

Capital Works Reserve Fund

REPORT OF THE DIRECTOR OF AUDIT



Audit Commission

The Government of the Hong Kong Special Administrative Region

Independent Audit Report To the President of the Legislative Council

I certify that I have examined and audited the financial statements of the Capital Works Reserve Fund set out on pages 38 to 47, which comprise the statement of assets and liabilities as at 31 March 2016, and the statement of receipts and payments for the year then ended, and a summary of significant accounting policies and other explanatory information.

Director of Accounting Services' responsibility for the financial statements

In accordance with section 16(1) of the Public Finance Ordinance (Cap. 2), the Director of Accounting Services is responsible for the compilation and supervision of the accounts of the Government of the Hong Kong Special Administrative Region, for the management of accounting operations and procedures, and for ensuring that all regulations, directions or instructions made or given under the Public Finance Ordinance relating thereto and in respect of the safe custody of public moneys and its accounting are complied with.

Auditor's responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with section 12(1) of the Audit Ordinance (Cap. 122) and the Audit Commission auditing standards. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used by the Director of Accounting Services, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements of the Capital Works Reserve Fund for the year ended 31 March 2016 are prepared, in all material respects, in accordance with the Public Finance Ordinance and section 11(1) of the Audit Ordinance.

David Sun
Director of Audit

26 October 2016

Audit Commission
26th Floor
Immigration Tower
7 Gloucester Road
Wanchai, Hong Kong

Capital Works Reserve Fund

STATEMENT OF ASSETS AND LIABILITIES AS AT 31 MARCH 2016

	Note	2016 HK\$'000	2015 HK\$'000
Assets			
Investments with the Exchange Fund	3	59,926,086	77,914,677
Cash and bank balances		952	4,101
		59,927,038	77,918,778
Liabilities			
Deposits	4	(1,756,652)	(1,556,334)
		58,170,386	76,362,444
Representing:			
Fund Balance			
Balance at beginning of year		76,362,444	79,772,902
Deficit for the year		(18,192,058)	(3,410,458)
Balance at end of year	5, 6, 7	58,170,386	76,362,444

Notes 1 to 10 form part of these financial statements.

Martin SIU
Director of Accounting Services
22 August 2016



Capital Works Reserve Fund

STATEMENT OF RECEIPTS AND PAYMENTS FOR THE YEAR ENDED 31 MARCH 2016

	Note	2016 HK\$'000	2015 HK\$'000
Cash and bank balances at beginning of year		4,101	909
Receipts	8	60,990,535	77,990,057
Payments	5, 9	(79,182,593)	(81,400,515)
Deficit for the year		(18,192,058)	(3,410,458)
Other cash movements	10	18,188,909	3,413,650
Cash and bank balances at end of year		952	4,101

Notes 1 to 10 form part of these financial statements.

Martin SIU
Director of Accounting Services
22 August 2016



Capital Works Reserve Fund

NOTES TO THE FINANCIAL STATEMENTS

1. Purpose and Legislation

The Capital Works Reserve Fund was set up to finance public works programmes, acquisitions of land, capital subventions and major systems and equipment items. It was initially established on 1 April 1982 by a Resolution of the Legislative Council passed on 20 January 1982 and has been reconstituted since 1 January 1998 under another Resolution passed on 17 December 1997 (hereinafter referred to as the Resolution).

2. Accounting Policies

- (i) The accounts of the Capital Works Reserve Fund are kept on a cash basis. Transactions are recorded when moneys are received or paid. The Statement of Assets and Liabilities of the Fund excludes fixed assets, loans, investments other than those made under paragraph (d)(iii) of the Resolution, and debtors and creditors other than those deposits referred to in Note 4 below.
- (ii) For the purposes of these financial statements, a contingent liability is defined as:
- (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Government; or
- (b) a present obligation that arises from past events but is not recognised because:
- it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
 - the amount of the obligation cannot be measured with sufficient reliability.
- (iii) Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates ruling at the transaction dates.

