

ITEM FOR FINANCE COMMITTEE

HEAD 190 – UNIVERSITY GRANTS COMMITTEE Subhead 492 Grants to UGC-funded institutions

Members are invited to –

- (a) accept the total recurrent funding requirement of the University Grants Committee-funded institutions for the 2001/02 to 2003/04 triennium estimated at \$36,269.5 million;
- (b) approve supplementary provision of \$522.4 million to meet the shortfall in the assumed tuition fee income of the institutions in the 2000/01 academic year; and
- (c) approve the arrangement for the institutions to carry up to 20% of their respective recurrent grant in a triennium to the next as reserves.

At the Finance Committee meeting on 9 February 2001, Members were requested to consider the above proposal. The item was withdrawn to allow for more thorough discussion, which took place at the meeting of the Legislative Council Panel on Education (the Panel) on 19 February 2001. The previous Finance Committee agenda item (FCR(2000-01)72) and the paper subsequently presented to the Panel are at Enclosures 1 and 2 respectively. This paper addresses, and provides further information on, key points raised at the last meeting of the Committee and the Panel.

Encls.1&2

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The proposal on Government's funding for the University Grants Committee

2. Insofar as the funding requirement of the University Grants Committee (UGC)-funded institutions for the 2001/02 to 2003/04 triennium is concerned, this proposal seeks Members' approval of the **overall amount of Government's subvention to the UGC**. In other words, the approval is in respect of Government's interface with the UGC, where the UGC acts on behalf of the universities as a whole.

3. Issues such as how the UGC intends to apportion the Government's subvention among the institutions, how resources are utilized within the institutions, and how individual institutions make their management and academic decisions are separate from, and beyond the immediate remit of, the current proposal. We believe these issues should best be left to the UGC and the institutions to pursue, so as not to compromise the institutional autonomy of the universities. The UGC and the Administration will be happy to follow up comments made at the Education Panel to ensure that available resources are put to the best possible use.

Adequacy of Government funding

4. The Panel paper at Enclosure 2 explains in detail how the proposed funding has been arrived at. The Government has **not** requested any further reduction in the unit cost beyond the agreed 10% target (or 5% net if the 5% plough back to the UGC for academic developments is discounted). In view of this 5% net reduction, the Administration and the UGC have agreed that the UGC is **not** required to deliver additional savings under the Enhanced Productivity Programme that applies to the public sector.

5. As a result, **the student unit cost for the next triennium will only be 1% less than that in the 2000/01 academic year**, and this reduction basically reflects the deflation during the current triennium. As institutions have been making genuine and sustainable efforts to control costs and achieve productivity gains in the past three years, we believe the leveling-off of the student unit cost at the present level from now on will not present insurmountable difficulties to the institutions.

6. An integral part of the current proposal is that the institutions should be allowed to accumulate up to 20% of their grants as reserves. The institutions are expected to have cash-flow surpluses to the order of \$5 billion in total by the

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end of this triennium, representing 13.9% of the institutional grants for this triennium. Assuming that the proposed carry-over mechanism is approved, and discounting the portion intended for specific purposes, **the amount of surplus that can be carried over to the next triennium and freely used by the concerned institutions will amount to around \$1.5 billion, or over 4% of the institutional grants proposed for the next triennium.** For Members' reference, the proposed reduction in the UGC's recurrent funding requirement for the 2001/02 to 2003/04 triennium, inclusive of the full effect of the 5% net reduction in student unit cost, adjustments due to changes in student target number and the deflation factor mentioned above, is only 3.9% of its total funding requirement.

7. The UGC is satisfied that this modest reduction in funding will not affect the overall quality of teaching and learning in the institutions.

The UGC's allocations to individual institutions

8. The UGC is nonetheless keenly aware of the difficulties that certain institutions may be facing arising from the cumulative effect of the reduction in funding. In this connection, the UGC itself expects to have accumulated savings of around **\$250 million** by the end of the current triennium. If the proposed carry-over mechanism for the institutions is approved, the **UGC will distribute its central savings to the institutions** so that they can carry them over to the next triennium as additions to the block grant.

9. For the 2001/02 to 2003/04 triennium, the UGC will distribute the bulk of Government funding to individual institutions as their recurrent block grant. However, this does not represent the maximum funding to be allocated to the institutions. The UGC will in addition distribute a substantial part of the Government funding it receives, to the order of \$2.5 billion, to the institutions as earmarked grants for specific purposes. The UGC has also set aside \$700 million of the Government funding as performance-related funding for further distribution to the institutions after a broad-based assessment exercise.

Government's additional funding support

10. The Government also agrees that the current practice of using the crude average student unit cost to determine the recurrent funding for the UGC sector may in the longer term impose difficulties for the UGC as we seek a

/progressive

progressive increase in degree and above places. The Government therefore **undertakes to review the current funding methodology**, so that student mix and student unit cost by levels can be taken into account in determining funding for the UGC, subject to the availability of resources. During the 2001/02 to 2003/04 triennium, should the UGC sector encounter any genuine financial difficulties, the Government **undertakes to identify scope for additional allocation to the UGC, over and above the funding level currently proposed.**

Proposal

11. Given the above considerations, we are satisfied that the current proposal, which is the outcome of a lengthy process of negotiation and which reflects the final joint recommendation of the UGC and the Administration, should be resubmitted for Members' approval.

