

HONG KONG SPECIAL ADMINISTRATIVE REGION

Audit Commission

Annual Report 2004-05

**Audit Commission
Hong Kong
May 2005**

AUDIT COMMISSION
ANNUAL REPORT 2004-05

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MESSAGE FROM THE DIRECTOR

First Annual Report

The year 2004 marked the 160th anniversary of the Audit Commission (Audit). Since I took up the post of the Director of Audit in December 2003, I have wanted to record Audit's historical development and major areas of our work, and highlight the challenges facing us. This has prompted me to compile Audit's first Annual Report, which covers the period from 1 January 2004 to 31 March 2005. (Future Annual Reports will cover the period 1 April to 31 March.)

Taking stock of Audit's historical development

2. In 2004, Audit celebrated the 160th anniversary of the appointment of the first Director of Audit (formerly known as the Auditor General). Audit is one of the oldest government departments in Hong Kong. I am pleased and honoured to have joined this Commission with such a long and respectable tradition of professionalism and commitment. In this Annual Report, I have dedicated a whole chapter (Chapter 1) to trace the development of government audit in Hong Kong over one and a half centuries. I am sure that we are able to look back with pride at Audit's accomplishments in the past, which set a firm foundation for its future development.

Four main objectives

3. The four main objectives which I focused on as a new Director of Audit are:
- (a) ensure that Audit plays a positive and constructive role;
 - (b) maintain effective relationships with all stakeholders;
 - (c) enhance governance, accountability and transparency in the public sector; and
 - (d) improve the organisation and capability of Audit to meet the challenges in the 21st century.

Ensure that Audit plays a positive and constructive role

4. It is our mission to help the Government enhance public sector performance and accountability. In order to provide a value-added service to the community, we must continue to play a positive and constructive role in conducting our audit work. It is all the more important when we are dealing with subjects of great public concern.

5. In the past year, we issued a number of high-profile value for money (VFM) audit reports, notably the reviews of the Harbour Fest, the English Schools Foundation (ESF), and the Grant of Land at Discovery Bay and Yi Long Wan. In all these reviews, we

made great efforts to help the Government learn lessons and add value. Our recommendations were generally accepted by the Administration. Details about these reviews are set out in Chapter 3 on VFM Audit.

Maintain effective relationships with all stakeholders

6. Since my appointment as the Director of Audit, I have noted on a couple of occasions that the role of Audit is not always fully understood. Some sectors of the community still mistakenly believe that the primary role of Audit is simply to criticise the Government. We made efforts in the past year to do more public relations work targeted at different stakeholder groups with a view to dispelling this misconception.

7. A briefing on Audit's work to the newly-appointed Members of the Public Accounts Committee was conducted. I delivered a number of talks and presentations on subjects related to our work to various government departments and professional bodies. I also took part in some media interviews and radio phone-in programmes, in order to let the general public know more about our work. Details of such public relations work are described in Chapter 4 on Corporate Services.

Enhance governance, accountability and transparency in the public sector

8. Audit helps the Government enhance governance, accountability and transparency in the public sector by conducting two types of audits: regularity audit and VFM audit. The implementation of accrual reporting is a key initiative of the Government for improving its financial accountability and transparency. We have been keeping a close watch on the development of accrual accounting in the Government, as it will have wide ramifications on our regularity audit work. We also keep in view the implementation of the new Government Financial Management Information System to see how it affects our work. Chapter 2 gives more details about our regularity audit work.

9. In recent years, governments worldwide have put governance and accountability issues high on their agenda. Hong Kong is no exception. In the past year, our VFM audit work put corporate governance and public accountability in the limelight. The Harbour Fest review highlighted the essence of public accountability — i.e. government officials, who are entrusted with public resources, are answerable for the fiscal, managerial and programme responsibilities that are conferred. The Discovery Bay case showed that there might not be any time limit for public accountability. In the ESF audit, we made useful recommendations for improvement in the corporate governance of the ESF. Chapter 3 gives more details about these VFM audits.

Improve the organisation and capability of Audit to meet the challenges in the 21st century

10. A key focus in the past year was the stepping up of efforts to improve the organisation and capability of Audit. I believe that only by continuously updating our knowledge and upgrading our capability can we meet the challenges facing Audit in the

21st century. Soon after taking up the post of the Director of Audit, I embarked on a number of important initiatives, including the reorganisation of the Commission, the merger of the Auditor and Examiner grades, and the comprehensive revision of the Audit Manual. I also encouraged all staff to take part in training courses and development programmes. All these help ensure that Audit is a learning organisation, which is able to keep pace with the development of Hong Kong as a world-class city. More details about our work in these areas are set out in Chapters 2 to 4.

Looking ahead

11. I am impressed by the integrity, objectivity and professionalism that all staff of the Commission display in their work. I would like to put on record my appreciation of their efforts in delivering quality services in both regularity and VFM audits. I am grateful too for the Legislative Council and the public's response to our work over the past year.

12. I am also thankful for the cooperation given by the bureaux and departments audited and their positive attitude in dealing with my recommendations and findings. To put things in proper perspective, although our reports show that there are inadequacies in the operations of bureaux and departments audited, this does not necessarily mean that these bureaux and departments are badly managed. I firmly believe that our role is to partner with the government to improve public governance which is a continual process. Hong Kong people expect their government to manage its services and programmes well, give them value for their tax dollars, and be honest, forthcoming and accountable for its actions. We are all determined to meet this challenge.

Benjamin Tang
Director of Audit
May 2005



Mr Benjamin Tang
Director of Audit

CHAPTER 1: DEVELOPMENT OF GOVERNMENT AUDIT IN HONG KONG

Introduction

1.1 The Audit Commission (Audit), which was known as the Audit Department before 1 July 1997, has a long history. The necessity for an audit presence was recognised in the very early days of Hong Kong. As a matter of fact, Audit is one of the oldest government departments. The first Director of Audit (formerly known as the Auditor General) was appointed in 1844. The current incumbent, Mr. Benjamin Tang, took up the post as the 22nd Director of Audit in December 2003. The year 2004 marked Audit's 160th anniversary. Audit took this opportunity to take stock of the historical development of government audit in Hong Kong, with a view to its further development in the years ahead.

1.2 The duties and powers of the Director of Audit are stipulated in the [Audit Ordinance \(Cap. 122\)](#) which was enacted in December 1971. On 1 July 1997, pursuant to the [Basic Law of the Hong Kong Special Administrative Region of the People's Republic of China](#), Audit was established and the Director of Audit became one of the [principal officials](#) of the Hong Kong Special Administrative Region (HKSAR).

The pre-1997 era

The early colonial years

1.3 Hong Kong has been part of China since ancient times. It was occupied by Britain after the Opium War in 1840. Mr. A. E. Shelley, the first Director of Audit, was appointed in 1844. He functioned locally in Hong Kong reporting to the then Commissioners for Colonial Accounts in the United Kingdom.

1.4 From 1867, the accounts of colonies were audited by the local governments concerned, subject to an audit by the Comptroller and Auditor General in London under certain circumstances. In May 1910, the Colonial Audit Department was established, which consisted of a small central establishment in London and establishments in colonies. All these establishments were under the supervision of the then Director of Colonial Audit. In 1947, the title of the Director was changed to Director General, and the title of his representative in charge of a territorial audit department was changed to Director of Audit. In 1954, the Colonial Audit Department was renamed the Overseas Audit Department.

1.5 The then Director General in London certified the accounts of the Government on the basis of assurances and reports given to him by the Director of Audit until the office of the then Director General was abolished and the central establishment in London was closed at the end of 1971. It was decided that the responsibility for audit in dependent territories should rest with the head of the territorial audit department (i.e. the Director of Audit). Each territory was asked to enact legislation to give effect to this decision.

Enactment of the Audit Ordinance

1.6 A key milestone in the development of public auditing in Hong Kong was the enactment of the Audit Ordinance in December 1971. The Ordinance provides for the appointment, tenure of office, duties and powers of the Director of Audit and for the auditing of and reporting on the public accounts. The enactment of the Ordinance established the statutory framework for the audit and certification of the accounts of the Government. The Ordinance confers wide powers on the Director in carrying out his statutory duties. He has wide powers of access to the records of departments and he can require any public officer to give an explanation and to furnish such information as he thinks fit to enable him to discharge his duties. In the performance of his duties and the exercise of his powers under the Ordinance, the Director is not subject to the direction or control of any other person or authority. The audit work carried out in accordance with the Ordinance is generally known as regularity audit.

Establishment of the Public Accounts Committee

1.7 In March 1976, a Member of the [Legislative Council](#) (LegCo) expressed concerns that there was a need for adequate machinery to ensure that there was no extravagance or wastage in the expenditure of public funds once those funds were approved in the Estimates. In March 1976, the Director of Audit made a recommendation to the Financial Secretary for the adoption of a Public Accounts Committee (PAC) system in view of the fact that the Director had no power to require that action be taken to rectify any failings stated in his reports, and LegCo had little opportunity to investigate the efficacy with which the revenue was collected or to enquire into the purposes for which the moneys voted had actually been expended.

1.8 In 1978, the [PAC](#) was established as a standing committee of LegCo. The PAC considers the reports of the Director of Audit on the accounts of the Government, on such other accounts required to be laid before LegCo as the PAC may think fit, and on any matter incidental to the performance of the Director's duties or the exercise of his powers as the PAC may think fit. The PAC also considers any value for money (VFM) audit report of the Director laid on the table of LegCo. The task of the PAC is to ensure that the funds provided by LegCo through the Appropriation Ordinance have been spent in the way intended. The establishment of the PAC was an important milestone in the development of public accountability in Hong Kong.