3. Investments with the Exchange Fund

- (i) These are investments and deposits held under paragraph (d)(iii) of the Resolution:

	2016 HK\$'000	2015 HK\$'000
Investments (Note (ii) below)	59,877,819	77,870,016
Deposits	48,267	44,661
	<u>59,926,086</u>	<u>77,914,677</u>

- (ii) The investments represent the cost of investments together with the investment income received in the year being reported. Effective from 1 April 2007, the investment income is calculated, in accordance with an arrangement entered into with the Hong Kong Monetary Authority in 2007, on the basis of the average annual investment return of the Exchange Fund's Investment Portfolio for the past six years or the average annual yield of three-year Exchange Fund Notes (replaced by three-year government bond with effect from 1 January 2016) for the previous year subject to a minimum of zero percent, whichever is the higher. The rate of return for the calendar year 2015 was 5.5% (2014: 3.6%). The annual investment income is receivable on 31 December of each year. The investment income of HK\$3.98 billion for the calendar year 2015 was set aside and retained within the Exchange Fund, and not received (Note 8(i)).

Capital Works Reserve Fund

4. Deposits

These are moneys received from time to time from individuals or organisations for a variety of reasons and are in due course either repayable or transferable for credit to the Fund:

	2016	2015
	HK\$'000	HK\$'000
Contract retention money	1,375,914	1,244,115
Others	380,738	312,219
	<u>1,756,652</u>	<u>1,556,334</u>

5. Fund Balance

The Fund Balance includes receipts from sums borrowed for the purposes of the Capital Works Reserve Fund under the Loans Ordinance (Cap. 61) that are required to be credited to the Fund under paragraph (b)(v) of the Resolution. Repayments of the principal in relation to the outstanding liabilities in respect of sums borrowed are included in payments charged to the Fund under paragraph (d)(ii) of the Resolution.

Following a resolution passed under section 3(1) of the Loans Ordinance, the Government issued in July 2004 bonds and notes totalling HK\$20 billion to retail and institutional investors. These include institutional notes of US\$1.25 billion denominated in United States dollars. The outstanding liabilities, not included in the Statement of Assets and Liabilities, in respect of sums borrowed are as follows:

	2016	2015
	HK\$'000	HK\$'000
Outstanding government bonds and notes	<u>1,500,000</u>	<u>1,500,000</u>

The outstanding bonds and notes are denominated in Hong Kong dollars with maturity in July 2019. During the financial year, there were payments of interest of HK\$77 million on the notes but no repayment of principal.

6. Contingent Liabilities

As at 31 March 2016, the amount of contingent liabilities arising from legal claims, disputes and proceedings was HK\$3,906 million (2015: HK\$5,976 million).

Capital Works Reserve Fund

7. Commitments

The balances of the approved project estimates that were unspent were as follows:

Head	2016	2015
	HK\$'000	HK\$'000
Land acquisition		
701 Land acquisition	<u>6,181,799</u>	<u>3,907,116</u>
Sub-total	<u>6,181,799</u>	<u>3,907,116</u>
Capital works – Public Works Programme		
702 Port and airport development	148,701	166,764
703 Buildings	48,655,352	28,059,134
704 Drainage	14,814,933	17,388,346
705 Civil engineering	64,194,638	40,141,846
706 Highways	176,553,909	191,326,762
707 New towns and urban area development	22,930,399	13,924,087
709 Waterworks	12,117,324	13,663,909
711 Housing	3,448,818	2,852,925
Sub-total	<u>342,864,074</u>	<u>307,523,773</u>
Capital subventions		
708 (part) Capital subventions	<u>32,749,403</u>	<u>35,223,480</u>
Sub-total	<u>32,749,403</u>	<u>35,223,480</u>
Systems and equipment		
708 (part) Major systems and equipment	3,005,762	4,284,070
710 Computerisation	7,519,921	7,117,451
Sub-total	<u>10,525,683</u>	<u>11,401,521</u>
	<u><u>392,320,959</u></u>	<u><u>358,055,890</u></u>

