policies pursued by the fund are formulated by the Financial Secretary in consultation with the Exchange Fund Advisory Committee.

Localization in the Government Service

3. MR WANG asked: —

> Sir, what steps are being taken to accelerate the pace of localization in the Government Service, in particular for the more senior administrative appointments?

THE COLONIAL SECRETARY: —Sir, Government policy on localization, which is set out in Chapter VI of the 1973 Report on the Civil Service is, briefly, to recruit overseas only when suitable and qualified local candidates are not available.

Overseas officers are normally recruited on contract terms and may transfer to permanent terms only if it is apparent that a local candidate

is unlikely to become available to replace the overseas officer in the reasonably foreseeable future. Only in the Administrative Class and the Police Inspectorate is there a regular intake of a proportion of overseas officers.

Most senior posts are filled by promotion from within the service. All qualified candidates are considered for promotion on equal terms. The number and proportion of local officers appointed to the directorate and equivalent levels has increased steadily, and on the 1st January of this year, out of 471 officers at this level, 118 were local officers.

Triad influence in schools

4. MISS KO asked: —

Sir, (*a*) does Government agree that there is an increasingly serious influence of triad societies in schools;

(*b*) if so, what instructions or assistance will Government give to schools to help tackle the problem?

MR TOPLEY: —Sir, there is no evidence of increasing triad influence in schools; nor is there any evidence of planned infiltration. I have made this assessment in close consultation with the Commissioner of Police.

Last year only eight reports from schools complaining of suspected triad activities were received by the police. In addition, of the total of 1,618 people under 21 years of age arrested for triad offences in 1974, only 120 were students. When compared with the one million children in the 12-21 age group, the percentage is very small indeed.

As indicated by my colleague, the Secretary for Security, on 14th August last year, in most of those cases investigated by the police it was established that the students had joined triad societies, or groups professing to be triads, in the neighbourhood where they live and outside school hours.

My department has advised schools to be on the alert at all times and to contact the police direct if they receive any reports of triad activities in their schools. Separately, the police have arranged and held meetings with headmasters.

In response to the "Fight Violent Crime" Campaign my department produced a special ETV programme, issued teaching materials, and assisted schools in organizing exhibitions, forums and talks including advice on combating triad activites. Moreover, a "reaching out" scheme of school social work has been initiated by the Social Welfare and Education departments to help schools solve their pupils' behaviour problems.

In short, although there is no evidence of increasing triad activity in schools, the Government is concerned about any reported attempt by triads to infiltrate schools. The Police Force and the Education Department are keeping a vigilant eye on this problem.

Compensation for properties frozen by town planning

5. MR LO asked: —

When will Government decide either to pay for or defrost the properties located in the urban renewal and urban improvement districts which have been frozen by town planning decisions?

THE COLONIAL SECRETARY: —Sir, the earlier decision to implement the Urban Improvement Schemes (including that for the Urban Renewal District in Western) was confirmed by Executive Council in September last. A revised estimate of the cost of acquisition of private property affected by these schemes and the necessary financial provision were approved by Finance Committee shortly thereafter. Since then, negotiations have been taking place with owners and agreement an acquisition terms has been reached in many cases.

However, in view of the financial constraints to which we are likely to be subject in the next year, the Government is having to consider ways of reducing the effects of these schemes on private property in those areas. Proposals will probably be submitted to Executive Council in the near future.

MR LO: —Sir, may I ask whether the Government has a more accurate assessment of the time it will take to decide than probably in the very near future?

THE COLONIAL SECRETARY: —I don't think we can expect to do it more quickly than in the very near future.

Oral answers

Work permits for engineering students

6. MR James WU asked: —

> Sir, has any progress been made on a scheme, to be operated by the Hong Kong Government Office in London, where by individual engineering students from Hong Kong are assisted in obtaining temporary work permits so that they can receive pay during training in Britain?

SECRETARY FOR SOCIAL SERVICES: —Sir, there are three main channels through which a Hong Kong engineering student can obtain a temporary work permit in order to receive practical training in the United Kingdom.

Firstly, he can make his own arrangements in getting a place with a firm. In this connection, the heads of departments of the Hong Kong Polytechnic usually assist their students and correspond direct with firms in the United Kingdom.

Secondly, he can obtain a place in a polytechnic or a university in the United Kingdom on either a sandwich or full-time course. These institutions apply for blanket approval to enable all their students to have practical employment experience, and work permits are granted almost automatically.

Thirdly, he can seek assistance from the Overseas Students Advisory Bureau through the Hong Kong Government Office in London.

But it is becoming increasingly difficult to find places for practical training for those who are not attending a college or a university in the United Kingdom, because there are usually more students wanting practical training than there are vacancies offered by firms. Most large firms give some training to their own employees and many allocate higher priority to requests from their overseas subsidiaries, associates and important customers. Naturally, firms benefit only indirectly from training anyone who is not an employee of theirs or likely to become one. Consequently, individual firms in the United Kingdom vary in their reaction to applications from students for training and they are not necessarily treating students unfairly if they do not support their individual applications for work permits. A degree of reluctance on their part in the present world economic circumstances is indeed understandable.

Sir, the Hong Kong Government Office in London already gives a great deal of valuable help to our students and all those intending to seek training in the United Kingdom are strongly advised to register with the office through the Education Department here before leaving Hong Kong.

But, I think it would not be unfair to say that it is preferable for students to receive their practical training in Hong Kong, where they will be employed when qualified. I appreciate that there may be areas in which practical training is not yet available locally, and I have therefore asked the Hong Kong Training Council to advise Government upon the problems relating to the practical training of technologists locally. The Council has set up an *ad hoc* committee to look into the availability of this type of training in Hong Kong, and I understand that my honourable Friend Mr James WU is among its distinguished membership. I look forward to the early receipt of their advice, as we cannot expect the United Kingdom to provide all the practical on-the-job training which our industrial expansion increasingly requires. We must be prepared to find the bulk of this ourselves.

Code of aid for schools

7. MRS SYMONS asked: —

> Sir, will Government indicate when the proposed code of aid for subsidized primary schools will be ready?

MR TOPLEY: —Sir, the proposed code of aid for primary schools has been prepared and a Finance Committee agenda item is now being drafted.

Telephone rentals—application for increase

8. MR CHEUNG asked: —

> Sir, will Government
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> (*a*) inform Council what increase in telephone rentals are sought by the Hong Kong Telephone Company, and
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> (*b*) state, without prejudice to Government's position, the reasons and facts advanced by the company for seeking such increases?

Oral answers

THE FINANCIAL SECRETARY: —Yes, Sir, but I am able, in fact, to state the Government's attitude towards the company's application for increases in certain of its scheduled charges. I propose also with your permission, Sir, to describe the measures which we think should be taken immediately and what arrangements we think should be put in hand to consider longer term measures.

On 27th August last the Telephone Company applied for the following increases in charges with effect from 1st January 1975: —

Annual residential line rental from $280 to $480, that is an increase of $200 or 71%;

Annual business line rental from $410 to $700, that is an increase of $290 or 71%;

Exchange line installation fee from $125 to $220, that is an increase of $95 or 76%.

The company, Sir, gave three reasons for seeking these increases. First, that world-wide inflation, together with high interest charges on borrowed capital and greatly increased operating costs, was having a serious effect on the company's cash flow and future profitability. Secondly, that there had been a fall off in demand for telephone services which had reduced budgeted income. And, thirdly, that the company had to remain a viable operation showing an adequate return on employed capital and a degree of profitability so that it could continue to raise new capital when conditions were suitable and, in the meantime, to raise funds in the offshore loan capital market.

The company's application was the subject of detailed examination by officials and was referred to the Advisory Committee on Telephone Services for advice. The Advisory Committee established that the Telephone Company is facing a chronic cash shortfall due to the large capital expansion programme it has embarked upon in recent years and interest costs on past borrowings, together with a considerable slowing down in 1974 in the demand for new telephone lines. In other words, the company has spent more than it has earned. The company's net cash shortfall in 1974 was estimated to be about $160 million and this is estimated to rise to about $250 million in 1975 if charges are not increased. The Advisory Committee expressed great concern at this situation and the Government is equally concerned. But I am afraid that the comment must be made that no public company which plays an essential role in the life of the community, as does the Telephone Company, should have permitted such a situation to arise.

The Advisory Committee's investigations have established that additional loans to meet such cash shortfalls cannot be raised and that, if the financing had to be met by increased charges, it would be necessary for annual business and residential line rentals to be increased respectively to $624 (or by 52%) and $420 (or by 50%) and increases made to many of the other charges, though some decreases were also proposed largely to establish a more rational system of charges. But, even if such increases were to be implemented from 1st March this year, the Advisory Committee estimated that a net cash shortfall of about $100 million would still have accrued this year. So the Company would not be viable even with the implementation of these increases. In other words, the Committee's view, based on the evidence before them, was that these increases are the minimum necessary just to keep the company going, that is to say, to enable the company to finance its recurrent outgoings and debt service charges.

The situation revealed by the Advisory Committee's report indicates a failure of the management and the Board of the Company in the past properly to monitor its financial position and to draw appropriate conclusions for future planning. These conclusions might—and I stress might—might have involved a much earlier review of charges than that undertaken in 1973, in order to generate surplus funds to finance capital expenditure and thereby make it feasible for the equity market to be approached. Instead, the company has tended to drift into a situation where it has a high loan gearing. Furthermore, the report points to the fact that even an examination as careful as that the Advisory Committee has been able to carry out in the time available to it, is not comprehensive enough to reveal the whole position of the company and to make recommendations for future corrective action. For instance, the Committee's examination has concentrated almost exclusively on the company's general financial and technical position and this has been most thorough. The Committee was not able, however, to probe in any detail into other aspects of the company's management and, in particular, the general question of the form future public control over its operations as a public utility might take. Furthermore, the Government is conscious of the fact that public opinion is naturally disquieted at the prospect of substantially higher telephone charges at a time of growing economic difficulty coming, as they will do, only a year or so after the company was granted increases of 17% in business line rentals and 19% in residential line rentals.

The Government believes, therefore, that enough is not yet known about these aspects of the company's affairs to enable a comprehensive and definitive assessment to be made of the level of charges that will be

[THE FINANCIAL SECRETARY] **Oral answers**

needed in the future if the company is to remain viable. But it recognizes that the position revealed by the Advisory Committee's report is such that to refuse any increases in charges at this time would precipitate a crisis in the company's affairs which would simply not be in the public interest.