1.9 On 13 November 1984, the PAC held its first public hearing on the Director of Audit's report. Since then, members of the public and of the press are admitted as spectators at sittings of the PAC. The opening up of PAC hearing is another important milestone in the development of public accountability in Hong Kong.

The Value for Money Audit Guidelines

1.10 Prior to the enactment of the Audit Ordinance in December 1971, audit examination was under the control of the then Director General in London and was required

to be carried out in accordance with a programme of work subject to his approval. It was predominately a “regularity” type audit, designed primarily to give the then Director General the assurances he needed to enable him to certify that the accounts were correct. Few VFM audits were conducted. Initially, developments in VFM audit focused on the examination of capital works contracts. This was because, by reason of their nature, size, escalation in costs, cancellation or curtailment, these projects might involve waste, extravagance or even fraud. In 1968, the then Director General gave his full support to the Director of Audit in his efforts to pay greater attention to VFM in the course of auditing revenue and expenditure. In the mid-1970s, VFM audit was extended to cover organisations in receipt of government grants.

1.11 In November 1985, when tabling the Director of Audit’s report on the accounts of the Government for the year ended 31 March 1985, the then Chief Secretary stated in LegCo that the appropriate forum for considering policy issues, including any that might be raised in the Director’s report, was LegCo where they could be properly and fully debated. In response, the Director made a statement in the PAC that what he had done was not to criticise Government’s policies but to comment on the way Government’s policies had been implemented and to examine the arrangements by which policy decisions were reached. The Director believed that he was within his conventional remit to conduct VFM audits and to report thereon, having regard to the internationally accepted government audit standards of economy, efficiency, and effectiveness with which public money was spent.

1.12 In January 1986, the PAC accepted that the Director of Audit was not criticising government policy. The PAC noted that while it was of the view that the Director did have a remit to examine and report on policy implementation, the action to his report (see para. 1.11) indicated that the boundaries of that remit, particularly in relation to VFM studies, had not been clearly defined. A set of VFM Audit Guidelines was agreed between the PAC and the Director and accepted by the Government. In November 1986, a paper (“*Scope of Government Audit in Hong Kong — ‘Value for Money’ Studies*”) was presented to LegCo by the Chairman of the PAC. This paper covered the scope of work and guidelines for VFM audits. The VFM Audit Guidelines set out the authority and boundaries within which the Director might conduct VFM audits. The promulgation of the Guidelines set an important milestone in the development of VFM audit and public accountability in Hong Kong.

Reporting to LegCo

1.13 ***Requirements of the Audit Ordinance.*** Section 12 of the Audit Ordinance provides that:

- (a) the Director of Audit shall, within a period of seven months after the close of the financial year (i.e. in October), prepare and submit to the President of LegCo (see also paras. 1.14 to 1.16) a report in respect of his examination and audit of the accounts of the Government;
- (b) within a period of one month after the receipt of the report and certified statements from the Director (see para. 2.2), a copy of the report and certified statements shall be laid before LegCo; and

- (c) within a period of three months after the laying of the report and certified statements from the Director, a copy of the PAC's report shall be laid before LegCo.

1.14 ***Amendment of Audit Ordinance in 1978.*** When the Ordinance was enacted in 1971, the Director of Audit was required to submit his report to the then Governor. In 1978, the Ordinance was amended to provide for the submission of the Director's report to the then Governor as President of LegCo.

1.15 ***Requirements made in 1987.*** In October 1987, the Chairman of the PAC tabled in LegCo a Codicil to the paper presented in November 1986 (see para. 1.12). According to the Codicil, the Director of Audit had to report his findings on VFM studies in LegCo twice each year:

- (a) one report had to be combined with the Director's annual report on the accounts of the Government, which he submitted to the then Governor as President of LegCo within seven months of the end of the financial year. The combined report had to be handled in accordance with section 12 of the Audit Ordinance; and
- (b) another report had to be submitted to the then Governor as President of LegCo by the 7th of April each year. By the 30th of April, copies of the report had to be laid before LegCo.

1.16 ***Changes made in 1993.*** In 1993, when the then Governor was relieved of the office of the President of LegCo, the Audit Ordinance was further amended to provide for the Director's report to be submitted to the President of LegCo. The Chairman of the PAC tabled in LegCo a revised Codicil to the paper presented in November 1986 (see paras. 1.12 and 1.15). According to the revised Codicil, the Director's VFM reports had to be submitted to the President of LegCo.

The Government Minute

1.17 In 1978, when the PAC was established, the Government agreed to prepare a Government Minute, after considering the comments and recommendations contained in the PAC's report, within three months of the tabling of the PAC's report. The Government Minute would contain the Government's responses to the PAC's report, indicate what action the Government would take to rectify any irregularities brought to its attention by the PAC or the Director of Audit and, if necessary, explain why it was not intended to take any follow-up action. The requirement for the tabling of the Government Minute was stated in the two Codicils mentioned in paragraphs 1.15 and 1.16.

The post-1997 era

The Basic Law and the establishment of the Audit Commission

1.18 Since China's resumption of the exercise of sovereignty over Hong Kong on 1 July 1997, Hong Kong has become a special administrative region of the People's Republic of China. According to [Article 58 of the Basic Law](#), a Commission of Audit shall be established in the HKSAR, which shall function independently and be accountable to the Chief Executive of the HKSAR. Consequently, the former Audit Department (“核數署”) was renamed the Audit Commission (“審計署”) with effect from 1 July 1997. The post title of the Director of Audit in Chinese was also changed from “核數署署長” to “審計署署長” with effect from the same date.

The new Value for Money Audit Guidelines

1.19 In February 1998, a paper (“*Scope of Government Audit in the Hong Kong Special Administrative Region — ‘Value for Money Audits’*”) was presented to the Provisional Legislative Council by the Chairman of the PAC. This paper covered the scope of work, guidelines and procedures for VFM audits. This new set of [VFM Audit Guidelines](#) was agreed between the PAC and the Director of Audit and accepted by the Government of the HKSAR.

The new procedures for value for money audits

1.20 According to the paper presented in February 1998 (see para. 1.19), the Director of Audit shall report his findings on VFM audits in LegCo twice each year:

- (a) the first report shall be submitted to the President of LegCo within seven months of the end of the financial year. Within one month, copies of the report shall be laid before LegCo; and
- (b) the second report shall be submitted to the President of LegCo by the 7th of April each year. By the 30th of April, copies of the report shall be laid before LegCo.

The Director's report shall be referred to the PAC for consideration when it is laid on the table of LegCo. The PAC shall follow the rules governing the procedures of LegCo in considering the Director's reports (i.e. [Rule 72 of the Rules of Procedure of LegCo](#); and [PAC's Procedure](#), as determined by the PAC in accordance with the Rule 72). A Government Minute commenting on the action the Government proposes to take in respect of the PAC's report shall be laid on the table of LegCo within three months of the laying of the report of the PAC to which it relates.

Directors of Audit to date

1.21 The past and present incumbents of the post of Director of Audit (formerly also known as Auditor General or Auditor) are listed below:

Auditors General

1	Adolphus Edward Shelley	1844 – 1846
2	William Caine, Lieut-Col	1846 – 1854
3	William Thomas Mercer	1854 – 1858
4	William Hepburn Rennie	1858 – 1870
5	John Gardiner Austin	1870 – 1879
6	William Henry Marsh, CMG	1879 – 1887
7	Frederick Stewart, LL.D	1887 – 1890

Auditors

8	Hilgrove Clement Nicolle	1890 – 1904
9	Hugh Richard Phelips	1904 – 1930
10	Percival Lorimer Collisson, OBE	1930 – 1938
11	Arnold Pollard	1938 – 1948

Directors of Audit

12	Percival Henry Jennings, CBE	1948 – 1955
13	Frank Ernest Lovell Carter, CBE	1955 – 1959
14	William John Dupre Cooper, CBE	1959 – 1965
15	Denis George Britton, OBE	1965 – 1970
16	Percy Thomas Warr	1970 – 1975
17	Gordon Evershed Lyth, OBE	1975 – 1982
18	Norman Bertram Stalker, OBE	1982 – 1988
19	Robert Jeffrey Hutt, OBE	1988 – 1992
20	Brian George Jenney, OBE	1992 – 1995
21	CHAN Yin-tat, Dominic, S.B.S., JP	1995 – 2003
22	TANG Kwok-bun, Benjamin, JP	2003 - present

Looking ahead

1.22 The above paragraphs present a brief outline of the development of government audit in Hong Kong since the appointment of the first Director of Audit in 1844. Over some one and a half centuries, Audit has evolved from a small colonial audit unit to a well administered and efficient audit office, providing a full range of quality audit services.

1.23 Today, Audit functions independently and plays a vital role in the public accountability system in the HKSAR. The work of Audit is highly regarded by the Legislature, the Administration, the media and the general public. Audit is proud of its history and achievements in the past and will continue to build on this foundation to realise its corporate vision of “*excellence in public sector auditing*”.

CHAPTER 2: REGULARITY AUDIT

Introduction

2.1 The aim of regularity audits is to provide LegCo with an overall assurance that the Government's financial and accounting transactions and those of funds of a public or quasi-public nature are proper and that they conform to generally accepted accounting standards.

