

Appendix A (2)

REPORT TO THE DIRECTOR OF COLONIAL AUDIT ON THE AUDIT OF THE ACCOUNTS OF HONG KONG 1934.

Subject to the comments contained in this report the accounts generally have been satisfactorily kept and rendered and the existing regulations appear to provide reasonable accounting protection against irregularities and fraud.

The last of the Annual Statements was received from the Treasurer on 27th July.

2. The relation between the excess of Assets over Liabilities for the years 1933 and 1934 is established as follows:—

Excess 31st December 1933.....	\$13,823,625.33
Revenue 1934	29,574,285.57
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	43,397,910.90
Expenditure 1934	31,149,155.66
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Excess of Assets 31st December 1934	\$12,248,755.24
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3. Comparison of the revenue and expenditure for the year with the approved Estimates and with previous years is dealt with fully in the Treasurer's Report (Enclosure M) and in the detailed statements (Enclosures C and D).

AUTHORITY FOR EXPENDITURE 1934.

4. The Estimates for the year received the approval of the Secretary of State in his Despatch No. 34 of 29th January 1934 and were passed by the Legislative Council in Ordinance No. 19 of 1933.

5. Supplementary Estimates for the year amounting to \$772,000 were duly passed by the Legislature and approved by the Secretary of State in his telegram of 20th July.

The 1934 Supplementary Appropriation Ordinance (No. 30 of 1935) was passed by the Legislature on 11th July 1935 thus providing complete local authority for the expenditure of the year.

LIABILITIES.

GOVERNMENT HOUSE AND CITY DEVELOPMENT FUND.—
\$1,218,741.28.

6. The special appropriation of the revenue from certain Land Sales to this particular expenditure was legalised by Ordinance No. 30 of 1934.

A small amount of preliminary expenditure during the year has since been authorised by resolution of Legislative Council.

SUSPENSE ACCOUNT—\$975,589.24.

7. The main item in the figures leading to this liability is still \$975,413.78 on account of "Military Contribution" referred to in many previous reports, but as the Estimates for 1935 provide for this as a Miscellaneous Receipt presumably the amount will during the current year be transferred to Revenue and the discussion of many years will in this particular respect come to a satisfactory conclusion.

EXCHANGE ADJUSTMENT—\$28,038.16.

8. Now that all Sterling Investments have been realised this liability merely represents provision for the dollar difference arising from fluctuation of holdings in the Joint Colonial Fund.

TRADE LOAN ACCOUNT.

9. A full statement of the position of this account is given in the Treasurer's report and the relevant items in the Balance Sheet call for no further comment.

ASSETS.

TREASURER'S CASH BALANCE.

10. The constitution of the Cash Balance in the hands of the Treasurer at the end of the year has been referred to in the Annual Report for 1930 and each subsequent year. This vexed question has at last been settled by the Secretary of State in despatch No. 99 of 12th March 1935 supporting the original audit contention and ruling that he is unable to authorise any relaxation of the important rule that payments can only be charged at the date on which they are actually made. Two methods for future procedure were suggested by the Secretary of State but the decision of the Government giving effect to his ruling has not yet been communicated.

11. The attention of Government was drawn to the fact that the Annual Board of Survey of the Treasury Cash had been made after the commencement of business on the first day of the new year. Arrangements have now been made for future boards to be held in conformity with regulation.

12. Under standing instructions the Secretary of State is kept informed at six-monthly intervals of the amounts of Government Funds deposited with the local banks and of the balance of the current account kept with the Hong Kong and Shanghai Bank. The very large sums held locally on deposit on 31st December 1934 are therefore known to him.

JOINT COLONIAL FUND £242,000 (\$2,913,103).

13. During the year the Sterling Investments (consisting of Government and Corporation Stocks of a nominal value of £117,829) forming part of the Surplus Balances of the Colony were realised for the purpose of assisting in the redemption of the 3½% Inscribed Stock.

The proceeds were, however, not so utilised and, in consequence, there occurred the excess on authorised loan expenditure referred to in paragraphs 32 and 33 below.

14. The Assets held by the Crown Agents have been supported by the certificate of the Comptroller and Auditor General.

SUPREME COURT ACCOUNTS.

15. During the audit of these accounts attention was drawn to the large sums which had been on deposit over 5 years for which no liability was likely to arise, and in accordance with Colonial Regulation 330 arrangements have been made to transfer over \$25,000 to Revenue.

SECRETARIAT FOR CHINESE AFFAIRS.