In these circumstances, the Government has decided that the company's application for an increase in telephone rental and installation charges of about 70% from 1st January 1975 is not acceptable. Instead, the Government is prepared to seek this Council's approval on 5th February next for increased charges from 1st March 1975 of' about 30% for business and residential lines and party lines. Thus the new rental charges would be $528 for business lines, $360 for residential lines, $396 for business party lines and $276 for residential party lines. The increases in various other charges proposed by the Advisory Committee and which are listed in the paper already distributed to honourable Members, are acceptable to the Government and I hope will commend themselves to honourable Members.

I might add that all these increases, on their own, will not be enough to keep the company's head above water and undoubtedly extended bank credits will be necessary and I have reason to believe that the Company's bankers are prepared to arrange these. But it will be necessary, in addition, for the Company's Board to recommend to shareholders that no dividend payments should be made in 1975 in respect of 1974 and by way of an interim dividend for 1974 amounting on present indications to about $48 million in all. Quite apart from the financial reasons for this, it is the Government's view that the shareholders should bear some of the consequences of the company's past failure in management. As an indication of the Government's interest in the affairs of an essential public utility company, the company's consent is also being sought to the appointment of a Government director to the Board of the Company. Finally, if the Company agrees to the increased charges immediately proposed and to the other two proposals relating to dividends and a Government director, the Government will introduce a bill into this Council on 5th February next to waive royalty payable by the Company under section 5 of the Telephone Ordinance in respect of the years 1974 and 1975. This will benefit the cash flow to the extent of about $12 million.

It may be asked why a 30% increase in telephone rentals. The answer is that the effect of this level of increase on the company's finances, together with the waiver of royalty and no dividend payments

in 1975, would roughly equate to a 50% increase in telephone rentals, as proposed by the Advisory Committee. As I have already said, Sir, with the 50% increase the cash shortfall in 1975 would be about $100 million. With a 30% increase in rentals and no dividend and royalty payments, the cash shortfall should be not very different and, in fact, a little less (just under $90 million).

I would stress, Sir, that these are all interim measures and represent the Government's response to the urgent and difficult situation faced by the Company and public alike. But on the information available the Government is not in a position to suggest long term solutions to the problem of the company's financial situation or of its relationship with the Government and hence to the public interest. Before this can be done there is also a need to examine further the organization and structure of the Telephone Company and its future policies for the expansion of its services, together with the implications for its finances, including the future level of rentals, so as to give the public some assurance that it will not be faced with a recurrence of this sort of crisis situation in future. Clearly, the report of the Advisory Committee will be a point of departure for such an examination. It is proposed that this examination shall be undertaken by a Commission of Inquiry set up under the Commissions of Inquiry Ordinance. The terms of reference of the Commission have yet to be worked out, but they would include an examination of the company's present management structure and future plans, its debt liabilities and its profitability. The Commission would also be asked to recommend whether and, if so, when further increases in rentals would be necessary to secure the permanent viability of the Company, while being able to make recommendations on amendments which might be made to the Telephone Ordinance to ensure adequate public control over the future operations of the company as a public utility, including of course the establishment of a development fund. I would not presume to anticipate how such a development fund would be operated with the Telephone Company, but the concept itself is clear enough: it would be credited with profits in excess of a fair rate of return to the Company and would be used to help finance necessary capital expansion.

MR CHEUNG: —Sir, are the interim increases of about 30% about to be recommended to this Council the absolute minimum which would keep the company operating viably until the Commission of Inquiry reports?

Oral answers

THE FINANCIAL SECRETARY: —Yes, Sir, I can confirm that. And I think I have adequately demonstrated the point in the reply I have just given to my honourable Friend's question.

MR LO: —Sir, does the Government at this stage have any idea at all how it is possible for a public utility company which reported at its annual general meeting in April 1974 that it had reasonable prospects for the future with no mention of any cash flow problems, suddenly to find itself going insolvent only four months later?

THE FINANCIAL SECRETARY: —The Government is not able, Sir, to give a satisfactory answer to that question and it is for that reason that you, Sir, have decided that a Commission of Inquiry should be appointed.

MR BREMRIDGE: —In framing the terms of reference of the Commission of Inquiry, will Government request the Commission to inquire into alternative methods of increasing the company's cash flow, for example, by requiring subscribers to purchase instead of renting equipment?

THE FINANCIAL SECRETARY: —We have no intention, Sir, of limiting the scope of the Commission of Inquiry.

MR JAMES WU: —Does Government consider that the various interim measures as proposed by the Financial Secretary to be the best that can be devised for the time being?

THE FINANCIAL SECRETARY: —Yes, Sir.

Government business

Motions

CROSS-HARBOUR TUNNEL ORDINANCE

THE FINANCIAL SECRETARY moved the following motion: —

> That the Cross-Harbour Tunnel (Amendment) By-laws 1975, made by the Cross-Harbour Tunnel Company Limited on the 2nd December 1974, be approved.

He said: —Sir, under section 62(2) of the Cross-Harbour Tunnel Ordinance all by-laws made by the Cross-Harbour Tunnel Company are subject to the approval by resolution of this Council. The Cross-Harbour Tunnel Company has amended its by-laws to provide for a fee of $50 to be paid for the issue of a permit for the use of the tunnel by extra large vehicles or for vehicles with extra large loads. The issue of a permit entails administrative work and the provision of a special escort service. The proposed fee will recover the cost.

Question put and agreed to.

RATING ORDINANCE

THE FINANCIAL SECRETARY moved the following motion: —

That, for every tenement in a specified area set out in the first column of the Schedule, the general and Urban Council rates shall be computed on the basis of the percentage of the rateable value of such tenement set out opposite such area in the second and third columns of the Schedule.

SCHEDULE

Specified Area	*General Rates*	*Urban Council Rates*
A	9%	6%
B	9%	6%
C	9%	6%
D	15%	Nil
E from 1st April 1978	15%	Nil
until 31st March 1978	11%	Nil

He said: —Sir, the present percentage rate charges are contained in sections 18 and 19 of the Rating Ordinance. These sections are repealed by section 4 of the Rating (Amendment) Ordinance 1975 and are replaced by a new section 18 which lays down that new percentage rate charges shall be determined by resolution of this Council.

As section 4 of the ordinance will come into operation on 24th January 1975, this resolution seeks to reinstate the current percentage rate charges on the same day.

Question put and agreed to.

FACTORIES AND INDUSTRIAL UNDERTAKING ORDINANCE

MR PRICE moved the following motion: —

> That the Factories and Industrial Undertakings (Cargo Handling) Regulations 1975, made by the Commissioner for Labour on the 2nd January 1975, be approved.

He said: —Sir, I move the motion standing in my name on the Order Paper for the approval of the Factories and Industrial Undertakings (Cargo Handling) Regulations 1975.

On 4th July 1973, my predecessor informed honourable Members that the Factories and Industrial Undertakings (Amendment) Bill 1973 was designed to clear the way for safety regulations in respect of construction work and cargo handling. He added that the increasing use of modern devices and sophisticated techniques for cargo handling, including containerization, had brought with it new safety problems requiring specialized treatment.

The regulations now before Council are designed to cover the handling of cargo to, or from, docks, quays and wharves, and will complement the Factories and Industrial Undertakings (Lifting Appliances and Lifting Gear) Regulations 1974 which came into effect on 1st November 1974 and which, by virtue of the definition of industrial undertaking in section 2 of the principal ordinance, cover also shore based lifting equipment used for the handling of cargo.

Part I of the regulations contains definitions, and states that the regulations shall come into operation on a day to be appointed by the Commissioner for Labour by notice in the *Gazette*. To give proprietors an adequate period of notice within which to comply with these new requirements, I propose to bring them into force from 1st April 1975.

Part II of the regulations sets out safety requirements and provides for safe access to, and efficient lighting of, docks, quays and wharves as well as facilities for rescue from drowning. It also provides for the proper maintenance, protection and use of electrical equipment and portable electrical equipment which must be inspected once a day by a competent person who is appointed in writing for that purpose by the proprietor, and who by reason of his training and practical experience is competent to perform the inspection. The definition of competent person in regulation 6(3) is analagous to that used in the Construction Sites (Safety) Regulations and in the Lifting Appliances and Lifting Gear Regulations.

Part II further provides for the maintenance and use of fork-lift trucks, the safe stacking or unstacking of cargo or goods, and prohibits the unauthorized removal of safety appliances or fencing.

Part Ⅲ deals with first aid facilities. Its provisions, with appropriate modifications, are similar to those contained in the Construction Sites (Safety) Regulations 1973. It is necessary to include first aid facilities in these regulations now before Council because, while cargo handling at docks, quays and wharves is an industrial undertaking, such activities do not fall within the definition of registrable workplaces under section 9 of the principal ordinance. Therefore the First Aid in Registrable Workplaces Regulations will not cover cargo handling.

Part IV contains miscellaneous provisions for the exhibition of notices and for penalties.

The proposed regulations received the unanimous approval of the Labour Advisory Board on 30th May 1974. The four major employers' associations were then consulted in July. One sought, and received, certain clarifications, and all have signified their full support.

New legislation now being prepared by the Marine Department will cover the seaward side of cargo handling, namely the loading, unloading or transfer, of cargo using cranes or other lifting gear on ships or lighters.

Question put and agreed to.

First reading of bill

EMPLOYMENT (AMENDMENT) BILL 1975

Bill read the first time and ordered to be set down for second reading pursuant to Standing Order 41(3).

Second reading of bills

EMPLOYMENT (AMENDMENT) BILL 1975

MR PRICE moved the second reading of: —"A bill to amend the Employment Ordinance."

He said: —Sir, a contract of employment may be terminated under the Employment Ordinance by the giving of notice of termination as required by section 6, or by an agreement to pay a sum of wages in lieu of notice in accordance with the provisions of section 7.

[MR PRICE] **Employment (Amendment) Bill—second reading**

Until very recently it was thought that where a contract of employment is wrongfully terminated by either party to it—that is to say terminated otherwise than in accordance with the provisions I have just mentioned—a liquidated sum, that is a fixed or ascertained amount, equal to wages in lieu of notice was payable to the other party.

However, the Full Court has recently held that this is not the case under the law as worded at present, and that the remedy available is the ordinary common law action for unliquidated damages for breach of contract. Unliquidated damages cannot be predetermined because factors other than mere loss of wages arising from a breach of contract have to be taken into consideration. Such damages have to be proved in each case.