2.2 Regularity audit is carried out mainly under the Audit Ordinance which, among other things, provides for the submission of annual statements by the Director of Accounting Services, the examination and audit of those statements by the Director of Audit, and the submission of his report thereon to the President of LegCo. The statements required to be rendered by the Director of Accounting Services are the Statement of Assets and Liabilities and the Statement of Receipts and Payments of:

- (a) ***General Revenue Account (GRA).*** For control and funding purposes, the Government's financial activity is undertaken through a variety of accounts and funds. The GRA acts as the central funding device with resources transferred as necessary to and from a number of purpose-specific funds; and
- (b) ***Funds established under section 29 of the Public Finance Ordinance (Cap. 2).*** There are eight funds, namely Capital Investment Fund, Capital Works Reserve Fund, Civil Service Pension Reserve Fund, Disaster Relief Fund, Innovation and Technology Fund, Land Fund, Loan Fund and Lotteries Fund. Financial reporting requirements of the first seven Funds are laid down in the Audit Ordinance, while those of the Lotteries Fund in the Government Lotteries Ordinance (Cap. 334).

2.3 The Director of Audit examines and audits the financial statements of the GRA and seven funds in accordance with the Audit Ordinance (see para. 2.2) and the Audit Commission auditing standards which are adopted as a framework for the proper conduct of public-sector audits. These auditing standards are, in all relevant and material respects, in line with those issued by the International Organisation of Supreme Audit Institutions and the Hong Kong Institute of Certified Public Accountants.

2.4 Regularity audit is conducted in accordance with a programme of work, which is determined annually by the Director of Audit. Audit adopts a risk-based approach in the planning and conduct of regularity audit. It puts emphasis on risk assessment and focuses audit tests on areas with risk of significant errors and irregularities. It is not the intention of regularity audit to disclose each and every accounting error or financial irregularity. With the considerable volume and variety of government revenue and expenditure, this examination of accounts is of necessity carried out by means of selective test checks and in-depth reviews designed to indicate possible areas of weakness. Reliance for detailed

checks on the regularity of the accounts is placed largely on the systems of internal control operated by individual departments.

2.5 Regularity audit is similar to financial audit in the private sector. Compared with private-sector auditors, we put more emphasis on the regularity and probity aspects. This is because we are required by section 8 of the Audit Ordinance to satisfy ourselves, among other things, that the public funds have been applied to the services and for the purposes intended; and that the payments and receipts of public moneys are in accordance with the relevant rules and regulations. It also gives an assurance that all rules and regulations, which are established to ensure good governance practices, are always followed.

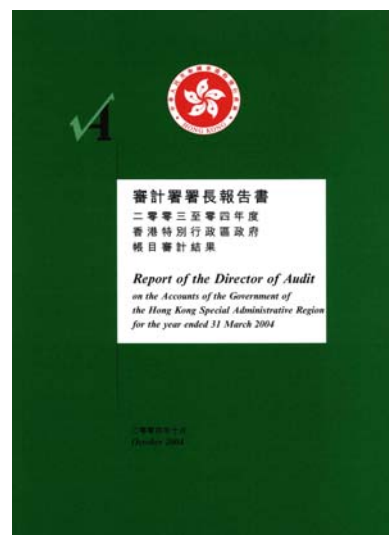
2.6 To discharge the wider responsibilities of the Director of Audit under section 8 of the Audit Ordinance, we supplement our normal certification audit work with a programme of risk audit, which examines risks related to regularity, propriety and financial control. In conducting risk audit work, Audit periodically review the Government's activities to identify areas where there are significant risks of irregularity, impropriety or failure in financial control. The aim is to ensure that all significant risks are identified, examined and, if necessary, reported over a reasonable period of time.

The year under review

Accounts certified in 2004

2.7 After taking up the post of the Director of Audit in December 2003, Mr. Benjamin Tang signed his first Report on the Accounts of the Government of the HKSAR (for the year ended 31 March 2004) on 23 October 2004 and submitted it to the President of LegCo on 29 October 2004.

2.8 In 2004, a total of 75 accounts were audited and certified, i.e. the GRA and the eight funds mentioned in paragraph 2.2, five Trading Funds, the Exchange Fund, the Hong Kong Housing Authority, and 59 other funds. Appendix A is a list of these 75 accounts. The resources deployed to regularity audits represented 30% of Audit's available resources. The amount involved constituted only a very small percentage (i.e. 0.015%) of the Government's total expenditure.



Report of the Director of Audit on the Accounts of the Government of the HKSAR for the year ended 31 March 2004

Meeting increasing workload with less resources

2.9 In recent years, the Government has had substantial fiscal deficits. The Government is committed to eliminating its fiscal deficits by 2008-09, and the annual operating expenditure of the public sector will be gradually reduced to the \$200 billion level

by 2008-09. Government departments (including Audit) and other public sector organisations are required to achieve significant savings during 2004-05 to 2008-09. In order to achieve the savings required by the Government, the Commission has to try its best to work with less resource while ensuring that essential services are not affected.

2.10 However, our regularity audit workload has been increasing because of:

- (a) ***Widening expectation gap.*** In overseas countries, a number of high-profile corporate failures and frauds (e.g. “Enron” case in the USA) in recent years have widened the expectation gap as to how far the auditors’ role should go in carrying out financial audits. There is increasing demand for reducing the risk of major frauds in the use of public funds. As a result, our regularity audit work has become more demanding; and
- (b) ***Additional and complex workload.*** Audit has to cope with additional and complex workload from the Government’s adoption of accrual accounting (see paras. 2.11 to 2.13) and the implementation of a new Government Financial Management Information System (GFMIS — see paras. 2.14 and 2.15).

Implementation of accrual reporting in the Government

2.11 The financial statements of the GRA and the eight funds (see para. 2.2) are prepared on the conventional cash basis, which recognises transactions only at the time when cash is received or paid. In 1999, Audit conducted a VFM audit review on the financial reporting framework of the Government, which was reported in the [Director of Audit’s Report No. 33 of October 1999](#). Audit recommended that the Government should expedite action on deciding whether or not to adopt accrual accounting, which recognises transactions at the time when they occur.

2.12 In 2001, the Financial Secretary announced in the 2001-02 Budget Speech that starting with the financial year for 2002-03 the Government would publish two separate sets of annual accounts, one under the existing cash accounting convention and another on the accrual basis. The implementation of accrual reporting is a key initiative of the Government for improving its financial accountability and transparency.

2.13 The [Government’s accrual-based Consolidated Statement of Financial Position and Consolidated Statement of Financial Performance for 2003-04](#) reported a number of assets and liabilities, e.g. investments in government business enterprises (\$171 billion), fixed assets of the Hong Kong Housing Authority (\$120 billion), pension liabilities (\$321 billion) and provision for untaken leave (\$20 billion). Starting with the accrual-based financial statements for 2004-05, government-owned fixed assets and their depreciation would be reported. The Government’s adoption of accrual accounting will have wide ramifications on our regularity audit work.

Implementation of the GFMIS

2.14 In June 2003, the Treasury commenced a project to implement a new computer system GFMIS to replace some of its existing computer systems and processes. One of the objectives of the GFMIS is to support the implementation of accrual reporting. It is a set of modern, web-based accounting and financial management software. There are four core modules, namely costing/operating accounts module, reporting module, accrual module and cash ledger. The GFMIS project would be implemented by phases in the near future.

2.15 The GFMIS would involve some 80 bureaux and departments and about 5,400 users spread around different geographical locations in Hong Kong. It is a complex system, based on whole-of-government business processes, application design and integration requirements. It is a large-scale system implementation in the Government, facing a wide range of requirements and expectations of many different stakeholders. The Government's implementation of the GFMIS has a significant impact on our regularity audit work.

Revision of Audit Manual

2.16 Audit has all along been keeping its audit methodology under review, with incremental changes being made from time to time to align its audit methodology with best practices of the profession and to improve the efficiency and cost-effectiveness of its audit work. In 2004, Audit commenced a comprehensive revision of its Audit Manual. The new Audit Manual will comprise three separate volumes, namely Volume I — General Audit Manual (GAM), Volume II — Regularity Audit Manual (RAM) and Volume III — Value for Money Audit Manual (VAM).

2.17 The consultation of the draft GAM was completed. GAM would be promulgated in early 2005. The two other Manuals (RAM and VAM) are under compilation and are expected to be completed by September 2005. These two Manuals will provide our staff with more guidance on regularity and VFM audit work.

Improving organisation and grade structures

2.18 In 2004, Audit conducted comprehensive reviews of its organisation structure and of its grade structure, since both of them had remained unchanged for many years. Upon completion of the reviews in late 2004, Audit decided to implement two key initiatives to improve its organisation and grade structures, namely the reorganisation of the Commission (see paras. 2.19 to 2.23) and the merger of the Auditor and Examiner grades (see paras. 2.24 to 2.26).

Reorganisation of the Commission

2.19 At present, each Division is responsible for performing both regularity audit and VFM audit for a set of government policy areas. In addition to regularity and VFM audit work, the Headquarters Administration Division is also responsible for departmental

administration, technical and special duties, computer audit, the Director of Audit's report production work, and other support services.

2.20 In 2004, the Directorate Meeting discussed the reorganisation issue, having regard to the organisation structures of major overseas national audit offices. It was agreed in principle that Audit should move toward more specialisation of work. Possible options of reorganisation were explored in consultation with the Division Heads. The Directorate Meeting endorsed the final reorganisation proposal which was issued for staff consultation. In January 2005, two briefing sessions were held for the Auditor and the Examiner grade staff respectively. Based on their feedback, our staff generally supported the proposal to set up new specialised Divisions, each responsible for only one core business (i.e. regularity audit, VFM audit, or corporate services).

2.21 In devising the reorganisation proposal, Audit followed the guiding principle that the new organisation structure had to help build up staff expertise in the respective audit areas, and enhance efficiency and productivity of work. After the reorganisation, the existing five Divisions (see para. 2.19) would be replaced by six new specialised Divisions, namely one Corporate Services Division, one Regularity Audit Division, and four VFM Audit Divisions. The new organisation structure will take effect from 1 September 2005.