16. Reference has been made in previous reports to these accounts which owing to their special nature are "outside the accounts of the Colony except in so far as the Treasury acts as banker". It happens, however, that this particular department collects a small amount of purely Government revenue and incurs Government expenditure on Personal Emoluments &c, the transactions for which are merged in the main accounts of the office.

Thus in the 2nd Quarter of 1934 the revenue collected was \$340 out of total receipts amounting to \$69,600. To audit this very small portion it becomes necessary to examine to a certain extent the books of the Secretariat for Chinese Affairs without actually being responsible for their entire audit.

17. This is unsatisfactory and it would undoubtedly be of advantage and more correct if the accounts for the actual Government revenue and expenditure were kept completely separate and in different books from the remaining accounts of the Secretariat for Chinese Affairs. The suggestion in audit that this should be done was not accepted. (Enclosure P refers).

CHINA COMPANY FEES.

18. The annual local examination of the Registrar of Companies Accounts at Shanghai was made in September and the accounts audited to date. The revenue from this source during the year was \$177,867, as compared with \$141,342 for the previous year.

COUNTERFOIL RECEIPTS.

19. Consequent on your Circular Reference Sheet No. 167 a special investigation was made early in the year into the control of this important method of accounting for the collection of revenue.

With one exception the departmental control was satisfactory though in every case discrepancies were revealed between the Central Register kept in the Treasury and that kept in the department.

POST OFFICE.

20. A shortage of \$357.86 in the cash and stamps of an absconding clerk was made good in part by the estreatment of his security and forfeiture of salary while the balance was written off with the approval of the Secretary of State.

KOWLOON CANTON RAILWAY.

21. A copy of the Manager's Annual Report is forwarded (Enclosure N). The accounts have been regularly rendered and satisfactorily kept.

The final division sheets of Through and Joint Sectional Traffic Receipts have been audited to the end of the year and accepted by both Administrations.

22. A new Working Agreement came into operation on 1st October 1934 the chief feature of which being that the British Section Share of terminal through traffic receipts was reduced from 35% to 28%. In spite of this the total revenue showed an increase over the revenue of the previous year.

During the negotiations leading to this new Agreement it was agreed that claims against the Chinese Section amounting to \$1,025,533 should be waived (Vide para 31 of 1929 Annual Report). This has been reported to the Secretary of State.

23. During the year arrangements were brought into force for issuing combined rail and bus tickets, the bus companies being both in the Colony's Territory and the Kwangtung Province. The experiment was entirely successful and the division of receipts presented no difficulty in audit.

24. The Advance Account "Purchase of Three Locomotives for Chinese Section" continues to be repaid by the agreed amount of \$10,000 per month and the claims for haulage fees by British Locomotives have been regularly met.

25. The Balance of the Unallocated Stores Account \$170,372.02 is within the limit authorised by the Secretary of State and a reconciliation of the balance as shown in the Treasury and the Railway books is attached (Enclosure K).

26. Twelve surveys on the accounts of the Railway Stations, including the Head Office, were carried out during the year and call for no special comment.

LOAN ACCOUNTING.

27. An important feature of the year's accounts has been the redemption of the Inscribed Stock Loans of 1893 and 1906 amounting to £1,485,733 and the flotation locally of the 3½% Dollar Loan.

The actual redemption of the Sterling Loans was carried out by the Crown Agents and their figures have been accepted.

28. There have been so many departures from the authorised accounting procedure that it is necessary to comment at some length.

29. During the year bonds to the amount of \$14,000,000 were issued by Government under the Ordinance No. 11/1934.

Though the arrangements for the issue of the Loan were placed in the hands of two local banks the cheques accompanying the application money and in payment of the full allotment were made "payable to the Hong Kong Government", crossed with the name of the bank. No account of these moneys has been submitted for audit nor was any information accorded to this department of the preliminary accounting arrangements of the Loan. The first entry in the accounts of the Colony in regard to the Loan is the receipt in the Treasury Cash Book of \$13,860,000 being 99% of \$14,000,000 issued. This receipt together with the Crown Agents voucher for the printing of the bonds has formed therefore the only basis on which audit was possible.

30. As applications, accompanied by application money, were received far in excess of the authorised issue there were obviously transactions such as refunds or adjustments of application money which were subject to account and, it was submitted, should have been subject to audit.