This was not the intention of the law. Therefore, clause 2 of the bill provides for a new section 8A which will restore the position to that which it was thought to be—namely a right of action for liquidated damages for wages in lieu of notice.

Clause 3 makes a minor change in the wording of section 25 of the principal ordinance.

Motion made. That the debate on the second reading of the bill be adjourned—MR PRICE.

Question put and agreed to.

INLAND REVENUE (AMENDMENT) (NO 3) BILL 1974

Resumption of debate on second reading (27th November 1974)

Question proposed.

DR CHUNG: —Your Excellency, my honourable Friend Mr Q. W. LEE who is supposed to speak during the resumed debate on this particular bill today has suddenly lost his voice and has asked me to speak on his behalf. May I have your permission to do so, Sir? Since his speech is written in Chinese, I shall therefore deliver his speech in the Cantonese dialect.

(Address delivered in the Cantonese dialect. The following is the interpretation of what Dr CHUNG said.)

Sir, the main object of the Inland Revenue (Amendment) (No 3) Bill 1974 is to change the method of computing profits for tax from a preceding year basis to a current year basis.

When the bill was published it attracted much adverse comment from the public. Most people feared that the proposals would result in taxpayers having to pay more tax or having to pay tax in advance. Some quite naturally felt that this was not a time to bring in any such changes in the present economic atmosphere.

These criticisms were based on a misunderstanding of the effects of the bill, in spite of the clear and careful explanation by the honourable Financial Secretary when he actually introduced the bill. Here I must say his explanations have been ably followed up by senior officers of the Inland Revenue Department in TV and press interviews as well as conferences with interested bodies and some of the fears of the public successfully cleared.

I think these comments are hardly surprising in view of the technical complexity of the bill. This is borne out by the fact that the Unofficial Members had to meet no fewer than eight times to consider and discuss the bill in the light of all the representations that had been made, whether to the Government, to UMELCO or in the press. Following these lengthy deliberations, and after having taken careful note of all the representations made, the Unofficials have reached the conclusion that this bill is a beneficial and necessary change in the tax law, the main principle of which we support.

As the bill involves such an important change in taxation law and its actual provisions are so complex, and as the Government has agreed to the suggestions of the Unofficial Members to amend some of the provisions of the bill since it was published, I should like to explain what its effects will now be. To do this I would like first to say something about the existing system and its weaknesses; then about how the new system will be applied and the effect on taxpayers.

How the existing system works

At present profits tax is assessed for each year of assessment based on profits of the preceding year. On commencement of a business, the profit of the first year is used as the basis for the first two years of assessment in order to get onto the preceding year method of calculation. But for both the second and third years of assessment, the taxpayer may ask for a revision of the assessment based on the actual profits for those two years, if this is more beneficial to him.

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Thereafter the business pays tax every year on profits made in the preceding year.

On cessation of that business the profit of either the penultimate year or the year before that is dropped out from assessment. The drop-out is a compensating benefit for the double use of the first year's profit. But the right is with the revenue to assess the higher profit. It follows, therefore, that the smaller profit of those two years would be dropped out.

If the profits of a business from commencement to cessation were evenly made every year, the commencement and cessation provisions of the existing system would have no effect either on the taxpayer or the revenue. However, reality is such that this is never the case, because business operations are subject to so many factors that profit and loss inevitably vary. And this gives rise to a few weaknesses in the existing system as well as to the possibility of tax avoidance upon cessation. In view of the urgent need for revenue to finance the greatly increased social services, the closure of this gap may help to stave off other forms of new or increased taxation. I hope, therefore, that all responsible citizens will conclude, as the Unofficials have done, that this aspect of the bill should be supported.

The weaknesses of the existing system

The weaknesses of the existing system may be categorized as follows.

Firstly, that tax is not directly related to profits earned. If the profits of a business are greater in the commencement years and less in cessation years, over the years the taxpayer has to pay more total tax because the greater profit in the commencement year is assessed to tax twice and this is not compensated by the drop-out of a smaller profit upon cessation. However, if the profits in the drop-out years on cessation are greater than those in the commencement years the situation is just the reverse because more benefit is obtained from the drop-out of a more profitable year upon cessation. Thus different patterns of profit or loss result in some taxpayers having to pay more tax in relation to the total profits earned over the life of their business and some less. In other words, under the existing system profits assessed to tax do not bear an exact relationship to profits actually earned. It is as fundamentally wrong for taxpayers to pay more tax as it is for them to pay less in relation to actual profits.

Secondly, the cessation provisions provide an opportunity for avoidance of tax. As the cessation provisions entitle the taxpayer to have a year's profit dropped out it is possible to avoid tax by simply timing a suitable cessation date so that one of the profitable years would fall out of assessment. Substantial revenue has thus been lost because of taxpayers deliberately taking advantage of the cessation provisions. As I have already mentioned the change in the law will remove this loophole.

Thirdly, there is the inconsistency with other taxes. All other direct taxes such as interest tax, property tax and salaries tax are now assessed on the current year basis. Profits tax is the only exception. This means that for purposes of personal assessment it is necessary to group together different incomes, some on the current year basis and some on the preceding year basis. This is clearly inconsistent as well as illogical.

Haw the proposed new system will work

By changing to the current year basis it will be possible to eliminate these weaknesses. Profits tax for a year of assessment will be based on the profits actually earned in that year or as shown by the accounts closed in that year. There will be no artificial use of one year's profits for two years of assessment; hence, profits assessed will be in an exact relationship with the profits earned. The taxpayer will be required to pay tax on no more and no less than what he has actually earned in a year.

Transitional adjustment

To change over it is necessary to have some transitional adjustments in the transitional year of 1974-75 both for profits and for initial allowances for capital expenditure.

First on the profits: because one year’s profit was assessed twice upon commencement, so, to compensate the taxpayer, a year's profit must be dropped out on the change-over to the current year basis. And to preserve the rights to which the revenue is already entitled the bill provides that the smaller profit years of 1973-74 or 1974-75 will be dropped out, in line with the existing cessation provisions.

It is difficult to quantity the consequences to the taxpayers and to the revenue as a result of this. Generally speaking, if profits are steady, there will be no adverse effect on the taxpayer or the revenue. If profits are falling, it pays for the taxpayer to have one year's profit dropped out now rather than in later years. Conversely, if profits are

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on a rising trend right up to cessation, then the taxpayer will be at a disadvantage because the profit dropped out now would be less than the profits in the later years. However, as normally a business will cease only when profits decline or losses are incurred, it is likely that any profits now dropped out under the transitional adjustment would in most cases be greater than those excluded from assessment under the existing cessation provisions. The exception is where there is the deliberate tax avoidance under the existing system that I have already mentioned. This is what the bill seeks to bring to an end and I am sure the public would like this Council to do so in the interest of protecting the revenue.

It has been suggested that instead of the complicated transitional adjustments it would be simpler to assess only either 1973-74 or 1974-75 but this is not practical because without such adjustment, businesses coming into profitability or exceptional profitability in the two years of 1973-74 or 1974-75 would escape assessment on a very profitable year, Obviously this is not desirable.

I will discuss initial allowance for capital expenditure later in this speech.

Provisional tax

After the transitional year tax will be paid on the current year basis. But because the actual result of a year may not be known until the end of that year, to wait for it would mean to defer the collection of tax into the next year. Therefore, in order to preserve the pay-as-you-go principle a provisional tax based on the preceding year profits is to be paid on account. When the actual results of the year are known an adjustment up or down will be made. As such adjustment will be made in the following year, a part of the tax will always be in arrears where profits are in an upward trend. The provisional tax is in fact a payment of tax on account of the current year of assessment and is not an advance payment for the following year of assessment. There should be no cash flow problem for the taxpayer. For instance, the provisional tax for 1975-76 will be payable sometime in late 1975 or early 1976 when: —

all of the profits will already have been earned if accounts are closed between April and December; and

most of the profit will already have been earned if accounts are closed between January and March.

It has been suggested that provisional tax should be based on an estimate of the profit by the taxpayer instead of on the profit of the preceding year, with an adjustment to actual result when it is known. This amounts to a form of self-assessment. Obviously such a system could lend itself to abuse unless adequate penalties were provided to guard against deliberate under-estimates of profits by taxpayers. Undoubtedly this will be even more complicated and the Unofficials believe therefore that the system of provisional tax as proposed in the bill, with provision to stand-over where required, is more appropriate.

Stand-over provision

Under the provisional tax system there is a "stand-over" provision to give relief to those whose profits are smaller in the current than in the preceding year. The bill provides that, if the current year profit is less than 80% of the preceding year's profit, an application may be made to the Commissioner for the whole or part of the provisional tax to be held over. The Unofficials feel that this requirement may operate unreasonably against some taxpayers because a margin of 20% is too wide to qualify or disqualify them from applying for stand-over. I am glad to say that Government has agreed to substitute 90% for 80%. This means that taxpayers will only have to pay the full amount of provisional tax when the current year's profits are or are likely to be not less than 90% of the preceding year's profits; otherwise they can apply for stand-over of provisional tax in whole or in part.

I might mention here that, under the existing system, even if a loss is incurred in a year of assessment, the tax assessed nevertheless has to be paid on the preceding year's profit. In order to claim a refund of the tax overpaid, the loss has to be agreed before it may be set off against profits in the next assessment. This means waiting for a year or so, as the accounts of the year in which the loss is incurred are required to substantiate the loss. By comparison the stand-over provision under the new system gives quicker and so better relief to the cash flow problem of a business in a situation of declining profits and it is precisely in such a situation that this problem is most pronounced and the relief most needed.

Effects of new system on taxpayers

Having explained the workings of the new system, I shall attempt to show the effects on the taxpayer.

In January 1975 the taxpayer will pay tax for 1974-75 based on the 1973-74 profit. This is payable whether or not the system is changed.

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If the actual profits in 1974-75 are greater than those in 1973-74 then, in January 1976, under the transitional adjustment, final tax for 1974-75 will be payable on the excess. At the same time the taxpayer will be called on to pay provisional tax for 1975-76 based on the profit of the preceding year *i.e.* 1974-75. The number of taxpayers paying final tax as a result of the transitional adjustment should be comparatively small in view of the fact that 1974-75 is a lean year for most business. If 1974-75 profit is in fact smaller than that of 1973-74, the only payment in January 1976 will be the provisional tax for 1975-76 based on, as I have just mentioned, the profit of 1974-75.