Education and Manpower Bureau
February 2001

For discussion
on 9 February 2001

FCR(2000-01)72

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Members are invited to –

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- (b) approve supplementary provision of \$522.4 million to meet the shortfall in the assumed tuition fee income of the institutions in the 2000/01 academic year; and
- (c) approve the arrangement for the institutions to carry up to 20% of their respective recurrent grant in a triennium to the next as reserves.

PROBLEM

The eight institutions funded by the University Grants Committee (UGC)⁽¹⁾ have to finalise their budgets and academic programmes for the 2001/02 to 2003/04 triennium, which will start on 1 July 2001. They need confirmation of the level of recurrent grants they will receive for that period and the amount of funds they will be allowed to carry over from the current triennium (i.e. 1998/99 to 2000/01) in order to finalise their programmes. Also, the UGC needs

/supplementary

⁽¹⁾ They are City University of Hong Kong, Hong Kong Baptist University, Lingnan University, The Chinese University of Hong Kong, The Hong Kong Institute of Education (HKIEd), The Hong Kong Polytechnic University, The Hong Kong University of Science and Technology and The University of Hong Kong.

supplementary provision to meet the institutions' shortfall in tuition fee income due to the freeze of the tuition fee levels in the 2000/01 academic year.

PROPOSAL

2. The Secretary for Education and Manpower proposes that Members -
 - (a) accept the total recurrent funding for the eight institutions for the 2001/02 to 2003/04 triennium estimated at \$36,269.5 million;
 - (b) approve a supplementary provision of \$522.4 million to meet the institutions' shortfall in tuition fee income in the 2000/01 academic year; and
 - (c) allow the institutions to carry up to 20% of their recurrent grants in a triennium to the next as reserves.

JUSTIFICATION

Recurrent funding requirements for the 2001/02 to 2003/04 triennium

Encl. 1

3. Based on the established method, the UGC has assessed the recurrent funding requirements of the eight institutions under its aegis for the 2001/02 to 2003/04 triennium, having regard to the indicative student number targets as shown at Enclosure 1, as well as the Academic Development Proposals of respective institutions. Paragraphs 4 and 5 below explain how we have arrived at the funding requirements, and paragraphs 6 and 7 below explain how we have arrived at the recommended level of government grants.

4. As agreed in 1996 between the UGC and the Administration and as reported to Members vide FCR(97-98)111, there has been a 10% point-to-point reduction in average student unit cost by the end of the 1998/99 to 2000/01 triennium⁽²⁾, with half of the savings ploughed back to the UGC for redistribution to the institutions to meet new developments such as Areas of Excellence Scheme. In effect, this works out to be a 5% net reduction in the overall average student unit cost. This reduced unit cost has formed the basis for determining the total funding requirements of the UGC for the 2001/02 to 2003/04 triennium. The Administration has not requested further reduction in the unit cost beyond the above agreed target.

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⁽²⁾ The reduction in student unit cost does not apply to the HKIED.

5. Adopting the reduced unit cost in calculating the funding requirements for the next triennium results in the total requirements for the coming triennium being smaller than that for the current one. A diagrammatic presentation is at Enclosure 2. As a result of the full triennial effect of the unit cost reduction, deflation during the current triennium and changes in student number targets for the next triennium, the recurrent funds required by the UGC-funded sector in the 2001/02 to 2003/04 triennium will be about 3.9% less than that in the 1998/99 to 2000/01 triennium⁽³⁾. The recurrent funding requirements and student number targets for the next triennium, compared with the current one, are shown at Enclosure 3.

Specific recommendations on the level of Government grants

6. Government determines the level of recurrent grants to the UGC-funded institutions by deducting from the institutions' total funding requirements an assumed income of the institutions which includes tuition fees⁽⁴⁾ (please also see paragraph 9 below). In the light of Government grants available, the UGC has determined the level of specific recurrent grants for the individual institutions and for other earmarked purposes in the 2001/02 to 2003/04 triennium. The recommendations are shown below –

	Academic year (July to June)			
	2001/02	2002/03	2003/04	Total
	\$ million	\$ million	\$ million	\$ million
City University of Hong Kong	1,555.0	1,503.8	1,502.5	4,561.3
Hong Kong Baptist University	595.7	589.4	594.1	1,779.2
Lingnan University	211.8	205.0	205.2	622.0
The Chinese University of Hong Kong	2,481.8	2,437.5	2,452.9	7,372.2
The Hong Kong Institute of Education	768.3	764.1	770.1	2,302.5
The Hong Kong Polytechnic University	1,799.8	1,739.7	1,735.7	5,275.2
The Hong Kong University of Science and Technology	1,380.7	1,353.9	1,358.0	4,092.6
The University of Hong Kong	2,409.0	2,330.4	2,328.0	7,067.4
Performance- and mission-related funding	-	349.4	350.6	700.0
Sub-total	11,202.1	11,273.2	11,297.1	33,772.4
Earmarked Research Grants	510.8	543.3	577.9	1,632.0
				/Teaching

⁽³⁾ This includes additional funding to HKIEd in the course of the 1998/99 to 2000/01 triennium for the progressive upgrading of the sub-degree teacher education places to degree and above levels.