2.22 Each of the six new Divisions will be specialised in one core business: the Regularity Audit Division in regularity audit; each VFM Audit Division in VFM audit of a set of government policy areas; and the Corporate Services Division in corporate services, including departmental administration, the Director of Audit's report production work, and other support services.

2.23 Audit believes that both its staff and management will reap the benefits of having specialised Divisions. For the staff, specialisation of work will help them better focus their efforts and develop their expertise in the respective audit areas. For the management, with more specialisation and increased professionalism, the new organisation structure will enable Audit to better meet the challenges ahead.

Merger of the Auditor and Examiner grades

2.24 As at the end of 2004, Audit had an establishment of 185 posts, consisting of the directorate grade (13 posts or 7%) and the non-directorate grade, i.e. the Auditor grade (45 posts or 24%), the Examiner grade (88 posts or 48%) and the clerical and other supporting grades (39 posts or 21%). The Auditor and Examiner grades had 133 posts (72%). In the review of its grade structure, Audit conducted research on grade structures of major overseas national audit offices and other professional departments in the Hong Kong civil service. A working group chaired by an Assistant Director of Audit was formed for the review of grade structure. It was proposed that the existing grade structure should be simplified by combining the Auditor and the Examiner grades. The benefits of the merger proposal include improving career prospect of grade members, boosting staff morale, and streamlining grade management and structure.

2.25 In devising the merger proposal, two guiding principles were followed: cost neutrality (i.e. maintaining the same staff cost) and flexibility (for the management to conduct, if necessary, direct recruitment of staff with specialised knowledge and experience at the professional level from the private sector). The proposal formulated by the working group was endorsed at a Directorate Meeting. The existing and proposed grade structures are shown below.

Existing and proposed grade structures			
Existing structure		Proposed structure	
Grade	Rank	Grade	Rank
Auditor	Senior Auditor	Auditor	Senior Auditor
Examiner	Auditor	Auditor	Senior Assistant Auditor
	Chief Examiner		
	Senior Examiner		
	Examiner		Assistant Auditor

2.26 In January 2005, two briefing sessions were held for the Auditor and the Examiner grade staff respectively. Based on their initial feedback, our staff supported in principle the merger proposal. The working group will finalise departmental recommendations having regard to views from grade members. Consultations with staff associations will continue. The implementation of the merger proposal is subject to the advice of the Civil Service Bureau and the Advisory Body on Civil Service Salaries and Conditions of Service, and the approval of the Establishment Sub-committee of LegCo. While a definite timetable for the merger had not been worked out, Audit would implement the grade restructuring as soon as practical.

Looking ahead

2.27 Audit is facing a number of major challenges in its regularity audit work, including the reduction in resources, the widening expectation gap on the role of auditors, the great changes brought about by the implementation of accrual reporting in the Government, and the replacement of the existing computerised ledger accounting system by the new GFMIS. Audit would do its utmost to meet these challenges by improving the quality, efficiency and cost-effectiveness of its regularity audit work. For this purpose, we have been implementing a number of major initiatives, including the comprehensive revision of the Audit Manual (see paras. 2.16 and 2.17), the reorganisation of the Commission (see paras. 2.19 to 2.23), and the proposed merger of the Auditor and Examiner grades (see paras. 2.24 to 2.26).

2.28 We are pleased that most of the above tasks were well underway in 2004. However, a lot of work remains to be done in the year ahead. We expect that by September 2005, the revision of the Audit Manual and the reorganisation will be completed. With the establishment of a new Division specialised in regularity audit work and the promulgation of a new RAM, our regularity audit work will be more effective.

CHAPTER 3: VALUE FOR MONEY AUDIT

Introduction

3.1 The aim of VFM audits is to provide LegCo with independent information, advice and assurance about the economy, efficiency and effectiveness with which any audited body (i.e. bureau/department of the Government, agency, other public body, public office or audited organisation) has discharged its functions.

3.2 The terms “economy”, “efficiency” and “effectiveness” can be interpreted as follows:

- (a) ***Economy.*** It is concerned with minimising the cost of resources used for an activity having regard to appropriate quality;
- (b) ***Efficiency.*** It is concerned with the relationship between outputs, in terms of goods, services or other results, and the resources used to produce them; and
- (c) ***Effectiveness.*** It is concerned with the extent to which objectives have been achieved and the relationship between the intended impacts and actual impacts of an activity.

3.3 VFM audit is carried out under the VFM Audit Guidelines tabled in the Provisional Legislative Council in 1998 (see para. 1.19). The Guidelines also provide for the submission of the Director of Audit’s reports on the results of VFM audits to the President of LegCo, the tabling of these reports, the consideration of these reports by the PAC, and the tabling of the Government Minutes (see para. 1.20). Like regularity audit, VFM audit is conducted in accordance with the Audit Commission auditing standards (see para. 2.3) and a programme of work determined annually by the Director of Audit (see para. 2.4). A structured approach is adopted for conducting VFM audit, which consists of three main stages, namely the planning stage, the investigation stage and the reporting stage.

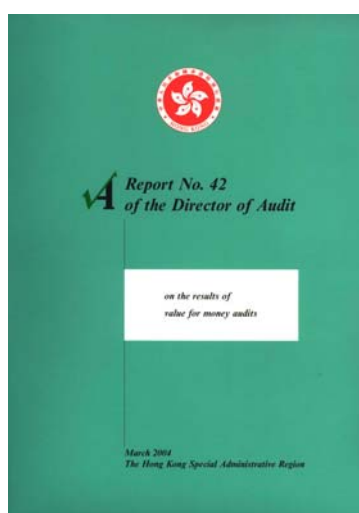
3.4 In conducting VFM audit under the VFM Audit Guidelines, the Director of Audit is entitled to exercise the powers given to him under the Audit Ordinance. However, he may not question the merits of the policy objectives, though he may question the economy, efficiency and effectiveness of the means used to achieve them.

The year under review

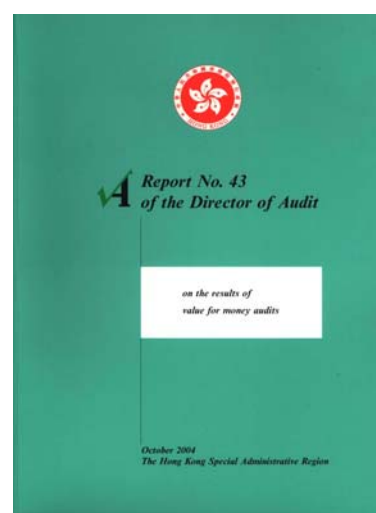
3.5 In 2004, two Director of Audit’s Reports on the results of VFM audits were issued in March (Report No. 42) and October (Report No. 43), covering a total of 21 audit subjects. The [Director of Audit’s Report No. 42](#) has ten subjects while the [Director of Audit’s Report No. 43](#) has 11 subjects. The resources deployed to VFM audits represented

70% of Audit's available resources. The amount involved constituted only a very small percentage (i.e. 0.035%) of the Government's total expenditure.

3.6 The PAC continued to show great interest in the audit subjects in these two reports. The following are examples of audit subjects, which put the issues of public governance and accountability in the limelight.



The Director of Audit's Report No. 42 of March 2004



The Director of Audit's Report No. 43 of October 2004

Examples of subjects reported in the Director of Audit's Report Nos. 42 and 43

Subject	Report No.	Chapter No.
Hong Kong Harbour Fest	42	4
Government subsidies to the English Schools Foundation	43	3
Corporate governance and Headquarters administration of the English Schools Foundation	43	4
School administration of the English Schools Foundation	43	5
Grant of land at Discovery Bay and Yi Long Wan	43	6

The PAC selected these subjects for public hearing and examined intensively a large number of issues raised in the audit reports. The audit conclusions and recommendations were generally accepted by the PAC and the Administration. Like the VFM audit reports issued in past years, these two reports were well received by the media and the public. Some of the audit subjects hit the headlines of newspapers. In general, the comments received from the media and the public were very favourable. The above five audit subjects are briefly described in paragraphs 3.7 to 3.20.

Harbour Fest review

3.7 **Background.** On 30 May 2003, the Finance Committee of LegCo approved \$1 billion for a campaign to relaunch Hong Kong's economy after the Severe Acute Respiratory Syndrome crisis. On 5 June 2003, the organiser proposed to organise an entertainment festival (the Harbour Fest) in October and November 2003. On 12 July 2003, a maximum of \$100 million was approved for this project. The objectives of organising the Harbour Fest were to boost morale in Hong Kong and to get the local economy growing again by boosting local consumption and tourism.

3.8 **Audit review.** The audit review covered a number of areas, including project conceptualisation and approval, project monitoring, and organisation and evaluation of the Harbour Fest. The Harbour Fest, comprising a series of 16 concerts, was staged from 17 October to 9 November 2003. For the 16 concerts as a whole, the total number of tickets sold was 43% of the total capacity. For individual concerts, the corresponding figures ranged from 15% to 89%.

3.9 Audit found that the Government, in its keenness to revive the economy of Hong Kong, had deviated from essential management principles in its monitoring of the Harbour Fest project. The Administration took note of the lessons to be learned, and generally accepted the audit recommendations.

3.10 After four public hearings in May 2004, the PAC concluded that, among other things:

- (a) the Government had put a substantial amount of public funds at risk as early as the inception stage of the event by approving too hastily the organiser's proposal for the Government to sponsor the Harbour Fest; and
- (b) the responsible government official, among other things:
 - (i) failed to adhere to the basic management principles and to put in place an appropriate system of cost control or monitoring to oversee the project; and
 - (ii) failed to discharge his responsibility to keep LegCo informed by providing reliable and complete information in a timely manner.

The PAC recommended taking disciplinary action against the responsible government official. The Administration accepted this recommendation.