In January of every following year, a similar process will be repeated: that is, if profits are on a rising trend, payment of final tax on the excess of the actual profit over the preceding year profit plus a provisional tax for the current year. If profits are on a downward trend, no final tax will be payable for the preceding year. Any provisional tax overpaid for that preceding year will be deducted from the provisional tax for the current year which may of course be held over if circumstances justify.

If a loss is made in 1974-75, it will be set-off against the original assessed profit for that assessment year. A refund of tax overpaid will be made in January 1976 with the balance of loss not yet set-off being carried forward. Because of the loss, no provisional tax for 1975-76 will be payable. It will be observed that, despite the transitional adjustment, the loss incurred in 1974-75 will not be dropped out.

Acceptability and implementation time of the bill

I hope it is now clear that while the bill eliminates the weaknesses of the existing system, it will not work to the disadvantage of taxpayers in that: —

(*a*) the amount of provisional tax will still relate to the preceding year's profit with adjustments for excess or small shortfall to be made in the following assessment, and

(*b*) the time of payment will still be the same as under the existing system.

It does not seek to impose any additional burden on the taxpayers or to require them to pay in advance.

As to the timing of the bill in the present slackened economy, this should have no effect on the taxpayers at all because, accepting that 1973-74 was generally a better year than 1974-75 and that tax on the 1973-74 profits has to be paid anyway at present by about January 1975, the first payment of provisional tax will be in January 1976 and on the smaller 1974-75 profit. The public may therefore rest assured that the bill will work equitably both to the taxpayer and the revenue. Provided that each business makes provision for tax based on the actual profit earned, and sets aside funds as any prudent manager will do, no hardship should ever exist in meeting the tax payments.

Proposed amendments

But, as in any legislation, there is some room for improvement. I have already mentioned the Government's agreement that, in the provision for stand-over of provisional tax, the percentage should be raised from 80 to 90.

Initial allowances for capital expenditure

On initial allowances for capital expenditure, clause 28 at present provides that the allowances will not be available for capital expenditure incurred in the year dropped out of assessment under the transitional adjustment. This would cause hardship to some taxpayers because the tax benefits might have been taken into account in capital expenditure decisions in 1973 and 1974 without any prior knowledge or notice of the bill. On the other hand, there are clearly no grounds for granting initial allowances on two years' expenditure against one year's assessable profit. I am glad to say that Government has agreed to grant initial allowance for the higher expenditure of the transitional years, irrespective of whichever year's profit is dropped out. Later the honourable Financial Secretary will explain how the initial allowance will be granted on the amended basis.

Procedure for stand-over of provisional tax

It has been represented that the bill as drafted gives the Commissioner unfettered discretion to accept or to refuse an application for stand-over. Suggestions have therefore been made that the bill should stipulate the circumstances in which a stand-over must be granted or provide for an objection or appeal in a case where the need for stand-over is in dispute.

After careful consideration, the Unofficials decided not to pursue the issue because, so far as a right of appeal is concerned, it was felt

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that there would be inadequate time for the appeal body to convene and deliver its decision before the due date for payment of tax. Since a notice of appeal would have to carry with it an automatic deferral pending the outcome of the appeal it would be possible for any taxpayer to avoid paying on time simply by lodging an appeal, thereby frustrating the purpose of the new system. Again, it was evident that any attempt to specify conditions for mandatory stand-over would necessitate spelling out very stringent conditions if abuse is to be avoided. This could have the opposite effect to that intended because if a genuine case should exist to which the Commissioner was inclined to give sympathetic consideration he would nevertheless have to refuse to stand-over the tax if the conditions were not fully met because his hands would be tied by law. This could work to the disadvantage of the taxpayer.

As, however, this is considered to be a matter of prime importance, the Unofficials have asked the Financial Secretary to give an assurance in this Council that a stand-over of provisional tax will not be unreasonably withheld. I understand that my honourable Friend is prepared to give this assurance.

Problems of taxpayers closing accounts between January and March

On cash flow problems, it is considered that taxpayers whose accounts are closed between January and March may experience some difficulties if they are required to pay provisional tax on the usual due dates in early January. This is because by that time the year's profit will not have been fully earned. Further, if in fact a smaller profit is earned in the current year, it will not be possible to quantify it in time to support an application for stand-over.

I am glad that Government is very sympathetic to this problem and proposes a change in the administrative procedure so that taxpayers in these cases will be allowed to pay the provisional tax in two instalments. The honourable Financial Secretary will explain the workings of this change in administrative procedure, but I would like to make a point: that this change is made despite a slower cash flow to the revenue proves the Government's intention of introducing a system that will not place the taxpayers at a disadvantage.

Finally, if I may say so, Sir, the handling of this bill is an excellent example of how this Council can and does do its job for the good of the community as a whole. The consultation machinery between Government and the people has again proved its worth. When the

bill was published, it caused great misgivings. The Unofficials were pleased that Government agreed to a lapse of nine weeks for the resumption of the debate so that they could examine the bill in the light of representations made against it. We have, as I have said, had eight meetings. In a matter that has caused as much public concern as this, we accept our responsibility to satisfy ourselves that the legislation proposed is sound and fair to all concerned. We came to the conclusion that generally speaking it was but that there were some particular aspects that could be improved. To deal with these we made representations to the Financial Secretary. He in his turn has, as I have mentioned, accepted most of our proposals and given notice that he will propose the amendments we seek at the committee stage. On another point he has answered us fully and convincingly and has also undertaken to give in this Council the public assurance that we have asked for.

The Unofficials are satisfied that with the changes on these important points, the bill is a good one; that the new system it embodies is an improvement on the old system, not just from the revenue point of view, but also from the taxpayers'. I am authorized by my colleagues to say that we all support it.

MR BREMRIDGE: —Sir, I also support this seemingly but not actually inopportune new bill, which rightly seeks to set company taxation on the same tax basis as individual salaries, property, and interest. While the principle is simple, the presentation is not.

As a result of this bill company taxation itself is not increased, but the payment of taxation at the proper level is ensured and accelerated. What Government thus is seeking to do is what all businessmen in Hong Kong and elsewhere attempt now more than ever; that is to cut down the time that money due is out with creditors. As a businessman, aware equally of the problems of big and small businesses, I understand Government's motives, though in common with my fellows I tend to deplore them when they are applied to me rather than purely to others. (*Laughter*.)

There seems indeed to be a growing tendency in Hong Kong to consider Government as a malign force to be resisted at all costs. When this thought occurs to me, as indeed it does with some frequency (*laughter*), to be fair I replace the word "Government" with the word "community"; and then the arguments often look very different. This does not mean that we should receive all Government bills with equanimity. We certainly do not. Moreover I fully accept that the view

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from a small factory in Kwun Tong may not be the same as that from this Chamber; though as a Member of this Council I do try to take into account all points of opinion. And so do we all. I still firmly believe that the backbone of Hong Kong is its trade and business, and particularly those interests engaged in export. If they do not flourish, nor does Hong Kong. We have no other resources. It is therefore *prima facie* dangerous to interfere with established taxation practice which may affect the level of investment both domestic and from overseas. But Hong Kong itself is a community of interests, and while therefore I am sad to see anything which makes the lot of trade and industry more difficult, as this bill may to some small extent do, I am at the same time fully aware of the need for greater expenditure on selected social measures, *i.e.* better schools, better housing, better medical facilities. There are others. The money must come from somewhere—even in the present difficult circumstances given the ruthless pruning of all non-essential projects, and, I hope, of civil service recruitment. My Friend the honourable Financial Secretary is engaged in a delicate balancing act in these trying times, and all of us should support him where we properly can. This must surely include an expression of our distaste when he is personally attacked for reasons charitably describable as inane, and uncharitably as seeking personal publicity at all costs.

I am therefore myself persuaded that the balanced interests of the community are served by this bill taken as a whole.

That is not to say that I find all its provisions attractive. I am personally disappointed, after hours of work in Committee ably and unsparingly led by my honourable Friend Mr Q. W. LEE, that we were not able to persuade Government in particular to change further their approach to the transitional arrangement for initial allowances. Speaking simply the effect of the new legislation is that in one of the two financial years 1973-74 or 1974-75 initial and annual allowances win not be granted by Government against capital expenditure. If, for example, capital expenditure of HK$10 million, does not attract these allowances for the year 1974-75, the effect will be that a company's cash flow in that year will come down by HK$544,000. This will in theory represent no tax increase because the money will be recovered by greater annual allowances in subsequent years. I say in theory because in practice this is not the case. With a simple approach it will take until 1991 to recover. With a discount of 20% to allow for the price of money and its certain depreciation, it will never come back in full.

This is almost disguised additional taxation, though I acknowledge that it is hard to find an absolutely fair solution to the transitional problem of initial allowances and that the Government has gone someway to meeting our objections.

No company meriting initial allowances can avoid this outcome, and all previous plans for future investment are involved. It is moreover retroactive legislation, which always is to be deplored. Apart from other companies, major utilities including perhaps the Telephone Company may expect to have an annual expenditure on capital investment in excess of HK$100 million. This new bill will worsen their cash flow in the one year by over Hk$5 million.

Why then should I support the bill? The answer is that Government needs the revenue from taxation as early as possible and I cannot accept in all fairness that company and individual taxation should not be placed on the same footing. I believe that the total amount involved on my particular point of loss of one year's initial allowances is of the order of HK$75 million, and that failing further compromise this Council has to decide whether this is better left for the time being in the hands of industrialists, or placed more quickly in the hands of Government, because if industry thus suffers an adverse cash flow it must be mirrored by an equivalent credit in Government's hands. In the circumstances of Hong Kong as they exist today I believe after much argument that this outcome is in the community's interests, though it is not in the interests of industrial companies who have long been encouraged by initial allowances to invest in capital equipment in order to provide more work for their employees (and need I say of course more profit for themselves as well).

Subject to these views I thus support the motion.

THE FINANCIAL SECRETARY: —Sir, I am most grateful to honourable Members and particularly, of course, my honourable Friend Mr Q. W. LEE and his *ad hoc* group, for the care with which they have examined the provisions of this bill. And I am sure this Council and the public at large will find my honourable Friend's accurate exposition of how these provisions will operate in practice helpful and more reassuring, apparently, than my own attempt in this Council some weeks ago. I am sorry that at the end of the day my honourable Friend was unable himself to deliver the main speech on behalf of Unofficial Members, but very ably indeed was presented by the Senior Unofficial Member.