⁽⁴⁾ In determining the recurrent funding to institutions for the 2001/02 to 2003/04 triennium, we have assumed that the tuition fee will continue to be frozen at the current level.

	Academic year (July to June)			
	2001/02 \$ million	2002/03 \$ million	2003/04 \$ million	Total \$ million
Teaching Development Grants	38.3	38.3	38.4	115.0
Language Enhancement Grants	72.5	72.5	72.5	217.5
Central Allocation Vote	140.5	175.2	209.9	525.6
Recurrent Grants to the UGC-funded institutions	11,964.2	12,102.5	12,195.8	36,262.5
Sum to be retained by UGC for administering inter-institutional projects	2.3	2.3	2.4	7.0
Total	11,966.5	12,104.8	12,198.2	36,269.5

Encl. 4

7. The UGC's methodology for determining the levels of triennial recurrent grants to the individual institutions is detailed at Enclosure 4. The formula gives a reasonably rigorous and precise assessment of the resources required to meet the teaching and research requirements of each institution, and includes an element of funding specifically related to the recent performance of the individual institutions in the research area. We will continue to monitor the operation of the funding methodology and encourage the UGC to refine it to meet changing and new circumstances.

8. In assessing the recurrent funding requirements of the institutions, we have not taken into account the financial implications of introducing the UGC Home Financing Scheme (HFS) since 1998, lest the initial additional cashflow expenditure for the UGC HFS would lead to unnecessary fluctuations in the student unit cost and tuition fees. The financial implications of HFS are therefore not reflected in the level of Government grants recommended above. In accordance with the established practice, we shall adjust the grants to the UGC-funded institutions in the course of the triennium to reflect Government's additional provision to the institutions for HFS, Government's share of the rental income arising from surplus staff quarters and the institutions' savings in non-HFS housing-related expenses.

/Tuition

Tuition fee shortfall in the 2000/01 academic year

9. As explained in paragraph 6 above, Government's total recurrent grant to the UGC-funded institutions is the estimated total funding requirement net of the institutions' assumed income from tuition fees and from other sources. The assumed tuition income is an estimate that has to be reconciled when the actual fee levels are known. This means that if the actual fee levels subsequently approved by the Administration for a certain academic year are lower than that assumed in determining the recurrent grant, the Government will normally provide additional funds to meet the shortfall. Conversely, if there is a surplus income as a result of the actual tuition fee level being higher than that assumed, the excess in recurrent grant will be clawed back by the Government.

10. In June 2000, the Administration decided to freeze the tuition fees for the 2000/01 academic year at their then prevailing (1999/2000) levels, that is,

Degree and above programmes	\$42,100
Sub-degree programmes (except those offered by the HKIEd)	\$31,575
Sub-degree programmes offered by the HKIEd ⁽⁵⁾	\$15,040

11. As a result of the freeze, the tuition fee income received by the UGC-funded institutions in the 2000/01 academic year is \$522.4 million less than the amount assumed when the funding level for the 1998/99 to 2000/01 triennium was determined in 1998. Following the principle in paragraph 9 above, supplementary provision from the Government is required.

Carrying over of unspent funds across triennia

12. At present, there is limited scope for the UGC-funded institutions to carry unspent funds from one triennium to another. They are not allowed to do so except by making allocations to the three purpose-specific reserve funds⁽⁶⁾ to cater for bulges in expenditure across the funding period. We consider there is a case to allow the institutions to replace these reserve funds with a bigger general reserve facility so as to –

/(a)

⁽⁵⁾ Sub-degree programmes of HKIEd are subject to a different scale of tuition fees. The bulk of HKIEd's sub-degree programme tuition fees comes from the Certificate in Education courses which are currently charged at \$15,040.

⁽⁶⁾ The three reserve funds are building-related reserve to cover maintenance and redecoration of premises, and replacement of premises-related equipment, non-building-related reserve to cover replacement of vehicles and equipment, and staff-related reserve to cover various types of staff payments.

- (a) encourage longer-term planning and prudent financial management. Increased flexibility provides an incentive to save money for future use. Such flexibility is given to a number of subvented organisations including aided schools, the Hospital Authority (HA), and more recently the Vocational Training Council (VTC); and
- (b) encourage the UGC-funded institutions to save up for the implementation of new initiatives arising from the education reform.

13. We therefore recommend that the UGC-funded institutions should each be allowed to carry unspent funds up to 20% of their respective institutional recurrent grants in a triennium to the next triennium as reserves. For Members' reference, the reserve ceilings for the HA and the VTC are 5% and 15% respectively. As regards aided schools, they are allowed to keep a reserve up to 100% of their respective annual Operating Expenses Block Grant and 500% of their Composite Furniture and Equipment Grant.