3.11 **Essence of public accountability.** The Harbour Fest attracted much media attention. This case highlighted the essence of public accountability — i.e. government officials, who are entrusted with public resources, are answerable for the fiscal, managerial and programme responsibilities that are conferred.

English Schools Foundation review

3.12 **Background.** The English Schools Foundation (ESF) was established under the English Schools Foundation Ordinance (Cap. 1117) in 1967. It operates 15 primary and secondary schools which receive recurrent government subsidies (\$299 million in the 2002-03 school year, representing 29% of the ESF income), and one primary school without such subsidies.

3.13 **Audit review.** The ESF review comprised three audit subjects:

Audit areas of the three ESF audit subjects

	Subject	Audit areas
1	Government subsidies to the ESF	Reviews of government subsidies to ESF schools and international schools.
2	Corporate governance and Headquarters administration of the ESF	Corporate governance, staff remuneration and recruitment, staff housing and medical benefits, etc.
3	School administration of the ESF	Corporate governance of schools, strategic planning, budgeting and cash management, etc.

3.14 The PAC held five public hearings to consider these three audit subjects. In particular, three hearings were conducted for the second subject. The audit review led to improvements in a number of areas, including issues about corporate governance and staff remuneration:

- (a) **Corporate governance.** In the ESF audit, Audit made some useful recommendations for improvement in the corporate governance of the ESF. For example, in response to Audit's observation that the membership size of the Foundation (i.e. the supreme governing body of the ESF) of 132 was large, the ESF proposed to make a restructuring, which included replacing the Foundation by the ESF Council with no more than 25 members; and
- (b) **Staff remuneration.** Audit found that the estimated average annual remuneration per ESF teaching staff member was the highest when compared with the corresponding figures of seven other largest local international schools. In this regard, the ESF's Remuneration Study Group, which was established to conduct reviews of the remuneration packages of ESF teaching staff, would make a report to the Executive Committee of the Foundation in June 2005. The Group's report would also be forwarded to the PAC.

3.15 **The question of auditability.** As mentioned in paragraph 3.12, the ESF received 29% of its income from public moneys, i.e. less than half of its income. According to the VFM Audit Guidelines (see para. 1.19), the Director of Audit may carry out a VFM audit of an audited organisation, including any organisation which receives more than half its income from public moneys. The ESF therefore did not satisfy this requirement. However,

the VFM Audit Guidelines also state that the Director may carry out a VFM audit of an organisation which receives less than half its income from public moneys by virtue of an agreement made as a condition of subvention. In March 2004, the Chairman of the Foundation informed the Government that the Executive Committee of the Foundation had decided, by way of mutual agreement with the Government and as a condition of subvention, to welcome the Director of Audit to perform VFM audits of the ESF. The ESF therefore became an audited organisation under the VFM Audit Guidelines.

Discovery Bay review

3.16 **Background.** In the 1970s, the Government granted land for holiday resort and residential developments at Discovery Bay and Yi Long Wan of Lantau Island. The Discovery Bay development covers an area of about 6,152,000 square metres and the Yi Long Wan development covers about 28,000 square metres. The Discovery Bay development is still in progress.

3.17 **Audit review.** The audit review covered four areas, including the change in concept of the Discovery Bay development, the provision of facilities in the Discovery Bay development, the changes in Master Layout Plans (MLPs) and premium implications, and the site boundaries of the Discovery Bay and Yi Long Wan developments.

3.18 A retired senior government official was invited to attend a PAC public hearing to give evidence on many issues, in particular the change in concept of the Discovery Bay development. The original concept and its change are as follows:

- (a) **Original development concept.** In December 1973, the Executive Council (ExCo) was informed that the basic concept of the development was to create a self-contained recreation and leisure community with a wide variety of recreational facilities. In 1976, having considered the lease conditions, ExCo advised and the then Governor ordered that the land at Discovery Bay should be granted to a developer for a holiday resort and residential/commercial development at a premium of \$61.5 million. In April 1977, ExCo was informed that the conditions allowed for low density development which, at the maximum, would provide over 401,342 square metres of residential resort accommodation and 140,284 square metres of hotel accommodation; and
- (b) **Change in development concept.** According to the lease conditions, the site should be developed in accordance with an MLP. In September 1977, MLP 4.0 was submitted, in which the developer requested that: the hotel gross floor area (GFA) would be reduced to 32,000 square metres; the resort accommodation GFA would be deleted; and housing accommodation GFA of 524,000 square metres would be added. In 1978, the Government approved the MLP 4.0. In July 1985, the Authorised Person for the development suggested to the Government that the surplus hotel and commercial GFA should be exchangeable for residential GFA on a one to one basis. He said that his proposal retained the concept of developing a first-home residential community (with access to recreational facilities in a natural environment). This submission raised the question as to whether the case should be reported to ExCo because the

development was very much less of a tourist resort and more of a typical residential development. It was decided to refer the case to the then Land Development Policy Committee first, and then to ExCo, if necessary. In October 1985, the then Development Progress Committee agreed that the proposal to change the overall concept of the development would not require formal approval.

3.19 After the hearings, the PAC recommended that the Government should expeditiously seek ExCo's endorsement of the change in concept of the Discovery Bay development.

3.20 ***No time limit for public accountability.*** The Discovery Bay case brought into the limelight governance issues on the decision-making process right at the most senior level of the Administration about a quarter of a century ago. It also showed that in cases involving matters of principle or material public funds, these will be subject to audit, for reasons of public accountability, even though the events may have happened a long time ago. The following are some special features of this audit review:

- (a) ***Events took place a long time ago.*** The Discovery Bay events spanned about a quarter of a century. The then Chief Secretary who attended a PAC public hearing (see para. 3.18), had expressed difficulties in recalling some of the details that took place over 25 years ago;
- (b) ***PAC hearings were spread over a long period of time.*** Among the audit subjects included in the Director of Audit's reports in 2004, this subject had the longest hearing period, with four public hearings spread over a five-week period in December 2004 and January 2005; and
- (c) ***Former government official attended a hearing after having retired for years.*** A former senior government official attended a PAC public hearing, although he had retired for over 17 years (see para. 3.18).

Looking ahead

3.21 Similar to regularity audit work (see para. 2.27), our VFM audit work is also facing the challenges of the reduction of resources and the widening expectation gap on the role of auditors. Despite the reduction of resources available for VFM audit, there has been growing public expectation for Audit to conduct more complex and high-impact VFM studies.

3.22 To meet these challenges, Audit is conducting a comprehensive revision of its Audit Manual (see paras. 2.16 and 2.17) to provide more guidance to its staff. Audit is also undergoing a major reorganisation with the establishment of specialised Divisions to handle regularity audit, VFM audit and corporate services separately (see paras. 2.19 to 2.23). We expect that a new VAM (see para. 2.16) will be promulgated before the new organisation structure takes effect on 1 September 2005. Upon completion of these initiatives, our VFM audit work will be much enhanced.

CHAPTER 4: CORPORATE SERVICES

Introduction

4.1 The Headquarters Administration Division of the Commission is responsible for the provision of corporate services, which include departmental administration, the Director of Audit's Report production work, translation services, technical audit, quality assurance, external and press relations, executive support, training, grade and personnel management, LAN administration, IT support, and other support services.

4.2 These corporate and support services are provided, among other things, to facilitate smooth operation of the Commission, as well as to maintain harmonious and effective relationships with its stakeholders.

The year under review

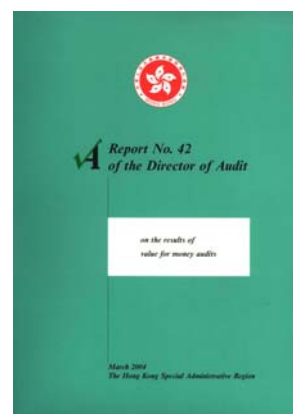
4.3 The year 2004 was eventful for those involved in the provision of corporate services. It was a busy but fruitful year. We stepped up efforts to improve our organisation and capability. More training and public relations work was conducted. The key initiatives, which we commenced in the year, would have far-reaching effects on our work. Our corporate services work included:

- (a) The Director of Audit's Report production work — Reports No. 42 and 43;
- (b) Support services:
 - (i) Corporate Plan;
 - (ii) Audit history;
 - (iii) Environmental Report;
 - (iv) Media research; and
 - (v) IT support;
- (c) External and press relations:
 - (i) Public relations work;
 - (ii) Speeches and presentations by the Director of Audit;
 - (iii) Participation in the 18th Congress of the International Organisation of Supreme Audit Institutions (INTOSAI);
 - (iv) Receiving visitors from Mainland China and overseas; and

- (v) Secondment from the Audit Commission of Macao;
- (d) Training and development:
 - (i) Local training and development programmes; and
 - (ii) International seminars and training programmes; and
- (e) Key initiatives:
 - (i) Revision of the Audit Manual;
 - (ii) Reorganisation of the Commission; and
 - (iii) Proposal to merge the Auditor and Examiner grades.

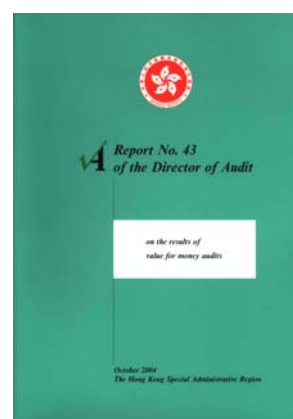
***The Director of Audit's Report production work
— Reports No. 42 and 43***

4.4 The Director of Audit's Reports No. 42 and 43 were issued in March and October 2004. They include the results of VFM audits completed during the period October 2003 to February 2004 and the period March to September 2004 respectively. The Director of Audit signed Report No. 42 on 2 April 2004 and Report No. 43 on 29 October 2004.