Needless to say, the purpose of each and every piece of legislation submitted by the Government for consideration by this Council is to protect and further the public interest. And so I would like to give my

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honourable Friend Mr BREMRIDGE this reassurance (and I think it is a very necessary reassurance): in the fiscal field it is not our policy—and I really do think our record is quite clear on this—it is not our policy to initiate changes for their own sake or regardless of their effects on commerce and industry. But we must be responsive to changing circumstances and I believe this bill constitutes a very necessary degree of reform and rationalization. Furthermore, when new legislation comes forward we readily admit there is always, or nearly always, room for legitimate doubt and discussion over points of substance and detail. Time consuming though this consultative process has been in this case, I am very glad that, as a result of the *ad hoc* group's examination of the bill and the many verbal and written exchanges with myself and my colleagues in the Inland Revenue Department, Unofficial Members now feel able to support this motion.

As a result of these exchanges I shall be moving several amendments at the committee stage and I shall explain the technical reasons for them at that time.

In winding up the debate on this motion, Sir, I need dwell only on five points. To begin with my honourable Friend Mr Q. W. LEE's request that I re-state the general effect of the new system of calculating assessable profits for profits tax purposes. I can do this in exactly the same words as I used in my speech moving the second reading: "as from the year of assessment commencing 1st April 1975 businesses will be finally taxed for each year of assessment on their actual profits earned for that year of assessment. So, in future, their tax liability will always have an exact relationship with their actual profits earned, both in the short term and over the life of a business." And I further said: "for all businesses the new system will mean that, from the year of assessment commencing on 1st April 1975, their tax liability will be no more and no less than the standard rate of tax applied to their actual profits. The erratic effects of the present commencement and cessation provisions will no longer be there."

Turning to the second point I wish to mention: I detect, Sir, that my honourable Friend Mr BREMRIDGE has at least a lingering doubt about the operation of clause 28 concerning initial allowance. As originally drafted, clause 28 provided that, for the purpose of initial allowance, capital expenditure incurred in the drop-out year (1973-74 or 1974-75) would also drop out. Quite apart from the logic of the situation, I am afraid that revenue considerations simply do not

permit the granting of initial allowance on more than one year's expenditure in one year's assessment. However, it has been represented to me that capital expenditure incurred by a business in the drop-out year could exceed that incurred in the accounting year taken as the basis period for the computation of assessable profits and that, in such a situation, it would be unfair to deny the business initial allowance on the higher expenditure. Thus, Sir, I shall be moving at the committee stage an amendment to provide

(*a*) that, where transitional adjustment applies and 1974-75 is the year of higher profits, then initial allowance will be granted on the higher of the capital expenditure in 1974-75 or 1973-74 which would be the drop-out year; and

(*b*) that, where transitional adjustment does not apply and 1974-75 is the drop-out year, then the higher of the capital expenditure in 1974-75 or 1975-76 will be taken for the purposes of initial allowance for the year of assessment 1975-76.

But revenue considerations do not permit initial allowance also to be granted in the following year of assessment on the lower capital expenditure which has been ignored for initial allowance; and it should be remembered that it will only be ignored because initial allowance is to be granted on the higher of the capital expenditure incurred in 1973-74 compared with 1974-75, or in 1974-75 compared with 1975-76. Given that, in addition, a full annual allowance will be granted on expenditure not qualifying for initial allowance there should, in fact, be no cash problem. On the contrary, the allowances granted against one year's profits in the transitional year will be somewhat higher than they would be under the present system. To sum up then: there can be initial allowance only on one year's capital expenditure allowed against one year's profits. But such expenditure will qualify in full for annual allowance in the year of assessment 1974-75 where transitional adjustment applies and in 1975-76 where it does not.

The third point I wish to make concerns the more generous criterion now proposed for stand-over of provisional tax, namely, 90% rather than 80% of the preceding year's assessable profits. I feel obliged to make it clear that, Sir, if there is abuse, we may have to consider the introduction of penalties. If this sounds harsh and bureaucratic, I can only remind honourable Members and the press and the public at large of their oft-stated wish to see the Inland Revenue Ordinance administered as efficiently as possible to improve its productivity and thus obviate the necessity to raise tax rates. With this objective I am wholly in sympathy, for I firmly believe in our traditional dependence on a low rate of profits tax and high yields flowing from a

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fast growth rate of the economy which, in turn, depends on a high rate of internally financed investment. In fairness to salaries taxpayers, I shall be proposing at the committee stage that section 63E(2)(*b*) of the ordinance should also be amended to provide for stand-over if net chargeable income is likely to be less than 90% rather than 80% of net chargeable income in the previous year.

My fourth point concerns the procedure for stand-over of provisional tax. I am certainly prepared to give the undertaking sought by my honourable Friend Mr Q. W. LEE: stand-over will not be "unreasonably withheld", but I would ask all concerned to remember that the Commissioner of Inland Revenue has certain obligations to the revenue and hence to the public interest. And so inevitably, his attitude must depend in part on his actual experience with individual taxpayers.

Finally, Sir, there is the difficult question of payment of their tax liabilities by businesses closing their accounts between January and March. In a period of reasonably buoyant trade the fact that these liabilities have to be discharged one to two and a half months before the end of the year of account cannot really be onerous—and let us not forget the level of our standard rate. However, I do not wish to argue against the logic of the proposition that a business should not have to discharge its tax liability in full before the end of its year of account and so, as a matter of administrative practice under section 72, the Commissioner of Inland Revenue will accept payment in two instalments: the first of 75% on the normal due date and the second approximately three months later. Again, in fairness to salaries taxpayers the same facility will have to apply to them. If all taxpayers are of a mind to take advantage of this facility the once-over cost to the revenue in 1975-76 will be some $280 million. I propose to finance this shortfall by temporarily drawing down the reserves and I stress temporarily. There will be a recurring loss of some interest on our balances and a permanent re-scheduling of our cash flow (but this latter effect is not in fact entirely unwelcome).

Question put and agreed to.

Bill read the second time.

Bill committed to a committee of the whole Council pursuant to Standing Order 43(1).

EXCHANGE FUND (AMENDMENT) BILL 1975

Resumption of debate on second reading (8th January 1975)

Question proposed.

Question put and agreed to.

Bill read the second time.

Bill committed to a committee of the whole Council pursuant to Standing Order 43(1).

ACETYLATING SUBSTANCES (CONTROL) BILL 1975

Resumption of debate on second reading (8th January 1975)

Question proposed.

Question put and agreed to.

Bill read the second time.

Bill committed to a committee of the whole Council pursuant to Standing Order 43(1).

LANDLORD AND TENANT (CONSOLIDATION) (AMENDMENT) (NO 2) BILL 1975

Resumption of debate on second reading (8th January 1975)

Question proposed.

Question put and agreed to.

Bill read the second time.

Bill committed to a committee of the whole Council pursuant to Standing Order 43(1).

CHILD CARE CENTRES BILL 1974

Resumption of debate on second reading (27th November 1974)

Question proposed.

Child Care Centres Bill—resumption of debate on second reading (27.11.74)

MR WANG: —Sir, before I begin to speak on this motion, I must confess that I am concious of the fact that I may appear to be playing to the gallery, being as I am in the presence of those two members whose authority on this subject matter is unchallengeable by virtue of their own personal experience. Though I am personally well-blessed with good fortunes of my own, I have been denied the opportunity to enjoy such experience. Fortunately or unfortunately, when the opportunity might have been present, my wife had not been introduced to Women's lib. I will therefore be brief, and allow honourable Members to bear with our two experts on the subject later.

Let me say at the outset that this bill should not suggest any area of controversy, though we did find some difficulty in determining what constitutes a child care centre. What does this term embrace? We did not wish to leave any doubt about the area in which control is sought; for wherever young children are involved the word "care" is surely the operative word. Unless the term is clearly defined it could lead to circumstances where some children would in fact be left uncared for—while those who might well do the caring stand aside—failing to act for fear of being prosecuted.

However, I think we have contributed some improvement on this point of definition, and I am prepared therefore to support this bill with the amendments which my honourable Friend the Secretary for Social Services has said that he will propose when the committee stage is reached.

Strictly speaking, the regulations, perhaps less so the code of practice that will accompany this bill, are not part of this bill. But the whole prospect of the achievement of this bill depends entirely upon the standards set by these regulations with which all registered operators are required to comply. We must of course be sure that a minimum standard should be set to ensure the health, welfare and safety of young children. Equally so, we must bear in mind that too high a standard may not necessarily be a good thing. If too high a standard makes the cost of such service prohibitive to those parents who are in genuine need of child care services, the result could be an absence of care, and that surely would not be in their interest or that of the innocent children.

Sir, we were at first rather reluctant to allow the passage of this bill through this Council without close scrutiny of the regulations and the code of practice, and we have in fact spent some time on this

exercise. But we need further time because of the importance of these regulations, and partly because some standards which are set are in need of evidence to support their necessity, and such evidence is not available to us at this moment.

To complete the exercise would cause further delay of the enactment of this bill, which delay none of us would wish to cause. However, we have been assured that a thorough examination of the regulations will occur, and that these will not be enacted until after full consultations have been made.

In view of these assurances, I am happy to support the motion.

MRS SYMONS: —Sir, it is with considerable pleasure and subdued gratitude that I welcome the Child Care Centres Bill 1974. Ever since the summer of 1972 I have waited for such legislation to provide, in time, minimum standards to be followed by all child care centres.

There will undoubtedly be critics who will deplore the timing of such legislation, just as there will be operators who will irresponsibly increase their charges using the bill as an excuse.

I submit, however, that when parents understand the reasons for the code of practice and the bill they will accept it in the spirit of its existence—the safety and welfare of very young children.

The flexibility and realism of the bill in allowing the Director of Social Welfare discretion in the implementation of its provisions must not be allowed to degenerate into mere procrastination by the operators of child care centres. The recruitment and training of staff must also be accelerated to make the bill workable.

I have twice asked Government to use mass media to achieve a better understanding of this problem of the care of young children in child care centres, and it is my hope that this aspect of the education of the general public will not be forgotten. Many well-educated young women I know, think nothing of leaving their babies in residential nurseries explaining in mitigation "but we are allowed to see them every day if we want". Few understand as Dr C. E. FIELD and Dr F. M. BABER have indicated in their detailed study of Hong Kong babies that children can suffer from maternal deprivation; and that other babies in the survey "were inhibited and excessively slow in performance tests, and retarded in some psychomotor milestones". Only last month when I questioned a young mother who had left her baby in a creche she replied—"Under six months a baby does not know anything".