Capital Works Reserve Fund

8. Receipts

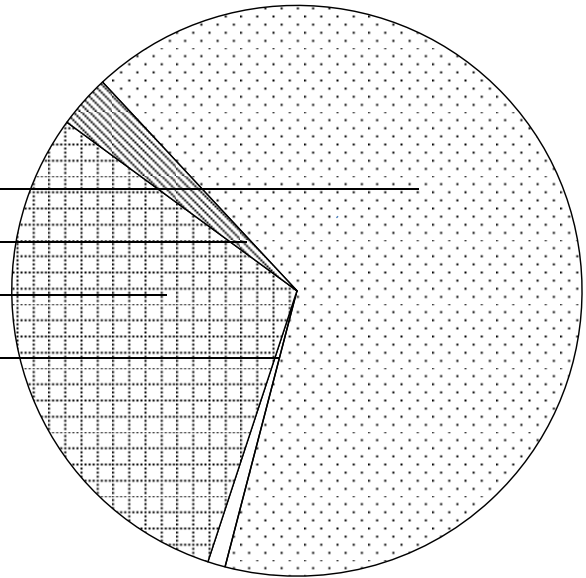
	2016		2015
	Original Estimate HK\$'000	Actual HK\$'000	Actual HK\$'000
Land premium			
Sales by public auction and tender	-	40,309,742	51,445,256
Private treaty grants	-	1,440,679	11,822,917
Modification of existing leases, exchanges and extensions	-	18,372,959	13,894,010
Fees received in respect of short term waivers	-	769,457	641,903
	70,000,000	60,892,837	77,804,086
Investment income			
Investments with the Exchange Fund (Note (i) below)	-	-	-
Others	-	2,341	2,210
	4,271,000	2,341	2,210
Other receipts			
Donations and contributions	24,880	988	70
Others	-	94,369	183,691
	24,880	95,357	183,761
	<u>74,295,880</u>	<u>60,990,535</u>	<u>77,990,057</u>

- (i) Pursuant to the Financial Secretary's directive in December 2015, the HK\$3.98 billion investment income of the Fund along with the investment income on other parts of the fiscal reserves for the calendar year 2015 was set aside and retained within the Exchange Fund as further injection to the Housing Reserve, and not received on 31 December 2015. The Housing Reserve was established in December 2014. As explained in the 2015-16 Budget Speech, the Housing Reserve is to provide financial resources to meet the ten-year public housing supply target. The investment income retained within the Exchange Fund earns the same rate of investment return as stipulated in Note 3(ii) and shall be receivable on a date as determined by the Financial Secretary. Together with the investment return of HK\$0.15 billion on the initial provision set aside from the HK\$2.88 billion investment income of the Fund for the calendar year 2014, the total sums earmarked as Housing Reserve amounted to HK\$7.01 billion.

Capital Works Reserve Fund

Analysis of Receipts for the year ended 31 March 2016

<u>Sales by public auction and tender</u>	HK\$40.3 Billion	66%
<u>Private treaty grants and fees received in respect of short term waivers</u>	HK\$2.2 Billion	3%
<u>Modification of existing leases, exchanges and extensions</u>	HK\$18.4 Billion	30%
<u>Investment income and other receipts</u>	HK\$0.1 Billion	1%