**The Director of Audit's
Report No. 42 of March
2004**

4.5 Report No. 42 was tabled in LegCo on 21 April 2004. It contains ten subjects, five of which were considered by the PAC during their public hearings held in May 2004. Report No. 43 was tabled in LegCo on 24 November 2004. It contains eleven subjects, five of which were considered by the PAC during their public hearings held in December 2004 and January 2005. The audit recommendations were generally accepted by the Administration. The Director of Audit's Reports are available on our website at http://www.aud.gov.hk/eng/pubpr_arpt/rpt.htm.



**The Director of Audit's
Report No. 43 of October
2004**

Corporate plan

4.6 The Corporate plan, which covers the three-year period 2004-05 to 2006-07, was issued in June 2004. It is the key document to communicate Audit's long-term objectives and strategies to its stakeholders. It outlines our Vision, Mission and Values (see Appendix B), as well as the key result areas on which we focus our efforts in the delivery of audit services.

4.7 The Corporate Plan is supported by the annual Business Plan and other work plans, including the Five-year VFM Audit Strategic Plan and the annual Programme of Work (POW). The Business Plan 2004-05, which was also issued in June 2004, set out the broad directions for conducting our core businesses and the key initiatives planned for the audit year September 2004 to August 2005. The Five-year VFM Audit Strategic Plan and the annual POW were then prepared to translate the initiatives set out in the Business Plan into detailed work programmes, the completion of which would contribute to the achievement of the key results which we aimed to achieve. Appendix C shows the key indicators of the Commission.

4.8 The Corporate Plan is available on our website at http://www.aud.gov.hk/eng/aboutus/about_corp.htm.

Audit history

4.9 In 2004, we celebrated the 160th anniversary of the Commission. We took the opportunity to conduct a thorough research on the development of government audit in Hong Kong over the past 160 years (see Chapter 1). Information on Audit history has been uploaded to our website at http://www.aud.gov.hk/eng/aboutus/about_history.htm.

Environmental Report

4.10 Starting from 2001, an annual Environmental Report has been issued to help promote environmental protection. The Environmental Report 2004 was the 4th report we issued. The environmental policy of the Audit Commission is that it is committed to ensuring that its operations conform to environmental protection principles and promote environmental protection practices. To help promote environmental protection, Audit:

- (a) adopts green housekeeping practices; and
- (b) carries out VFM audits on selected government activities which have a significant environmental impact and on related environmental issues, with a view to highlighting areas for improvement in the implementation of Government's environmental improvement policies.

4.11 The Environmental Report 2004 is available on our website at http://www.aud.gov.hk/eng/otherinfo/info_envrpt.htm.

Media research

4.12 We conducted media research on a daily basis (e.g. newspaper clippings) to keep in view possible audit issues reported in the media. We also collected useful feedback (e.g. media comments and views from the public) on our published VFM audit reports.



Newspaper clippings on the VFM audit of the ESF



Newspaper clippings on the VFM audit of the Harbour Fest



Newspaper clippings on the VFM audit of the Discovery Bay

IT support

4.13 Our Departmental IT Plan for the period 2004-05 to 2005-06 was issued in June 2004. The IT Plan:

- (a) takes stock of our IT facilities and of our progress in implementing IT tasks identified;
- (b) identifies areas where IT potential can be further exploited to enhance efficiency; and
- (c) sets out the IT tasks to be implemented in the period covered by the Plan.

4.14 In 2004, we launched the new Project Accounting and Management System (PAMS) to replace our Job Accounting System. PAMS records the budgeted and actual man-hours spent by audit staff on work items, and provides management information for job

monitoring and forward planning. We also revamped Audit's Internet Homepage for launching in the first quarter of 2005.

Public relations work

4.15 A key focus in the past year was the stepping up of efforts on our public relations work targeted at different stakeholder groups. The following are some of the key events:

- (a) the Association of Chartered Certified Accountants (ACCA) held their Spring Dinner on 9 February 2004. Our Director was invited to join the dinner and exchange views with professional accountants;



The ACCA Spring Dinner on 9 February 2004



The 16th Anniversary Dinner of the HKAAT on 13 May 2004

- (b) the Hong Kong Association of Accounting Technicians (HKAAT) held its 16th Anniversary Dinner cum Membership Launch at World Trade Centre Club Hong Kong on 13 May 2004. Our Director was invited to join the annual dinner;
- (c) the Hong Kong Institute of Certified Public Accountants (HKICPA) held its Annual Dinner in the InterContinental Ballroom on 25 November 2004. Our Director was invited to join the annual dinner and exchange views on matters of mutual interest;



The HKICPA Annual Dinner on 25 November 2004



Group photo taken at the HKAAT Annual Dinner on 27 January 2005

- (d) the HKAAT held its Annual Dinner and Prize Presentation Ceremony on 27 January 2005 at the JW Marriott Hong Kong. Our Director was invited to join the ceremony and exchange views with members of the Association;
- (e) the ACCA held its Spring Dinner on 22 February 2005. Mr Ying Kwok Wing, Assistant Director of Audit represented the Commission to join the dinner and share ideas and knowledge with professional accountants;
- (f) the Association of International Accountants – Hong Kong Branch (AIA) held its 2005 Annual Dinner on 23 March 2005 at the Hong Kong Bankers Club. Our Director was invited to attend the dinner as guest and to exchange views with the members of the Association;



The 2005 AIA Annual Dinner on 23 March 2005

- (g) our Director and his senior staff conducted a briefing on the work of Audit to the newly-appointed PAC Members in a luncheon at the Hong Kong Jockey Club on 18 November 2004; and
- (h) our Director took part in a number of media interviews and radio phone-in programmes:
 - (i) Cable TV on 7 May 2004 in the program of “飛常政經” (“Allen Lee Show”);
 - (ii) RTHK on 19 June 2004 in the program of “[香港家書](#)” (“Hong Kong Letter”); and
 - (iii) TVB on 13 January 2005 in the program of “新聞透視” (“News Magazine”).

Speeches and presentations by the Director of Audit

4.16 In the period January 2004 to March 2005, our Director delivered a number of speeches and presentations on subjects related to our work to various government departments and professional bodies. The following are some of the key events:

- (a) Speech by the Director of Audit on “Governance Issues at Government Departments” to the Management Consultancies Association of Hong Kong (MCA) at its Luncheon Meeting on 16 November 2004;



The MCA Luncheon Meeting on 16 November 2004

- (b) Presentation by the Director of Audit on “Value for Money Audit” to the Canadian Certified General Accountants Association of Hong Kong (CGA) on 2 December 2004;

- (c) Speech by the Director of Audit on “Governance and Accountability — The Role of the Public Auditor” to the Hong Kong Institute of Directors at its Luncheon Meeting on 26 January 2005;

- (d) Presentation by the Director of Audit on “Value for Money Audit Work of the Audit Commission” to the senior staff of the Government Property Agency (GPA) at its Experience Sharing Forum on 23 February 2005; and



The Spring Cocktail Reception of the HKICPA on 8 March 2005

- (e) Speech by the Director of Audit on corporate governance and public accountability at the Spring Cocktail Reception of the HKICPA on 8 March 2005.

Participation in the 18th Congress of INTOSAI

4.17 At the invitation of the National Audit Office of the People’s Republic of China (CNAO), Mr Benjamin Tang, Director of Audit and Mr John Chu, Senior Auditor (Research and Development) attended the 18th INTOSAI Congress, as members of the China delegation which was headed by the Deputy Auditor General of the CNAO, Dr Liu Jiayi. The Head of the Macao Audit Commission, Ms Fatima Choi was also a member of the delegation. The 18th INTOSAI Congress was held in Budapest, the capital city of Hungary, from 11 to 16 October 2004.

4.18 The participation of the Audit Commission in the Congress was very useful in helping us keep abreast of the developments of international public sector auditing. It also provided a good opportunity for us to exchange views and share good practices with our counterparts in the CNAO, the Macao Audit Commission and other overseas national audit offices.



The First General Plenary Session of the 18th INTOSAI Congress (From left to right: Mr Benjamin Tang, Director of Audit; Dr Liu Jiayi, Deputy Auditor General of the CNAO; and Ms Fatima Choi, Head of the Macao Audit Commission)



Hong Kong representatives at the 18th INTOSAI Congress: Mr Benjamin Tang, Director of Audit (right) and Mr John Chu, Senior Auditor (left)

Receiving visitors from Mainland China and overseas

4.19 In the period January 2004 to March 2005, Audit held a number of seminars for visitors from different provinces of Mainland China. These visits strengthened our linkage with our counterparts in Mainland China. The key events are as follows:

- (a) on 14 May 2004, a delegation comprising some 20 officials from the Audit Bureau of Hai Kou, Hai Nan, led by Mr WANG Li-wen, Vice Director, visited the Audit Commission. Our staff briefed the delegation on the organisation and work of Audit. The delegates showed great interest in our work;



Delegation from the Audit Bureau of Hai Kou, Hai Nan visited our office



Delegation from the Jiangsu Provincial Government attended the seminar in PolyU

- (b) on 30 June 2004, at the invitation of the Hong Kong Polytechnic University (PolyU), our staff delivered a talk on the topic “financial audit system in the Government of Hong Kong” at the campus of the PolyU. The talk was part of a two-week training programme organised jointly by the China Business Centre of the PolyU and the Personnel Department of Jiangsu Provincial Government in mid June 2004. On that day, our staff briefed some 30 participants of the training program from various offices in the Mainland on Audit’s work;

- (c) on 5 August 2004, a delegation from the Nanjing Audit University visited our office. The visit was arranged at the request of Deloitte Touche Tohmatsu (Deloitte) as part of its training programme for the University in early August. Our staff briefed the delegates on the organisation and the main work of Audit. The delegates showed great interest in the work of Audit;