[MRS SYMONS] **Child Care Centres Bill—resumption of debate on second reading (27.11.74)**

With the partial break-up of the traditional pattern of Chinese family life, this bill is sorely needed and must like the subjects of its ambit be nursed along with imagination and care.

Sir, I support the motion.

MISS KO: —Sir, the Child Care Centres Bill, which is designed to control and regulate the operation of child care centres, should be welcomed as necessary and timely. The bill is a significant step forward in establishing a system of registration, control and inspection over the operation of child care centres. It will be supported by regulations laying down realistic and practical standards of staff responsibilities and qualifications, structural requirements, fire precautions, health and sanitation.

As I mentioned before, it has been true for some time that some small, badly-run child care centres operating on a purely commercial basis, have proliferated. Instances of neglect or abuse have occurred in some of these centres in recent years and the conditions in others are detrimental to the children's health and safety; therefore the lack of legislative control has become one of our concerns. In view of the need for properly-run nurseries—1,000 places yearly as stated in the Social Welfare Five Year Plan—proper guidance in this field has become more important, especially regarding children's safety and care.

There is a danger, however, that the number of places in the commercial centres would decline as a result of legislative provisions being so restrictive as to force many operators out of business. I am glad that my honourable Friend, Mr F. K. LI, has mentioned that not only have certain minimum requirements been stipulated and offences prescribed to eliminate the worst abuses, but also, the bill allows the Director of Social Welfare discretion in enforcing this legislation by waiving the requirements of any regulation in any particular case. I hope that in order to help operators of child care centres to meet the required standards over some years, the Director of Social Welfare will exercise his authority to waive certain requirements temporarily at the beginning stage.

In this bill, it is obvious that Government has taken into account the difficulties facing those who wish to operate child care centres but who fear they cannot cope with the financial burden or other problems of such a venture. I hope that the requirements of this legislation and the phased implementation will not be an unbearable burden for them.

One important aspect regarding the implementation of the bill will be the need to recruit more trained staff members to carry on the work of inspection and provision of guidance to child care centres, especially at the beginning stage of the implementation.

It is also desirable that the regulations which will be made under this bill will be reviewed or revised if necessary from time to time in order to cope with the changing needs.

Sir, with these words, I support the motion.

SECRETARY FOR SOCIAL SERVICES: —Sir, I am grateful for the comments of my honourable Friends on this bill. It has had a long history and it is therefore particularly satisfying to me that it has at last the opportunity of being put on our statute books as a basis for the better regulation of child care centres and, I trust, the more efficient care of the children received into them.

My honourable Friend, Miss KO Siu-wah has emphasized the importance of having trained officers to administer the provisions of this bill and the regulations made under it. I am fully aware of the burden of work and responsibility which will be placed on the staff especially during the first three years of implementation when they will be called upon to advise on many matters with which their clients are unfamiliar. I assure my honourable Friends that the ordinance shall not come into operation until I am satisfied that there is sufficient staff available to guide the supervisors of these centres towards the proposed improvements.

My honourable Friend, Mrs Joyce SYMONS, has raised the important point of parental responsibility. I do not wish to dictate to parents on how to bring up their children and I fully understand the economic pressures to which they are subjected to in improving their life in order to bring to their families a better standard of living within this competitive society. However, I agree that in the search for more prosperity parents should not lightly regard residential centres as merely a substitute for the home environment and I agree that parents should not try to absolve themselves of the responsibility for looking after their own children.

I am similarly aware of the need to ensure that children are cared for and not merely parked in these centres and I hope that the regulations governing the day to day administration and maintenance of the child care centres and the words of guidance in the code of practice will ensure that this care is practised and is effective.

[SECRETARY FOR SOCIAL SERVICES] **Child Care Centres Bill—resumption of debate on second reading (27.11.74)**

I therefore assure honourable Members that the regulations and the Code of Practice will not be implemented without further informal consultations with those honourable Members who have a particular interest in this legislation before submitting the regulations to Your Excellency in Council for approval. Finally, I am most grateful for the support of my honourable Friends for this bill.

Question put and agreed to.

Bill read the second time.

Bill committed to a committee of the whole Council pursuant to Standing Order 43(1).

Committee stage of bills

Council went into committee.

INLAND REVENUE (AMENDMENT) (NO 3) BILL 1974

Clause 1

THE FINANCIAL SECRETARY: —Sir, I move that clause 1 be amended as set out in the paper before honourable Members.

Sir, this amendment simply recognizes that the original timing envisaged for enactment of this bill was over optimistic.

Proposed amendment

Clause

1 That clause 1(1) be amended by deleting "(No. 3) Ordinance 1974" and substituting the following—

"Ordinance 1975".

The amendment was agreed to.

Clause 1, as amended, was agreed to.

Clauses 2 to 15 were agreed to.

Clause 16

THE FINANCIAL SECRETARY: —Sir, I move that clause 16 be amended as set out in the paper before honourable Members.

Clause 16 is amended by the addition of a sub-paragraph to make it clear that losses incurred by a business after 1st April 1975 are to be available for relief by way of set-off only to the extent that they are losses attributable to activities in the Colony. This amendment does not introduce any new concept, but simply follows section 19 of the main ordinance.

Proposed Amendments

Clause

16 That clause 16 be amended in the proposed new section 19C(6)—

(*a*) by deleting the full stop at the end of paragraph (*c*) and substituting a semicolon; and

(*b*) by inserting, after paragraph (*c*), the following new paragraph

"(*d*) the amount of any loss to be set off under this section shall be the loss attributable to activities in the Colony.".

The amendments were agreed to.

Clause 16, as amended, was agreed to.

Clauses 17 to 27 were agreed to.

Clause 28

THE FINANCIAL SECRETARY: —Sir, I move that clause 28 be amended as set out in the paper before honourable Members.

This amendment implements the concession which honourable Members have urged upon me in relation to the granting of initial allowance on capital expenditure incurred during the year 1973-74, 1974-75 and 1975-76 and which I have already explained.

Proposed amendments

Clause

28 That clause 28 be deleted and there be substituted the following new clause—

Inland Revenue (Amendment) (No 3) Bill—committee stage

"Addition of new section 40A.

28. The principal Ordinance is amended by adding, after section 40, the following new section—

"Initial allowances in years of assessment 1974-75 to 1975-76.

40A. (1) Where—

(*a*) the assessable profits of a person for the year of assessment commencing on the 1st April 1974 are computed under section 18A; and

(*b*) there is an interval between the end of the basis period for the year of assessment ending on the 31st March 1974 and the beginning of the basis period for the year of assessment ending on the 31st March 1975, then, notwithstanding paragraph (*b*) of the definition of "basis period" in section 40(1), but subject to subsection (3) the initial allowance on capital expenditure provided under this Part shall be made only on the higher of the capital expenditure incurred in the interval or the second basis period referred to paragraph (*b*) of this subsection.

(2) Where—

(*a*) the assessable profits of a person for the year of assessment commencing on the 1st April 1974 have been computed under section 18; and

(*b*) there is an interval between the end of the basis period for the year of assessment ending on the 31st March 1975 and the beginning of the basis period for the year of assessment ending on the 31st March 1976,

then, notwithstanding paragraph (*b*) of the definition of "basis period" in section 40(1), but subject to subsection (3), the initial allowance on capital expenditure provided under this Part shall, in respect of the year of assessment commencing on the 1st April 1975, be made only

on the higher of the capital expenditure incurred in the interval or in the second basis period referred to in paragraph (*b*) of this subsection.

(3) Where the amount of capital expenditure incurred in the interval and the second basis period referred to in subsection (1)(*b*) or in subsection (2)(*b*) is the same, the initial allowance shall be made only in respect of the capital expenditure incurred in the second basis period.".".

The amendments were agreed to.

Clause 28, as amended, was agreed to.

Clauses 29 to 37 were agreed to.

Clause 38

THE FINANCIAL SECRETARY: —Sir, I move that clause 38 be amended as set out in the paper before honourable Members.

This redrafted clause deals with two quite separate points. First, the clause as originally drafted introduced an additional ground on which salaries taxpayers may apply to the Commissioner for stand-over of provisional salaries tax, namely, that the taxpayer has objected to his assessment to salaries tax for the preceding year—the year upon which his provisional salaries tax will have been based. However, I have been advised that clause 38 as originally drafted would not permit the Commissioner to require payment of the tax stood-over until the time for payment of final tax for the year, notwithstanding that there had been an earlier determination or settlement of the objection. The new clause 38 makes it clear that where provisional salaries tax has been stood-over on the ground of an objection to the assessment for the preceding year, stand-over will only apply until determination or settlement of the objection or until the taxpayer is required to pay his final tax for the year of assessment, whichever is the sooner. Secondly, having regard to the concession I mentioned in my speech winding up the debate on the second reading regarding the criterion for stand-over of provisional profits tax, it would be inequitable if a similar concession were not made to salaries taxpayers and this clause now contains, therefore, a consequential amendment to section 63E(2)(*b*) of the main ordinance substituting the figure of 90% for 80% for the purposes of applications for stand-over of provisional salaries tax.

Inland Revenue (Amendment) (No 3) Bill—committee stage

Proposed amendments

Clause

38 That clause 38 be deleted and there be substituted the following—

"Amendment of section 63E.

38. Section 63E of the principal Ordinance is amended—

(*a*) in subsection (1) by inserting, after "that year of assessment", the following—

"or, in the case of an application on the ground set out in subsection (2)(*d*), until—

(*a*) the determination of the objection or settlement thereof under section 64(3);

(*b*) he is required to pay salaries tax for that year of assessment,

whichever is the sooner"; and

(*b*) in subsection (2)—

(i) in paragraph (*b*) by deleting "eighty *per cent*" and substituting the following—

"ninety *per cent*";

(ii) by deleting the full stop at the end of paragraph (*c*) and substituting the following—

"; or"; and

(iii) by inserting, after paragraph (*c*), the following new paragraph—

"(*d*) that the person assessed to provisional salaries tax has objected under section 64 to his assessment to salaries tax for the year preceding the year of assessment.".".

The amendments were agreed to.

Clause 38, as amended, was agreed to.

Clause 39 was agreed to.

Clause 40

THE FINANCIAL SECRETARY: —Sir, I move that clause 40 be amended as set out in the paper before honourable Members.