14. We recommend a maximum reserve level of 20% for the UGC-funded institutions for the following reasons –

- (a) the education reform package has presented tremendous challenges to the higher education sector. For instance, there will be discussions on credit unit transfer and the normative length of an undergraduate programme. As higher education already takes up about one-third of the total government resources allocated to education, the recurrent subsidy to the UGC-funded sector is not expected to increase substantially in the short-term. By allowing a 20% reserve facility, we would encourage and facilitate the institutions to make more effective and flexible use of their existing resources;
- (b) unlike the HA, aided schools and the VTC which are funded on an annual basis, the UGC-funded institutions' recurrent grants are determined based on a broadbrush formula on a triennial basis. In particular, the non-salary related expenditure is calculated at the price level one year before the beginning of the triennium. While this mode of funding allows greater flexibility, institutions are expected to absorb the effect of inflation and deflation for non-salary related expenditure during the triennium and hence bear a higher financial risk. The UGC sector therefore needs a bigger reserve; and
- (c) the life cycle for some research infrastructure investment varies. Added flexibility is required as expenditure may straddle two or even more triennia.

15. The reserve will operate according to the following principles –
- (a) the institutions will be required to notify the UGC of the amount of their reserves as at the end of each triennium;
 - (b) the reserve funds must be spent within the ambit of the original grant. Windfall savings to the institutions may not be kept as reserves⁽⁷⁾;
 - (c) the interest income generated by the reserve funds will be treated as part of the assumed income in determining the recurrent grants to the UGC-funded institutions; and
 - (d) the reserve will not affect the calculation of student unit cost for the purpose of determining the recurrent funding requirements of the institutions and the tuition fee levels.
16. Based on the amount of recurrent grants to the individual institutions in the 1998/99 to 2000/01 triennium, the maximum amount of reserve that the institutions may carry over to the next triennium will be around \$7 billion in total.

FINANCIAL IMPLICATIONS

Recurrent funding proposal for the 2001/02 to 2003/04 triennium

17. The estimated total cost for implementing the UGC's recurrent funding recommendations for the 2001/02 to 2003/04 triennium is \$36,269.5 million at the 2001-02 Estimates price levels. In line with the normal arrangement governing triennium funding, once this amount is determined, it will not be adjusted during the triennium except for adjustments to take into account the civil service salary adjustment and the difference between the estimated and actual tuition fee income.

18. Compared to the 1998/99 to 2000/01 triennium, the 2001/02 to 2003/04 triennium will provide less sub-degree places and more places at degree and above levels. As more students will pay a higher tuition fee, we estimate that the requirement for means-tested grants under the existing Local Student Finance Scheme in the next triennium will on average increase by about \$19 million a year.

19. Subject to Members' agreement, we will include the necessary provision for the first nine months of the 2001/02 academic year in the 2001-02 draft Estimates. For the expenditure in the remainder of the 2001/02 to 2003/04 triennium, we will include sufficient provision in the annual Estimates of the relevant financial years.

/Supplementary

⁽⁷⁾ Examples are surplus in tuition fee income as a result of the Administration approving a higher level of tuition fee than that assumed in the calculation of the Cash Limit, or across-the-board adjustment to the terms and conditions of the civil service such as the lowering of entry salary.

Supplementary provision for the 2000/01 academic year

20. If Members approve the proposal to provide supplementary provision of \$522.4 million to meet the institutions' shortfall in tuition fee income in the 2000/01 academic year, we shall offset the supplementary provision by reserving an equivalent amount under Head 106 Miscellaneous Services Subhead 251 Additional commitments.

21. As a result of the freeze in the tuition fee levels, the estimated requirement for grants to students under the Local Student Finance Scheme will be reduced by about \$38.6 million for the 2000/01 academic year or the 2000-01 financial year.

BACKGROUND INFORMATION

22. We submit the recurrent funding requirements of the UGC-funded institutions to Finance Committee for consideration on a triennial basis. Recurrent funding to the institutions for the 1998/99 to 2000/01 triennium was considered by the Finance Committee in March 1998 (ref. FCR(97-98)111). Members accepted the financial implications for recurrent grants totalling \$35,399.4 million for the eight institutions.

23. As a result of the Government's decision to freeze the tuition fee levels for the 1998/99 and 1999/2000 academic years at the 1997/98 levels, Members approved supplementary provision of \$129.5 million and \$329.7 million to the UGC-funded institutions in 1998-99 and 1999-2000 respectively to meet their shortfall in tuition fee income (ref. FCR(98-99)70 and FCR(1999-2000)39). In view of the current economic situation, the Chief Executive in Council decided that the tuition fees for the UGC-funded institutions in the 2000/01 and 2001/02 academic years should continue to be frozen.

24. Expenditure on tertiary education accounts for about one-third of Government's education budget. We are pleased that the cost containment measure as recommended by the UGC and accepted by the Administration has been gradually achieved over the 1998/99 to 2000/01 triennium without detriment to the quality of education.