**Total Receipts
HK\$61.0 Billion**

Capital Works Reserve Fund

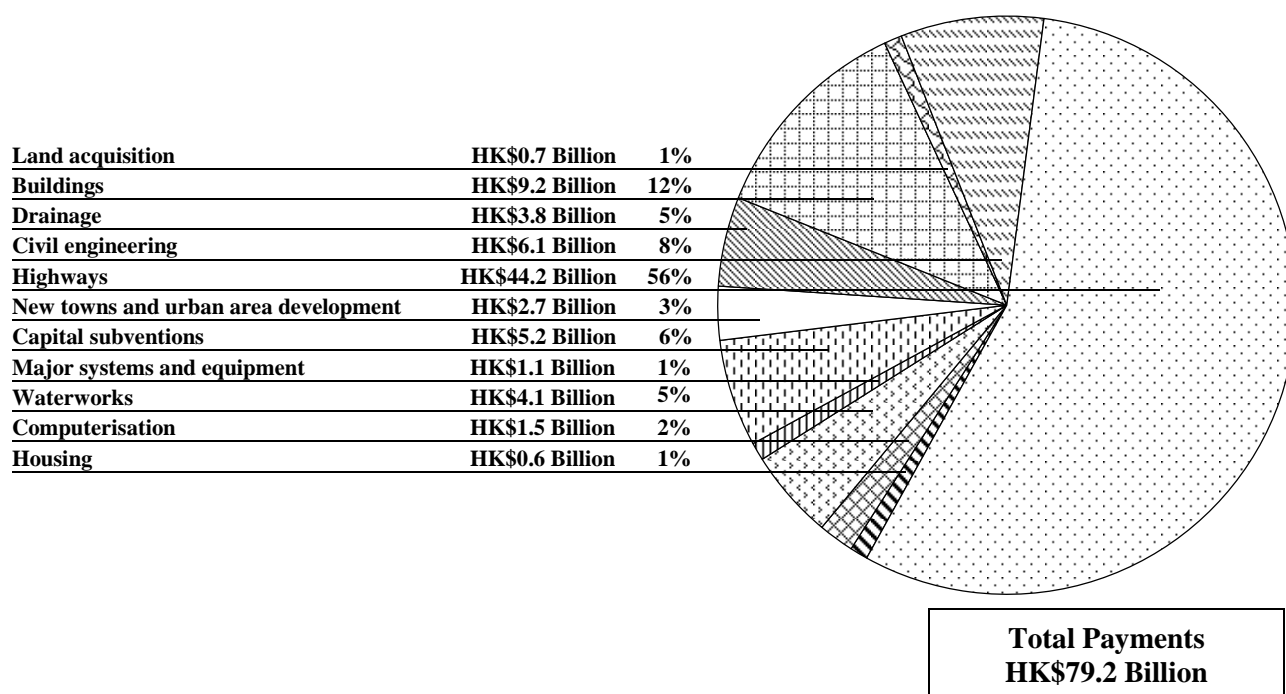
9. Payments

	2016		2015
	Original Estimate HK\$'000	Actual HK\$'000	Actual HK\$'000
Land acquisition	2,340,680	656,503	597,814
Public Works Programme			
Port and airport development	2,342	1,660	2,767
Buildings	7,322,683	9,157,521	7,635,375
Drainage	4,095,722	3,834,792	5,078,055
Civil engineering	6,040,503	6,040,310	4,338,765
Highways	38,020,745	44,168,403	38,189,058
New towns and urban area development	2,731,258	2,733,116	3,092,768
Waterworks	4,499,614	4,121,209	4,589,762
Housing	577,104	542,131	658,537
	63,289,971	70,599,142	63,585,087
Capital subventions and major systems and equipment			
Capital subventions	6,718,315	5,189,681	5,171,336
Major systems and equipment	1,184,383	1,133,293	476,893
	7,902,698	6,322,974	5,648,229
Computerisation	1,762,221	1,519,091	1,543,917
Government bonds and notes issued in July 2004			
Repayment	-	-	9,687,794
Interest and other expenses	77,302	77,301	325,126
	77,302	77,301	10,012,920
Other payments			
Refund of overpayment of land premium	-	7,582	12,548
	<u>75,372,872</u>	<u>79,182,593</u>	<u>81,400,515</u>

Further analyses of payments appear on pages 148 to 219 of the Supporting Statements.

Capital Works Reserve Fund

Analysis of Payments for the year ended 31 March 2016 *



* Actual payments on “Port and airport development”, “Refund of overpayment of land premium” and “Interest and other expenses on government bonds and notes” are not shown as it is less than HK\$0.1 billion each.

10. Other Cash Movements

These are cash movements arising from changes in other assets and liabilities:

	2016 HK\$'000	2015 HK\$'000
Reduction in Assets		
Investments with the Exchange Fund	17,988,591	3,144,610
Increase in Liabilities		
Deposits	200,318	269,040
	18,188,909	3,413,650

Capital Works Reserve Fund

Receipts, Payments and Fund Balance for the years ended 31 March 2007 to 2016

HK\$Billion