This clause has been amended in a similar way to clause 38 (which is in respect of provisional salaries tax) and again the purpose of the amendment is to make it clear that where the reason for stand-over of provisional profits tax has been that the assessable profits for the preceding year are under objection the tax stood-over will become payable when the objection is determined or settled or when the final tax for the year of assessment is payable whichever is the sooner.

This clause is also amended to increase the figure of 80% to 90% to enable applications for stand-over to be made where actual profits are, or are likely to be 90%, or less than 90% of those for the previous year.

Proposed amendments

Clause

40 That clause 40 be amended in the proposed new section 63J—

(*a*) in proposed subsection (1) by inserting, after "that year of assessment", the following—

"or, in the case of an application on the ground set out in subsection (2)(*e*), until—

(*a*) the determination of the objection or settlement thereof under section 64(3); or

(*b*) he is required to pay profits tax for that year of assessment,

whichever is the sooner"; and

(*b*) in proposed subsection (2)(*a*) by deleting "eighty *per cent*" and substituting the following—

"ninety per cent".

The amendments were agreed to.

Clause 40, as amended, was agreed to.

Clauses 41 to 43 were agreed to.

Clause 44

THE FINANCIAL SECRETARY: —Sir, I move that clause 44 be amended as set out in the paper before honourable Members.

[THE FINANCIAL SECRETARY] **Inland Revenue (Amendment) (No 3) Bill—committee stage**

Clause 44 of the bill provides that, in all cases, provisional profits tax for the year of assessment 1975-76 is to be calculated by reference to the amount of profits which would have been the assessable profits for that year under the old method of computation, that is to say, the profits of 1974-75. The purpose of the clause is to ensure that provisional profits tax for 1975-76 is calculated in all cases in the same way as will be provisional profits tax in the ensuing post-transition years, namely, by reference to the profits of the preceding year. Without clause 44 provisional profits tax would have to be calculated by reference to the higher 1973-74 profits in those cases where section 18A transitional adjustment does not apply and this would operate to the disadvantage of the taxpayer. However, I have been advised that clause 44, as originally drafted, may not permit the set-off of losses brought forward from the pre-transition years. It was certainly not the intention to deny the availability of such losses and, accordingly, clause 44 has been amended to place the matter beyond doubt.

Proposed amendment

Clause

44 That clause 44 be amended by inserting, after "in respect of that year", the following—

“, but after the set off of any loss available for set off in that year of assessment under section 19 of the principal Ordinance".

The amendment was agreed to.

Clause 44, as amended, was agreed to.

EXCHANGE FUND (AMENDMENT) BILL 1975

Clauses 1 and 2 were agreed to.

ACETYLATING SUBSTANCES (CONTROL) BILL 1975

Clauses 1 to 11 were agreed to.

Clause 12

THE ATTORNEY GENERAL: —Sir, I move the amendments set out in the paper.

They correct a drafting error and also enable searches to be made for evidence as well as for acetylating substances.

Proposed amendments

12 That clause 12 be amended—

(*a*) in subclause (1), by deleting "any acetylating substance which is", wherever it occurs in paragraphs (*b*), (*c*) and (*d*)(i), and substituting in each case the following—

"an article";

(*b*) in subclause (1)(*d*)(ii), by deleting "any acetylating substance" and substituting the following—

"an article";

(*c*) by deleting subclause (2) and substituting the following—

"(2) Any public officer may seize, remove and detain anything if he has reason to suspect that such thing is an article liable to seizure."; and

(*d*) by inserting after subclause (6) the following new subclause—

"(7) In this section, "article liable to seizure" means—

(*a*) any acetylating substance referred to in section 13;

(*b*) any money or thing which is liable to forfeiture under this Ordinance; and

(*c*) anything which is or contains evidence of an offence under this Ordinance.".

The amendments were agreed to.

Clause 12, as amended, was agreed to.

Clauses 13 to 19 and the Schedule were agreed to.

LANDLORD AND TENANT (CONSOLIDATION) (AMENDMENT) (NO 2) BILL 1975

Clauses 1 to 14 were agreed to.

Council then resumed.

Third reading of bills

THE ATTORNEY GENERAL reported that the

Inland Revenue (Amendment) Bill 1975 and the

Acetylating Substances (Control) Bill 1975

had passed through committee with amendment and that the

Exchange Fund (Amendment) Bill 1975 and the

Landlord and Tenant (Consolidation) (Amendment) (No 2) Bill 1975

had passed through committee without amendment and moved the third reading of each of the bills.

Question put on each bill and agreed to.

Bills read the third time and passed.

Adjournment

Motion made and question proposed. That this Council do now adjourn—THE COLONIAL SECRETARY.

4.35 p.m.

Mass Transit Railway

DR CHUNG: —Your Excellency, many people received with great disappointment and some even in anger the news that the Japanese consortium could not fulfil its commitment as stipulated in the Letter of Intent to build the initial four stages of our mass transit railway within the cost of $5,000 million.

Sir, allow me to recapitulate a few dates which have important bearings on this unfortunate development. It was on 1st August 1973 that my honourable Friend, the Financial Secretary, made the announcement

in this Council about the adoption of the single-contract approach and the negotiation with a number of consortia to build the initial system of the mass transit railway. The Japanese consortium submitted on 27th September 1973 its pre-emptive bid which was accepted by the Government in December 1973. The Letter of Intent was signed on the 15th February 1974.

Honourable Members will remember that the period between September 1973 and March 1974 was the worst period as far as rising prices for and shortages of basic materials are concerned. Let me cite a few typical and relevant examples to illustrate the situation at that time. On the London Metal Exchange, copper went up from a normal price of £ 500 to £ 1,200 per metric ton, and zinc from £ 200 to £ 600 per metric ton. Prices for reinforced steel bars increased by 70 *per cent* and for cement by 130 *per cent* as compared to their normal prices in the early part of 1973. At that time, any competent businessman would have taken into consideration the most likely event of continuing rapid inflation.

Honourable Members will also recall that the Government has since July 1973 been conducting negotiations with four consortia in London and Tokyo with a view to explaining to them our requirements for a single-contract arrangement with a ceiling price of $5,000 million and inviting from each of them a bid for the construction, equipping and financing the first four stages of the mass transit railway. One of the most important reasons, if not the most important one, for the Government to accept the Japanese consortium's bid was that it offered a firm price within our stipulated ceiling price of $5,000 million without subsequent cost escalation of any kind. There is now criticism that Government should not have accepted such an unrealistic bid at that time. But this criticism is misplaced. This is a consortium of the biggest Japanese industrial enterprises, known to be backed up by the Japanese Government. Furthermore, at that time, Government had no alternative but to accept this attractive bid, the only bid within the stipulated ceiling price. In the light of rapid inflation at that time, I nevertheless presume that the Government had naturally repeatedly sought and received assurance from the Japanese consortium on this most cogent issue of no cost escalation of any sort. Nevertheless, I would welcome a confirmation from Government on the correctness of this presumption. It is also important to note that the Letter of Intent was signed on a date more than four months after the announcement of the Arab oil embargo and in the midst of the famous "spring labour offensive" in Japan.

[DR CHUNG] **Mass Transit Railway**

Contrary to expectations, we saw during the second half of 1974 a general fall of material prices and a considerable ease in material supply. On the London Metal Exchange, prices for copper went down to £ 600 and zinc to £ 350 per metric ton. Both reinforced steel bars and cement prices have also dropped to a level lower than the peak prices. Furthermore, the current rate of inflation as compared to that at the peak early last year is about half in Japan and approximately threequarters locally. Such developments, one would have thought, would be in the Japanese consortium's favour. It is therefore difficult for the Government to accept the unreasonable request, first, for a revised price ceiling of $6,000 million together with new provision for price escalation and, secondly, for a degraded standard of design specifications and overall performance.

Sir, I am authorized by practically all my Unofficial colleagues, first, to say that Government is right in not accepting the above two requests from the Japanese consortium and, secondly, to support the view of Government that the consortium through no fault of our own has committed a serious error of judgment which will result in Hong Kong suffering both a time delay and a financial loss.

It is understood that there will be at least a year's delay in building the mass transit railway and that there will be a financial loss of $160 million. This sum of $160 million is the actual expenditure incurred from the date of the Government's acceptance of the Consortium’s pre-emptive bid in mid-September 1973 up to mid-January 1975 and would not be recoverable if the mass transit railway project were eventually abandoned altogether. Although it is likely that we will construct the modified S-shaped initial system, there is still presumably a substantial proportion of the sum of $160 million which is not recoverable. Like many other territories, we in Hong Kong are facing economic recession and, as members of the Finance Committee, the Unofficial Members are very concerned with this financial loss. Speaking again on behalf of the great majority of my colleagues, therefore, I urge the Government to continually press the Consortium for a much more just and fair financial compensation than what the honourable Financial Secretary described as a derisory offer of $5 million as an *ex-gratia* payment for non-fulfilment of the Letter of Intent. In the editorials of both the English morning newspapers, it is considered that this ridiculous offer of $5 million is merely adding insult to injury. I could not agree more. There is also the question of the international reputation and prestige not only of the particular firms concerned but of prestige Japanese

contractors in general. From that point of view alone I would have expected the Consortium to offer compensation of a sum more in line with the extent of the loss directly attributable to the unilateral breach of the Letter of Intent.

MR WANG: —Sir, I wish to endorse every word that my senior colleague has just said, as that which I believe is representative of the feelings and reaction of the people in our community, over the shock announcement on the Japanese Consortium's dishonouring of the Letter of Intent signed almost a year ago. In as much as a Letter of Intent is not a legal contract, so it is unquestionably an agreement which is commonly made between two parties of honourable standing, who are expected to understand its implication and obligations, and that, save for a breach of good faith or an act of God beyond human control, it is not to be dishonoured without the most serious consequences. I have not heard of any precedent where any consortium of international reputation has ever behaved so abominably as in the case in this instance.

Sir, to describe the present situation it would appear to be, in a nutshell—that in all this time that has elapsed, the consortium has maintained a poker-faced attitude, to now come after this long delay—to the table and to say—"No deal for a $5,000 million project, and for this abominable act we offer you a miserable $5 million irrespective of the colossal loss of time, money and trouble we have inflicted upon you". This act of serious irresponsibility—and I will agree also such an offer—is, at best, seen as adding insult to injury.

Sir, at this moment I cannot resist expressing also my disappointment and disapproval of those in our midst who for reasons best known to themselves appear to play in the role of Judas. I refer to those few people who at time—or any moment of distress—are ready to raise an accusing finger without first ascertaining the right target.