25. We briefed the Legislative Council Panel on Education at its meeting on 15 January 2001.

Enclosure 1 to FCR(2000-01)72

Indicative Student Number Targets for the 2001/02 to 2003/04 Triennium

Institutions	Target Undergraduate Places			
	2001/02	2002/03	2003/04	Total
CityU	7,134	7,134	7,134	21,402
HKBU	3,964	4,038	4,068	12,070
LU	2,043	2,037	2,037	6,117
CUHK	9,284	9,291	9,259	27,834
HKIED	1,787	2,453	2,919	7,159
PolyU	7,396	7,361	7,311	22,068
HKUST	5,524	5,483	5,457	16,464
HKU	9,103	9,025	8,972	27,100
Total	46,235	46,822	47,157	140,214

Institutions	Target Taught Postgraduate Places			
	2001/02	2002/03	2003/04	Total
CityU	914	896	853	2,663
HKBU	336	346	353	1,035
LU	-	-	-	-
CUHK	1,015	1,009	1,005	3,029
HKIED	474	508	561	1,543
PolyU	847	831	814	2,492
HKUST	540	493	456	1,489
HKU	1,510	1,435	1,375	4,320
Total	5,636	5,518	5,417	16,571

Institutions	Target Research Postgraduate Places			
	2001/02	2002/03	2003/04	Total
CityU	370	373	378	1,121
HKBU	137	138	139	414
LU	17	17	17	51
CUHK	1,193	1,235	1,275	3,703
HKIED	-	-	-	-
PolyU	351	364	381	1,096
HKUST	774	813	850	2,437
HKU	1,193	1,235	1,275	3,703
Total	4,035	4,175	4,315	12,525

Institutions	Target Sub-degree Places			
	2001/02	2002/03	2003/04	Total
CityU	4,725	4,725	4,725	14,175
HKIED	3,135	2,517	2,003	7,655
PolyU	4,725	4,725	4,725	14,175
Total	12,585	11,967	11,453	36,005

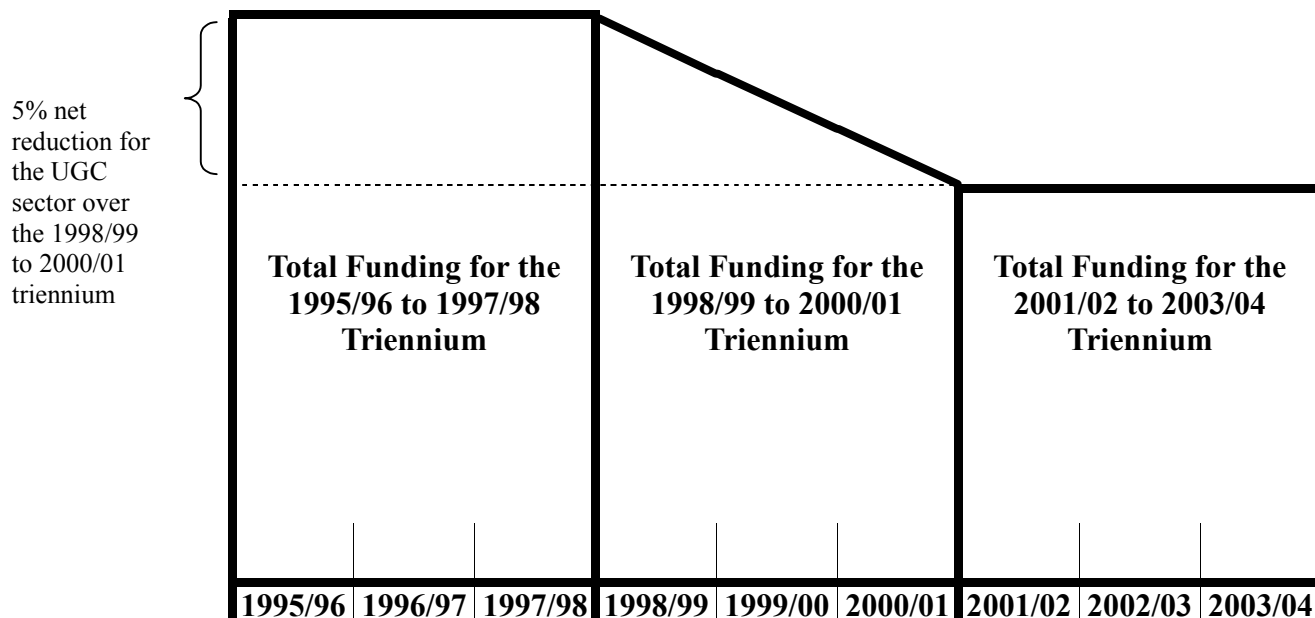
Institutions	Grand Total			
	2001/02	2002/03	2003/04	Total
CityU	13,143	13,128	13,090	39,361
HKBU	4,437	4,522	4,560	13,519
LU	2,060	2,054	2,054	6,168
CUHK	11,492	11,535	11,539	34,566
HKIED	5,396	5,478	5,483	16,357
PolyU	13,319	13,281	13,231	39,831
HKUST	6,838	6,789	6,763	20,390
HKU	11,806	11,695	11,622	35,123
Total	68,491	68,482	68,342	205,315

Note

The above figures are indicative only. There may be minor redistribution among institutions in the course of the triennium.

Diagram to Illustrate the Effect of Reduction in Average Student Unit Cost

Average Student Unit Cost



Note

For simple illustration, it is assumed that the student number is maintained at the same level over the three triennia.