Delegation from the Nanjing Audit University visited our office

- (d) Audit was invited separately by the HKU School of Professional and Continuing Education (HKU SPACE) and the PolyU to deliver a talk in their training programmes in late August 2004. The participants of the training programmes organised by the PolyU and the HKU SPACE were from the Finance Department of Panyu and the Audit Department of Guangzhou Provincial



Delegations from the Finance Department of Panyu and the Audit Department of Guangzhou Provincial Government attended the seminar in the HKU SPACE

Government respectively. On the morning of 24 August 2004, the participants of the two training programmes gathered together at the campus of the HKU SPACE to attend a briefing held by our staff on the role of Audit and the conduct of VFM audits;

- (e) on the morning of 26 August 2004, at the invitation of the HKU, our staff held a seminar on the topic “the role of the Audit Commission and the conduct of VFM audits” at the Knowles Building in the HKU campus for a delegation from the Jiangsu Audit Bureau. To enable the participants to gain a better understanding of VFM audit, our staff quoted some audit cases at the seminar. The responses of the participants were very encouraging;



Officials from the Jiangsu Audit Bureau attended the seminar in the HKU

- (f) on 7 January 2005, a study tour on VFM audit from the Tianjin Audit Bureau and three officials from three different Government offices in Shenzhen visited our office. Our staff gave them a presentation on Audit’s work. A very constructive exchange on various aspects of auditing was made between the visitors and our staff; and



Study tour on value for money audit from the Tianjin Audit Bureau visited our office

- (g) on the morning of 2 March 2005, a seminar on “The work of the Audit Commission” was held for a group of senior officials from the Office of the Auditor General (OAG) of Thailand. An exchange of ideas and experiences of auditing was made between the visitors and our senior staff.



Presentation to the senior officials from the OAG of Thailand



Group photo taken after the presentation

Secondment from the Audit Commission of Macao

4.20 Miss Susana To of the Macao Audit Commission started her six-month secondment to our office in early November 2004. She was deployed to the Social Services Division in the first three months, and then to the Works and Lands Division in the second half of secondment period.



Miss Susana To of the
Macao Audit Commission

Local training and development programmes

4.21 **English seminar.** We organised an English seminar on 8 January 2004 at the North Point training centre of the CSTDI. The objective of the English seminar was to improve the written English and report writing skills of our staff. Over 50 Directorate and Auditor grade staff attended the seminar. Colleagues found the seminar very useful in enriching their English writing skills.

4.22 **Leadership Enhancement and Development Programme.** Mr Wong Kau-on, Peter, Assistant Director of Audit was nominated to attend the Leadership Enhancement and Development Programme from 14 to 19 November 2004. The programme was conducted by the John F Kennedy School of Government, Harvard University and the course was held at the Hong Kong University of Science and Technology. It aimed to enhance the leadership and strategic management capacities of the top echelon of the civil service, focusing particularly on the evolving role of the civil service and methods of promoting public acceptance of government policy.

4.23 **Civil Service Advanced Management Programme.** Mr Wong Ying-tao, Peter, Principal Auditor was nominated to attend the Civil Service Advanced Management Programme organised by the Civil Service Training and Development Institute (CSTDI). The programme, which was held at the Poon Kam Kai Institute of Management of the HKU, was divided into six modules and each module was held within two to three days in the period April to November 2004.

4.24 **Leadership in Action Programme.** Two staff members, Mr Albert Wong, Acting Principal Auditor and Mr John Chu, Senior Auditor, were nominated to join the Leadership in Action (LIA) Programme organised by the CSTDI. This three-week training programme aimed to help participants broaden their strategic horizons and develop a new and clear focus. Mr Chu attended the LIA 3 Programme in September 2004 and Mr Wong attended the LIA 4 Programme in March 2005.

International seminars and training programmes

4.25 ***The 2nd International Audit Training Programme held by the CNAO.*** Ms Viola Tse, Auditor of the Works and Lands Division attended the 2nd International Audit Training Programme held by the CNAO for a three-week period in April 2004. The training programme, which was held primarily at the Huairou Training Centre in Beijing, comprised three major components. First, there was a series of lectures and discussions on various aspects of government audit in China. Second, visits to field audit sites of the CNAO and famous scenic spots and historic sites in Beijing were arranged. Third, the participants were divided into five groups to visit the resident audit offices of the CNAO at five different cities (Nanjing, Shanghai, Guangzhou, Kunming and Chongqing). She was assigned to visit the Shanghai office with six other participants.



Lecture room at the Huairou Training Centre of the CNAO



“Indian Night”
(Ms Viola Tse: third from left at the back)

4.26 ***The 2nd International Seminar on Information Technology Audit in Nanjing organised by the CNAO.*** Mr Maurice Chun, Acting Senior Auditor and Miss Yvonne Ho, Audit Analyst of the Computer Audit Branch attended the 2nd International Seminar on IT Audit held by the CNAO in Nanjing from 1 September to 4 September 2004. 50 delegates from 16 countries attended the seminar. The seminar, which was held at the Nanjing Audit University, was divided into five sessions, namely Session I: Formulation of IT Auditing Standards, Session II: General Issues and Legal Environment of IT Audit, Session III: Use of Data in On-line Auditing, Session IV: Data Collection and Processing, and Session V: Other issues of the Concern of the Seminar Participants.

4.27 Hong Kong was selected to chair the first session on 1 September 2004. Mr Chun chaired the session and delegates from five countries presented their papers during the session. All the participants actively exchanged their views and experiences in the relevant subjects.



Group photo of the 2nd International Seminar on IT Audit



Mr Li Jin-hua, Auditor General of the CNAO (left) and Mr Maurice Chun, Acting Senior Auditor (right)

4.28 ***ASOSAI Seminar on Environmental Auditing.*** Mr Terence Li, Senior Auditor and Mr Jonathan Tse, Auditor of the Works and Lands Division attended the seminar hosted by Mr Li Jin-hua, Auditor General of the CNAO, in his capacity as the Chairperson of the ASOSAI Working Group on Environmental Auditing (WGEA). The seminar and the work meeting were held from 27 to 31 March 2005 in Wuyishan City of Fujian Province, China. In total, 41 participants coming from 23 countries and regions attended.

4.29 On 28 March 2005, Mr Li Jin-hua officiated the opening ceremony, followed by a group-photo taking session and a tree-planting ceremony.



Group photo taken at the tree-planting ceremony



Photo taken at the tree-planting ceremony (From left to right: Mr Terence Li, Mr Li Jin-hua, Ms Mok Lai-meng of the Macao Audit Commission, and Mr Jonathan Tse)

Key initiatives

4.30 In 2004, the Headquarters Administration Division was busy working on a number of key initiatives, including the comprehensive revision of Audit Manual (see paras 2.16 and 2.17), the reorganisation of the Commission (see paras. 2.19 to 2.23), and the merger of the Auditor and Examiner grades (see paras. 2.24 to 2.26).

4.31 ***Revision of the Audit Manual.*** The revision of our Audit Manual is a major exercise that requires a great deal of technical research work. In particular, the volume on regularity audit (i.e. RAM) will require the input of the new specialised Regularity Audit

Division (to be formally established upon our reorganisation). The current target is that the revision of the whole set of Audit Manual will be completed before the reorganisation takes effect on 1 September 2005.

4.32 ***Reorganisation and merger proposals.*** The management has been working on two major initiatives that will bring about changes to our organisational set-up and the grade structure of the Commission. Two forums were held on 5 January 2005 to brief staff members on the proposals to reorganise the Commission and to merge the Auditor and Examiner grades.

4.33 The Audit Commission Auditors Association and the Audit Commission Examiners Association issued questionnaires to their members to solicit their views on the reorganisation and merger proposals. In general, staff members agreed with the reorganisation, which will take effect on 1 September 2005. Staff members also agreed in principle with the merger proposal. More consultations with the staff associations about the merger proposal will continue in 2005, with a view to implementing the merger of the Auditor and Examiner grades as early as practicable.



Forum to brief staff members on the reorganisation and merger proposals on 5 January 2005

Looking ahead

4.34 In 2004, we made great efforts to step up our public relations work, improve our organisation and grade structures, and enhance staff training. In the year ahead, we will continue with these efforts. We expect that most of the key initiatives we commenced in 2004, including the revision of Audit Manual and the reorganisation of the Commission, will be completed by September 2005. All these efforts will help us continuously update our knowledge and upgrade our capacity, with a view to meeting the challenges facing us in the 21st century.