I for one have not always seen eye-to-eye with my honourable Friend the Financial Secretary, on all issues, and very often have engaged with him in heated debate over many a proposal that he has submitted to this Council or to the Finance Committee. However there can be no doubt in this particular case that our Government—including my honourable Friend have acted in the most commendable good faith. At no time from the onset of this matter has there been any cause to suspect that such a consortium could let us down so deplorably. In fact I am still inclined to believe that what has occurred is a bad dream, bearing in mind the status of those who formed the

consortium—it is almost unbelievable. I would like to believe that when its representatives go home and meet with all authorities concerned they might yet come forward to suggest an amicable solution to this unhappy situation.

MR WILLIAMS: —Sir, in supporting the Government's stand in this matter there is little I can add to what has been said by the two previous speakers.

As I see it the main thrust of our complaint is the lateness of the withdrawal by the Japanese Consortium. A Letter of Intent may not be a legal contract but it is as good as a handshake, and that's good enough for most of us. Be that as it may if they had come to us earlier and admitted they could not meet their obligations the matter might have been resolved more satisfactorily. We are not unreasonable people and we are prepared to face facts.

But for ten months we have been visibly spending large sums of money on this abortive scheme, a good part of which is irrecoverable. And now they come to us with a derisory offer of compensation: to use a Japanese word an *okuyamiryo* or condolence payment with, as far as I know, a minimal expression of regret.

On the basis of the facts presented and, as far as I am aware, they have not been challenged by the Japanese Consortium, the situation is unacceptable, and we must obtain full repayment of our losses.

Good relations with Japan are of the utmost importance to us and to the Japanese. This unhappy event could seriously damage this relationship adding vastly to the losses on both sides. Let us all be realistic about this. I can only hope that what has been said this afternoon will be seriously considered by the Japanese Consortium with the result that this matter can be settled without further harm.

MR LO: —Sir, I consider that before we adjourn it would help to clear the air and allow all of us, as well as members of the public, to reach a better understanding of the situation if the Government would supply full answers to the following questions:

first, what was actually agreed between the Government and the Consortium;

second, what was it that the Consortium did not do which it had agreed to do;

third, how were the negotiations broken off;

fourth, what is the amount and the kind of financial loss that was suffered by Hong Kong;

fifth, what is the amount and the kind of compensation which the Government is asking for or is morally entitled to; and finally

sixth, why did the Government take the risk of incurring the losses without being covered legally?

The answers to these questions, Sir, will, I feel sure, make it evident as to whether the Consortium had lived up to its obligations and whether the Government had lived up to its responsibilities.

I support the motion that this Council do adjourn.

4.50 p.m.

THE FINANCIAL SECRETARY: —I fully endorse the remarks made by my unofficial colleagues about the Japanese Consortium's unilateral withdrawal from the negotiations which it agreed to enter into. And on behalf of the Provisional Authority, I am grateful to them for what I have taken to be a vote of confidence in the way the Provisional Authority has handled its negotiations with the Japanese Consortium.

My honourable Friend Dr CHUNG asked for confirmation that we had sought and received assurances from the Japanese Consortium that, throughout its negotiations for a formal contract, the Consortium would not seek cost escalation of any kind. In addition, my honourable Friend Mr T. S. LO asked what it was that the Consortium did not do which it had agreed to do.

Between April and mid-November 1974, the Provisional Authority held a series of meetings with the Japanese Consortium with a view to negotiating a formal contract as provided for, and within the terms of, in the Letter of Intent. As honourable Members will be aware from this document, it provided for the negotiation of a contract for building the first four stages of the railway within the agreed price ceiling of HK$5,000 million and adequate to meet our performance specifications. It was this the Consortium failed to do.

At each of these meetings the Provisional Authority was told that, notwithstanding certain financial and cost difficulties affecting every

member company within the Consortium, the Consortium was determined to proceed with the project because it was confident that these difficulties could be overcome. Let me hasten to add that these were very firm assurances given, let us remember, by a consortium led by the six most important commercial and industrial conglomerates in Japan. It was not until mid-November 1974, when the Consortium presented its package of incomplete and inadequate design proposals and solutions, that it said that it could not proceed with the negotiations unless the price ceiling was increased to HK$6,000 million and provision was made in addition for price escalation. Even then, the Provisional Authority gave the Consortium a second chance to stay in the field by affording a thirty-day grace period to produce a package broadly within the sprit of the Letter of Intent; that is to say, a package offering a fixed price which would preserve the overall viability of the project. On the expiry of the thirty days on 17th December 1974, the Consortium told the Provisional Authority that it was unable to offer such a package and withdrew from the negotiations.

I have taken careful note of my honourable Friends' views that the Government should continue to press for a just and fair compensation settlement. I can only assure them that the Provisional Authority hag already done its best in this matter in meetings with the Japanese Consortium over the period from 17th December 1974 to 10th January 1975. Furthermore, in the period between the adjournment of the Provisional Authority's meeting with the Japanese Consortium on 10th January and the meeting of the Executive Council on the morning of 14th January, the Consortium was given a further chance to come back with an offer more meaningful than the derisory sum of HK$5 million which it had offered on 10th January 1975 as an *ex gratia* payment. As honourable Members are aware the Consortium refused to improve its offer. Now that the Consortium has ceased to exist as a formal entity, and bearing in mind that the Letter of Intent did not legally bind the Consortium to build the railway, I have grave doubts about the likely success of pursuing our claim for compensation. On the other hand, I can assure honourable Members that the concern of the Hong Kong Government about the course of events is well-known to the relevant Japanese authorities.

Having said this, however, I should perhaps add, in answer to my honourable Friend Mr T. S. LO, that the loss arising from the Consortium's unilateral withdrawal could either be calculated in terms of the escalation of costs since the Letter of Intent was signed or, at the

other extreme, in terms of the interest foregone on actual expenditure incurred during the past twelve months or so and certain items of expenditure, mainly on travel, which we would not have incurred had we not signed a Letter of Intent with the Japanese Consortium. In point of fact, we chose a perfectly legitimate middle course between these two extremes, namely, actual expenditure incurred and firm commitments entered into over the pass 12 months or so. So whatever sum might have been negotiated in the end, the offer of $5 million was just out of the question from our point of view.

My honourable Friend Mr. T. S. LO has asked what possible benefits had persuaded the Government to take the risk of incurring this expenditure without being covered legally. The Letter of Intent was couched in terms which conformed with conventional commercial practice. The Consortium's bid, as, I have already stated on a number of occasions, was accepted by the Government for three reasons. First, it was the only bid which came within the Government's price ceiling, of HK$5,000 million which virtually assured the financial viability of the project because it made no provision for subsequent price escalation. Secondly, it seemed at that time to hold out the opportunity of an early start and an early finish for the project, namely, by mid-1979. But quite apart from the positive advantages this bid offered, the local agents of the Consortium—Jardine, Matheson and Company Limited—had given the Mass Transit Steering Group every assurance that a consortium of the size, technical competence and financial strength of the Japanese Consortium could hardly fail and was to be believed. Thirdly, the idea of the Letter of Intent was a commitment in honour to work, on the broad main terms which it sets out, towards realization of the Consortium's pre-emptive bid. The Consortium would not have agreed to bind itself legally to anything and, given the assurances to which I have referred, the Government saw no reason to worry over this.

It may also be asked why the Provisional Authority did not withdraw from the negotiations with the Japanese Consortium as soon as it became apparent that it was in difficulties. There are two answers to this question. First, the Provisional Authority would have placed itself in the wrong if it had withdrawn from the negotiations before it had firm evidence that the Consortium would not fulfil its obligations. Secondly, the Provisional Authority was twice led to believe that a national consortium of the size and reputation of the Japanese Consortium would not behave in the way it did. I have already made a brief reference to how the Provisional Authority was misled at the time the Consortium made its pre-emptive bid. Subsequently, given the

firm and repeated assurances that the Consortium was determined to proceed with the project and was doing its best to overcome its difficulties, our assumption during the June, August and September engineering discussions was that the Consortium's engineers had not fully understood the rationale behind our design parameters and performance requirements and our aim was to pull them back to meeting our requirements. Not until the engineering talks in December 1974 were we told that the Consortium had asked its engineers to pare everything to the bone.

Finally, Sir, a word or two about the future—and it is the future which now matters.

We now have a capability to proceed on a multi-contract basis something which we did not have in 1973. During 1974 we assembled a directorate for the future Mass Transit Railway Corporation and its component departments. It is this team of chief officers designate of the future Corporation, acting in conjunction with the staff of the Public Works Department, the Provisional Authority's consulting engineers, the Provisional Authority's financial advisers and the Provisional Authority's Secretariat who, within a short period of two months, developed the Modified Initial System and the method for implementing it, and I would like to record here, Sir, the Provisional Authority's and the Government's thanks to this team for the work they have done.

The Modified Initial System is a viable system for several reasons. First, the contract costs estimated at just over HK$3,900 million at 1974 values will, after allowing for cost escalation and a fairly generous margin for unforeseen contingencies, probably end up at HK$4,900 million or there-abouts by the time the project is completed. This puts the cost just below the ceiling of HK$5,000 million beyond which the project ceases to be viable. Secondly, although there can be no absolute certainty about the total price of the project if we proceed on a multi-contract basis cost escalation can be confined to fluctuations in wages and the prices of materials and there are good precedents in administering contracts with materials and wage fluctuation clauses. Thirdly, we are reasonably certain about our revenue projections. So much then for financial viability. From a public transport point of view the project is viable because it runs through the most densely populated parts of the urban areas. In so doing, it meets maximum demand for passenger transport and affords the maximum relief of congestion.

Sir, it remains the Government's policy to build an underground mass transit railway for we believe it to be a vital necessity in the years ahead. So the Government has decided in principle that the Modified Initial System should be proceeded with on a multi-contract basis and the Provisional Authority has already invited interested parties to express their interest in tendering for its construction, equipment and financing. When tenders have been received and analysed, the Provisional Authority will report back to the Governor in Council and I believe we shall be able to confirm that the Modified Initial System is a feasible proposition, in which event the first contracts will be let in August. The aim is to complete construction of the Modified Initial System and to have it fully operational by mid-1980.

Question put and agreed to.

Next sitting

HIS EXCELLENCY THE PRESIDENT: —Accordingly I now adjourn the Council until 2.30 p.m. on Wednesday, the 5th of February.

Adjourned accordingly at five minutes past five o'clock.

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