Enclosure 3 to FCR(2000-01)72

**Table 1 : Student Number Targets
1998/99 to 2000/01 Vs 2001/02 to 2003/04 Triennia**

Target Undergraduate (Ug) Number				
Institutions	1998-2001 Triennium¹	2001-04 Triennium	Difference	
			No.	%
CityU	22,225	21,402	-823	-3.7%
HKBU	12,045	12,070	25	0.2%
LU	6,210	6,117	-93	-1.5%
CUHK	27,626	27,834	208	0.8%
HKIED	324	7,159	6,835	2109.6%
PolyU	22,625	22,068	-557	-2.5%
HKUST	17,024	16,464	-560	-3.3%
HKU	27,098	27,100	2	0.0%
Total	135,177	140,214	5,037	3.7%
Ug as % of Total	65.8%	68.3%		
Target Taught Postgraduate (TPg) Number				
Institutions	1998-2001 Triennium¹	2001-04 Triennium	Difference	
			No.	%
CityU	2,805	2,663	-142	-5.1%
HKBU	615	1,035	420	68.3%
LU	-	-	-	-
CUHK	3,012	3,029	17	0.6%
HKIED	180	1,543	1,363	757.2%
PolyU	2,562	2,492	-70	-2.7%
HKUST	1,680	1,489	-191	-11.4%
HKU	4,656	4,320	-336	-7.2%
TPg held in reserve ²	180	-	-180	-100.0%
Total	15,690	16,571	881	5.6%
TPg as % of Total	7.6%	8.1%		
Target Research Postgraduate (RPg) Number				
Institutions	1998-2001 Triennium¹	2001-04 Triennium	Difference	
			No.	%
CityU	705	1,121	416	59.0%
HKBU	192	414	222	115.6%
LU	45	51	6	13.3%
CUHK	2,394	3,703	1,309	54.7%
HKIED	-	-	-	-

PolyU	630	1,096	466	74.0%
HKUST	1,530	2,437	907	59.3%
HKU	2,604	3,703	1,099	42.2%
RPg held in reserve ²	2,685	-	-2,685	-100.0%
Total	10,785	12,525	1,740	16.1%
RPg as % of Total	5.3%	6.1%		
Target Sub-degree (SD) Number				
Institutions	1998-2001 Triennium ¹	2001-04 Triennium	Difference	
			No.	%
CityU	14,175	14,175	0	0.0%
HKIED	15,380	7,655	-7,725	-50.2%
PolyU	14,175	14,175	0	0.0%
Total	43,730	36,005	-7,725	-17.7%
SD as % of Total	21.3%	17.5%		
Grand Total				
Institutions	1998-2001 Triennium ¹	2001-04 Triennium	Difference	
			No.	%
CityU	39,910	39,361	-549	-1.4%
HKBU	12,852	13,519	667	5.2%
LU	6,255	6,168	-87	-1.4%
CUHK	33,032	34,566	1,534	4.6%
HKIED	15,884	16,357	473	3.0%
PolyU	39,992	39,831	-161	-0.4%
HKUST	20,234	20,390	156	0.8%
HKU	34,358	35,123	765	2.2%
TPg held in reserve ²	180	-	-180	-100.0%
RPg held in reserve ²	2,685	-	-2,685	-100.0%
Total	205,382	205,315	-67	0.0%

Notes

1. The column reflects the planning targets for the 1998/99 to 2000/01 triennium, and does not include subsequent variations such as the upgrading of HKIED's sub-degree teacher education places to degree and above levels.
2. At the beginning of the 1998/99 to 2000/01 triennium, some TPg and RPg numbers were held in reserve by the UGC for distribution to the institutions during the triennium.

**Table 2 : Recurrent Funding
1998/99 to 2000/01 as compared to 2001/02 to 2003/04**

	(A) 1998-2001 Triennium	(B) 2001-04 Triennium	Difference	
			(B - A)/(A)	
	\$ million	\$ million	\$ million	%
Funding for eight UGC-funded Institutions				
<i>Government grant</i>	36,148.1	33,772.4	-2,376	-6.5%
<i>Assumed income</i>	10,052.3	10,212.7	160	1.6%
<i>Total Funds</i>	46,200.4	43,985.1	-2,215	-4.8%
Earmarked Research Grants (ERG)	1,286.0	1,632.0	346	26.9%
Teaching Development Grants	172.5	115.0	-58	-33.3%
Language Enhancement Grants	217.5	217.5	0	0.0%
Central Allocation Vote (CAV) including Areas of Excellence, etc.	489.0	525.6	37	7.5%
Grand Total to the UGC-funded Institutions				
<i>Government grant</i>	38,313.1	36,262.5	-2,051	-5.4%
<i>Assumed income</i>	10,052.3	10,212.7	160	1.6%
<i>Total Funds</i>	48,365.4	46,475.2	-1,890	-3.9%

Notes:

- 1 UGC will retain some money to administer inter-institutional projects, which amount to \$2.3 million, \$2.3 million and \$2.4 million for 2001/02, 2002/03 and 2003/04 respectively.
- 2 Funding for the 1998/99 to 2000/01 triennium includes \$522.4 million supplementary provision as proposed under paragraph 2(b) of the Finance Committee Agenda Item for approval by the Finance Committee.
- 3 Some of the provision originally approved for CAV in the 1998/99 to 2000/01 triennium has been reclassified under the institutional grant and ERG in accordance with the classification for the 2001/02 to 2003/04 triennium.