The 75 accounts certified in 2004-05

Government Funds

- (1) General Revenue Account
- (2) Capital Investment Fund
- (3) Capital Works Reserve Fund
- (4) Civil Service Pension Reserve Fund
- (5) Disaster Relief Fund
- (6) Innovation and Technology Fund
- (7) Land Fund
- (8) Loan Fund
- (9) Lotteries Fund

Trading Funds

- (10) Companies Registry Trading Fund
- (11) Electrical and Mechanical Services Trading Fund
- (12) Land Registry Trading Fund
- (13) Office of the Telecommunications Authority Trading Fund
- (14) Post Office Trading Fund

Statutory Funds

- (15) Exchange Fund
- (16) Hong Kong Housing Authority

Other Funds

- (17) AIDS Trust Fund

- (18) Bank deposits held under section 35/35A of the Insurance Companies Ordinance (Cap. 41)
- (19) Bankruptcy Estates Account
- (20) Brewin Trust Fund
- (21) Chinese Temples Fund
- (22) Companies Liquidation Account
- (23) Correctional Services Children's Education Trust
- (24) Correctional Services Department Welfare Fund
- (25) Customs and Excise Service Welfare Fund
- (26) Customs and Excise Service Children's Education Trust Fund
- (27) Director of Social Welfare Incorporated Accounts
- (28) District Court Suitors' Funds
- (29) Education Scholarships Fund
- (30) Emergency Relief Fund
- (31) Environment and Conservation Fund
- (32) Fire Services Department Welfare Fund
- (33) General Chinese Charities Fund
- (34) Government Flying Service Welfare Fund
- (35) Grant Schools Provident Fund
- (36) Grantham Scholarships Fund
- (37) High Court Suitors' Funds
- (38) Hong Kong Rotary Club Students' Loan Fund
- (39) Immigration Service Welfare Fund

- (40) Independent Commission Against Corruption Welfare Fund
- (41) J. E. Joseph Trust Fund
- (42) Kadoorie Agricultural Aid Loan Fund
- (43) Labour Tribunal Suitors' Funds
- (44) Language Fund
- (45) Legal Aid Services Council
- (46) Legislative Council Commission
- (47) Li Po Chun Charitable Trust Fund
- (48) Master in Lunacy Account
- (49) Minor Employment Claims Adjudication Board Suitors' Funds
- (50) Official Administrator's Account
- (51) Official Receiver in Bankruptcy Account
- (52) Official Receiver in Voluntary Arrangement Account
- (53) Official Solicitor's Accounts
- (54) Police Welfare Fund
- (55) Pneumoconiosis Ex Gratia Fund
- (56) Prisoners' Education Trust Fund
- (57) Prisoners' Welfare Fund
- (58) Quality Education Fund
- (59) Queen Elizabeth Foundation for the Mentally Handicapped
- (60) Samaritan Fund
- (61) Secretary for Home Affairs Incorporated Accounts

- (62) Sir David Trench Fund for Recreation
- (63) Sir Edward Youde Memorial Fund
- (64) Sir Robert Black Trust Fund
- (65) Small Claims Tribunal Suitors' Funds
- (66) Social Work Training Fund
- (67) Sing Tao Foundation Students' Loan Fund
- (68) Subsidised Schools Provident Fund
- (69) Supplementary Legal Aid Fund
- (70) MacLehose Fund
- (71) Traffic Accident Victims Assistance Fund
- (72) World Refugee Year Loan Fund
- (73) Fisheries Development Loan Fund
- (74) Poultry Trade Loan Fund
- (75) Loans to Poultry Wholesalers and Retailers affected by Avian Flu

Vision, Mission and Values

Vision

Excellence in public sector auditing

We strive for excellence in the provision of independent public sector audit services through commitment to professionalism and innovation.

Mission

To provide independent, professional and quality audit services to the Legislative Council and public sector organisations in order to help the Government enhance public sector performance and accountability in Hong Kong.

The primary objective of our audit services is to contribute to enhancing the performance and accountability of the Government and other public sector organisations in Hong Kong. We achieve our mission by:

- (a) conducting regularity audits which provide the Legislative Council with an overall assurance that the Government's financial and accounting transactions and those of funds of a public or quasi-public nature are proper and that they conform to accepted accounting standards; and
- (b) conducting value for money audits which provide the Legislative Council with independent information, advice and assurance about the economy, efficiency and effectiveness with which any bureau/department of the Government, agency, other public body, public office, or audited organisation has discharged its functions.

Values

We are committed to upholding a high standard of integrity and conduct in discharging our audit responsibilities. The following are the core values which all our staff members are expected to adhere to:

Independence

We strive to be, and be seen to be, objective, unbiased and free from undue influences in the provision of audit services.

Professionalism

We seek to achieve excellence by conducting our work with professional competence and expertise, in accord with the highest standards of ethics and proficiency in our professions.

Commitment

We are committed to adding value to public sector management by delivering quality audit services which serve the best interests of Hong Kong.

Innovation

We strive for continuous improvements by accepting, promoting and sharing creative and innovative ideas.

Objectivity

We are always fair, just and impartial in the conduct of our work.

Ethics and Integrity

We always act in an open, honest, ethical and professional manner.

Responsiveness

We always understand, acknowledge, and try our best to meet the needs and expectations of our stakeholders.

Key Indicators

	Unit	Target	2002-03 (Actual)	2003-04 (Revised Estimate)	2004-05 (Plan)
Regularity Audit					
Targets					
Number of Director of Audit's Reports submitted to the Legislative Council	Report	1	1	1	1
Time required to certify the statements of accounts of the Government after the end of each financial year	Month	7	7	7	7
Indicators					
Number of accounts certified	Account		75	75	75
Number of man-hours spent	Man-hour		98 028	98 137	102 129
Provision for regularity audit as % of total government spending	%		0.015	0.015	0.015
Value for Money Audit					
Targets					
Number of Director of Audit's Reports submitted to the Legislative Council	Report	2	2	2	2
Number of value for money audit reports issued to audited bodies	Report	18	21	19	18
Indicators					
Number of man-hours spent	Man-hour		187 530	178 137	166 989
Provision for value for money audit as % of total government spending	%		0.039	0.035	0.032

Calendar of key events
(1 January 2004 to 31 March 2005)

Date	Event
8 January 2004	An English seminar was held at the North Point training centre of the CSTDI.
9 February 2004	The Director of Audit attended the Spring Dinner of the Association of Chartered Certified Accountants.
2 April 2004	The Director of Audit's Report No. 42 was completed and signed.
21 April 2004	The Director of Audit's Report No. 42 was tabled in the Legislative Council.
April 2004	Audit staff attended the 2 nd International Audit Training Programme held by the National Audit Office of the People's Republic of China (CNAO) during a three-week period in April 2004.
7 May 2004	The Director of Audit took part in the program of “飛常政經” of the Cable TV.
13 May 2004	The Director of Audit attended the 16 th Anniversary Dinner cum Membership Launch of the Hong Kong Association of Accounting Technicians.
14 May 2004	A delegation comprising some 20 officials from the Audit Bureau of Hai Kou, Hai Nan visited our office.
20 May 2004	At the Directorate Meeting, it was agreed in principle that Audit should move toward more specialisation of work, in order to cope with the challenges arising from staff shortage problem and increasing public expectations for the delivery of quality audit services.
19 June 2004	The Director of Audit took part in the program of “香港家書” of the RTHK.
30 June 2004	Audit delivered a talk to the Personnel Department of Jiangsu Provincial Government.
June 2004	The Corporate plan, which covers the three-year period 2004-05 to 2006-07, was issued.
5 August 2004	A delegation from the Nanjing Audit University visited our office and a talk was delivered to them.
24 August 2004	Audit delivered a talk to the delegates from the Finance Department of Panyu and the Audit Department of Guangzhou Provincial Government.
26 August 2004	Audit held a seminar for a delegation from the Jiangsu Audit Bureau.

Appendix D
(Cont'd)

Date	Event
1 September 2004	Audit staff attended the 2 nd International Seminar on IT Audit held by the CNAO in Nanjing during 1 to 4 September 2004.
22 September 2004	A proposal for the reorganisation of the Commission was endorsed at the Directorate Meeting.
September 2004	A Senior Auditor attended a three-week Leadership in Action Programme in September 2004.
11 to 16 October 2004	The Director of Audit and the Senior Auditor (Research and Development) attended the 18 th INTOSAI Congress, as members of the China delegation which was headed by the Deputy Auditor General of the CNAO.
29 October 2004	The Director of Audit's Report No. 43 was completed and signed.
1 November 2004	A staff member from the Audit Commission of Macao started her six-month secondment to our office.
16 November 2004	The Director of Audit delivered a talk at the Management Consultancies Association of Hong Kong Luncheon Meeting.
18 November 2004	A presentation on the work of Audit was given to the new Public Accounts Committee Members at a luncheon.
24 November 2004	The Director of Audit's Report No. 43 was tabled in the Legislative Council.
25 November 2004	The Director of Audit attended the annual dinner of the Hong Kong Institute of Certified Public Accountants.
November 2004	An Assistant Director of Audit attended the Leadership Enhancement and Development Programme in November 2004.
November 2004	A Principal Auditor completed the Civil Service Advanced Management Programme (from April to November 2004).
2 December 2004	The Director of Audit delivered a talk to the Canadian Certified General Accountants Association of Hong Kong.
5 January 2005	Two forums were held to brief staff members on the proposals to reorganise Audit and to merge the Auditor and Examiner grades.
7 January 2005	A study tour on VFM audit from the Tianjin Audit Bureau and three officials from three different Government offices in Shenzhen visited our office. A talk was delivered to members of the study tour.
13 January 2005	The Director of Audit took part in the program of “新聞透視” of the TVB.
26 January 2005	The Director of Audit delivered a talk at the Hong Kong Institute of Directors Luncheon Meeting.

Appendix D
(Cont'd)

Date	Event
27 January 2005	The Director of Audit attended the Annual Dinner and Prize Presentation Ceremony 2005 of the Hong Kong Association of Accounting Technicians.
22 February 2005	An Assistant Director of Audit attended the Spring Dinner of the Association of Chartered Certified Accountants.
23 February 2005	The Director of Audit delivered a talk to the senior staff of the Government Property Agency.
2 March 2005	A group of senior officials from the Office of the Auditor General of Thailand visited our office.
8 March 2005	The Director of Audit attended the Spring Cocktail Reception of the Hong Kong Institute of Certified Public Accountants.
23 March 2005	The Director of Audit attended the 2005 Annual Dinner of the Association of International Accountants - Hong Kong Branch.
27 March 2005	Audit staff attended the ASOSAI seminar during 27 to 31 March 2005.
March 2005	An Acting Principal Auditor completed the Leadership in Action Programme in March 2005.