31. The Government, apparently on the ground that the Colonial Treasurer was satisfied, decided to let the matter rest. The principle that because the Treasurer is satisfied with

any portion of the public accounting audit can therefore be foregone was so entirely novel that it was considered advisable to report the circumstances to you as soon as possible (Audit Letter 100/99). A copy of this letter was forwarded by you to the Secretary of State and no further action has therefore been taken locally but it is necessary that it should be clearly understood at what stage and on what basis the audit of this particular section of the accounts has commenced.

32. In March 1935 last the Legislative Council approved a resolution that the sum of \$217,067.30 on account of loan works should be met from surplus balances during 1934 pending the issue of a further loan. This was necessary because the total expended was by this amount in excess of the amount raised (\$13,860,000). It was pointed out by this department that such authority or, if that was not possible, at least the authority of a Governor's Warrant (now by the new edition of the Colonial Regulations styled a Loan Warrant) should have been obtained immediately it was known that surplus balances were to be so used.

33. Included in the charges against the loan was an amount \$3,864,942.97 on account of Redemption of 3½% Inscribed Stock. As the schedule to the Hong Kong Dollar Loan Ordinance (No. 11 of 1934) limited this particular item to \$3,400,000 it was irregular to charge more than this amount against the loan. Before doing so it was necessary first to obtain the approval of the Legislative Council and the Secretary of State enabling the Governor to direct a re-appropriation of the items in the Loan Schedule. These irregularities were partially rectified by a series of resolutions in Council on 16th April 1935. Even so, the sanction of the Secretary of State has still to be obtained although the Ordinance reads that no transfer of appropriation should be directed until after such approval has been fully given.

34. The redemption of the Inscribed 3½% Stock was carried out by the Crown Agents in October and the transactions have been included in the Treasurer's books as credits and debits to the Dollar Loan Account. The result is that in the Annual Account the receipts on account of the 3½% Dollar Loan are shown as \$28,735,618.69 and the expenditure as \$28,952,685.99 or practically double the actual amounts received from the Issue of Bonds and expended on Loan Work etc.

35. On reference to Government it was agreed that it would have been clearer if a separate account had been opened for recording these, the final transactions of the Sterling Loan, but the books for the year having been closed the position has to a certain extent been clarified by an explanatory note being made in the main ledger (Enclosure Q).

36. It will be seen from the preceding paragraphs that the loan accounting during the year was not carried out in strict conformity with the formalities required either by the law (Ordinance 11/1934) or Colonial Regulations.

37. It may be noted here that with regard to this Dollar Loan Ordinance the usual notification of non-disallowance by His Majesty the King has not yet been gazetted.

38. The Statement of Funded Public Debt &c. as published with the Annual Statements was incorrectly prepared and on representation by this department an amended statement was published in the Gazette of August 2nd 1935 and is submitted as Encloure I.

STORE ACCOUNTS.

MEDICAL STORES.

39. Theft and subsequent disposal to a private firm of an expensive drug was discovered during the year and at the request of the Medical Department an intensive examination of the accounting for this particular drug was conducted by this department. The investigation revealed deliberate fraud and tampering with books and vouchers such as would not ordinarily have been discovered in audit. The matter was reported to the Secretary of State who has approved the appointment of an additional officer for this store which should ensure closer departmental control.

40. Except for this the examination of the various Store Accounts calls for no special comment. Surprise Surveys of Stores were made by this department during the year as reported in the Quarterly Returns.

ARREARS OF REVENUE.

41. The position with regard to Arrears of Revenue is as follows:—

Of the \$696,559.67 arrears outstanding on 31st December 1934 \$635,119.23 had been paid by 30th June 1935, \$27,486.84 was written off leaving \$33,953.60 still to be collected.

A certain amount of confusion periodically arises with regard to the preparation of the returns of outstanding revenue by departments, and the matter has been brought to the notice of the Treasurer for action.

42. There were no misallocations of revenue or expenditure brought to notice too late for adjustment.

QUERIES.

43. The queries raised during the year were of a routine nature and have all been settled. Among the larger amounts recovered in audit were £25, £42 and £49 on account of

Government passages incorrectly charged against Government Funds, and an overpayment of \$342 on Rent Allowance. A gratuity was reduced on audit calculation by £21 and a Widow's and Orphans' Pension by £6.17.4. per annum. Further, undercollections of revenue of \$91.65 Liquor Duty and \$100 Land Sales were rectified.

PARAGRAPH 53 OF 1933 REPORT.

44. The Secretary of State's authority was received to write off the \$800 referred to in the paragraph.

45. The usual Surprise surveys of cash, stamps &c. were made in the various offices during the year and there has been no material departure from the approved Programme of work.

P. L. COLLISSON,
Auditor.

15th August 1935.