Methodology for Determining the Levels of Recurrent Grants to the UGC-funded Institutions

The recurrent grants for the UGC-funded institutions are largely determined based on a methodology developed by the UGC in 1994 and improved over the years. In short, the amount of grant comprises three elements:

- (a) Teaching – about 75%
- (b) Research – about 23%
- (c) Professional Activity – about 2%

Teaching Element

2. The **Teaching** element is based on the student numbers, their levels (i.e. sub-degree, first degree, taught postgraduate and research postgraduate), mode of study (i.e. part-time and full-time) and disciplines of study. Some subjects are more expensive than others because they require special equipment, laboratory or more staff time, etc. Relative weighting by broad academic programme categories (APC) is shown in the following table:

	APC	Relative cost weightings		
1.	Medicine	4.0	-	5.0
2.	Dentistry	3.5	-	5.0
3.	Studies Allied to Medicine & Health	1.4	-	2.4
4.	Biological Sciences	1.3	-	3.8
5.	Physical Sciences	1.3	-	3.2
6.	Mathematical Sciences	0.9	-	1.5
7.	Computer Science & IT	0.9	-	1.5
8.	Engineering & Technology	1.2	-	2.3
9.	Architecture & Town Planning	1	-	1.6
10.	Business & Management Studies	0.8	-	1.6
11.	Social Sciences	1	-	1.6
12.	Law	1	-	1.6
13.	Mass Communication & Documentation	1	-	1.6
14.	Languages & Related Studies	0.8	-	1.5
15.	Humanities	0.9	-	1.2
16.	Arts, Design & Performing Arts	1.3	-	1.8
17.	Education	0.9	-	1.4

Research Element

3. The **Research** element is primarily related to the number of active research workers and the cost of research in respective fields. The number of active research workers in each cost centre was identified in the context of the Research Assessment Exercise last conducted in 1999 which assessed the research performance of different institutions and different cost centres within an institution.

Professional Activity Element

4. This element of funding is associated with professional (non-research) activities which should be undertaken by all members of academic staff. It is calculated based on the number of academic staff.

Allocation within Institutions

5. The UGC formula only serves as a basis for determining the allocation to the UGC-funded institutions. Once allocations are approved, institutions have a high degree of freedom and responsibility for determining the best use of the resources vested in them.

**For Information
on 19 February 2001**

Legislative Council Panel on Education

**RECURRENT FUNDING FOR THE UNIVERSITY GRANTS COMMITTEE-
FUNDED INSTITUTIONS IN THE 2001/02 TO 2003/04 TRIENNIUM**

Introduction

This note provides supplementary information on the key issues raised by members of the Finance Committee and members of the public regarding the recurrent funding for the University Grants Committee (UGC)-funded institutions for the 2001/02 to 2003/04 triennium.

Agreement on Unit Cost Reduction

2. In its report on “Higher Education in Hong Kong” published in 1996, the UGC considered that as the sector entered a consolidation phase, the sector should be able to achieve a 10% reduction in unit cost by the end of the 1998/99 to 2000/01 triennium without detriment to quality. In recommending the cost savings, the UGC took note of the fact that during a period of consolidation, institutions should be able to turn their energies from expansion to productivity and quality. They will also be able to reap the benefits from savings associated with economies of scale and the abandonment of ‘front-end loading’¹. Furthermore, certain tasks associated with expansion will no longer be necessary and institutions will be able to improve management procedures.

3. The Administration accepted the UGC’s advice, and agreed that the following parameters should form the basis for determining the funding requirements for the UGC-funded institutions for the current triennium:

- (a) The target 10% reduction in student unit cost should be achieved **gradually** over the 1998/99 to 2000/01 triennium. In line with this spirit, the Administration has accepted the UGC’s proposal to have a point-to-point² reduction, rather

¹ Front-end loading means the additional resources required during the start-up phase of an institution or an academic programme.

² Point-to-point reduction means cost savings achieved day-by-day along a sliding slope from 0% reduction at the starting point of the 1998/99 academic year to 10% reduction by the end point of the 2000/01 academic year. A diagrammatic illustration is at **Annex**.

than the normal year-on-year reduction. The savings achievable under the former approach (which we adopted) are some \$370m less than the latter.

- (b) Half of the savings should be ploughed back to the UGC in support of new developments such as Areas of Excellence Scheme and other quality assurance initiatives.
- (c) As the Hong Kong Institute of Education (HKIEd) is a new institution that came under the aegis of the UGC in 1996/97, HKIEd should be exempt from the student unit cost reduction.

4. The above agreement was made in 1996, and was promulgated through various documents including a Legislative Council brief (EMB CR 3/21/2041/89 V in November 1996) and a press release. The principles were reiterated in item for Finance Committee (FCR(97-98)111 dated 27 March 1998), and formed the basis for Finance Committee's approval of the recurrent funding for the UGC-funded institutions in the current triennium. Based on the above agreement -

- (a) the net savings to be delivered by the UGC-sector is 5% overall; and
- (b) the 5% savings to Government will be delivered over two triennia. In other words, the savings delivered in the 1998/99 to 2000/01 triennium are only **2.5%** of the total UGC recurrent expenditure in that triennium, or **\$1,115m** in money terms (in 1997-98 price). The remaining **2.5%** savings, or **\$1,166m** (in 2000-01 Estimates price), will only be delivered in the next triennium. A diagrammatic illustration is at **Annex**.

5. Since we finalised the funding for the 1998/99 to 2000/01 triennium in late 1997, the Government launched an Enhanced Productivity Programme (EPP) with a target savings of 5% of baseline expenditure. We have exempted the UGC sector from EPP in view of the student unit cost reduction. With only a total of 5% savings to be returned to Government over a period of six years, the UGC sector is in fact doing no more than what the entire public sector (including the Hospital Authority, the Vocational Training Council and the welfare sector) is required to achieve in terms of efficiency gains.

Implementation of the Agreement

6. We note that the institutions have been making efforts to control costs and achieve productivity gains. As a result, we expect cash-flow surpluses to the order of some \$5 billion in the entire UGC sector by the end of the triennium, representing 13.9% of the institutional grant for this triennium. Of this amount, about \$3.5 billion (or 9.7%) is intended for specific purposes, such as maintenance of buildings, replacement of equipment or deferred payment of staff costs. The amount of unappropriated surplus should still be substantial, amounting to about a third of total. Indeed, it is in view of this situation that we have proposed a mechanism to allow institutions to carry unspent funds from one triennium to the next, to increase the institutions' flexibility in financial management and to encourage longer term planning. A significant feature of the new mechanism is that the reserve will not affect the calculation of student unit cost for the purpose of determining the level of Government funding or the level of tuition fees. In other words, the amount of reserve will not be used to offset the level of Government funding as determined by the established methodology.

Sources of Funding other than the Block Grant

7. In addition to the recurrent block grant, institutions receive other sources of Government funding:

- (a) UGC provides earmarked grants for specific purposes including Earmarked Research Grant, Teaching Development Grant, Language Enhancement Grant and funding for Areas of Excellence Scheme, quality assurance initiatives and other projects. The amount is budgeted to be \$2.5 billion in the 2001/02 to 2003/04 triennium. Within this provision, the Earmarked Research Grant will increase significantly by \$346m (or 27%) over the current triennium.
- (b) Government provides additional funding to implement the UGC Home Financing Scheme (UGC HFS). The amount is estimated at \$689m in 2000-01, or \$1.6 billion in the current triennium.
- (c) Government reimburses the UGC-funded institutions for rates and Government rents on a recurrent basis. The provision for 2000-01 is over \$160m.

- (d) Government provides funding for UGC capital projects. The total capital works expenditure amounts to \$1.1 billion in 2000-01.
- (e) In the past three years (1998-99 to 2000-01), the Innovation and Technology Fund (and its predecessor, the Industry Support Fund) disbursed \$417m to the UGC-funded institutions in support of 127 projects, representing a 77% increase over the allocation of \$235m during the period from 1995-96 to 1997-98.
- (f) The UGC-funded institutions also received \$366m grant from the Quality Education Fund since 1998 in support of 118 projects.

8. Universities are also encouraged to explore new sources of income, such as technology transfer companies, self-financing courses and donations, for the enhancement of the institutions' development. These sources of income will not be counted as 'assumed income' and will not lead to any corresponding reduction in the block grant.

Comparison between the Current and Next Triennia

9. **The Administration has not requested further reduction in the unit cost beyond the agreed 10% target.** Based on the funding allocations, the student unit cost for the next triennium will only be 1% less than the 2000/01 level. This reduction merely reflects the deflation during the current triennium.

	Average student unit cost (Nominal price level)	% Change
1995/96 to 1997/98	\$209,507	
1998/99	\$240,714	+14.9%
1999/2000	\$234,428	-2.6%
2000/01	\$228,544	-2.5%
2001/02 (projected)] \$226,360	-1%
2002/03 (projected)] \$226,360	-0%
2003/04 (projected)] \$226,360	-0%

10. The estimated recurrent funds required by the UGC-funded institutions in the next triennium will be about \$1.9 billion (or 3.9%) less than that in the current triennium. The difference is attributable to the following three factors:

<i>Reasons</i>	<i>Amount (\$ Billion)</i>	<i>%</i>
Full triennial effect of the student unit cost reduction (See para. 4(b) above)	\$1.2	2.5% ³
Deflation during the current triennium	\$0.5	1%
Reduction in student number target	\$0.2	0.4%
Total	\$1.9	3.9%

Methodology in Calculating Cash Limit

11. The established practice, ever since the inception of the UGC system, is to adopt a crude average student unit cost in determining the Cash Limit for the UGC sector. This was consistently used as the basis for the discussion between the Administration and the UGC on triennial funding, and it was on this basis that the Administration has agreed to the overall student numbers and the changes in student load matrices, including a 20% increase in research postgraduate places by the end of the triennium.

12. The UGC has pointed out that the present formula will impose funding constraints on the UGC as we seek a progressive increase in degree and above places to be offset by a reduction in the less costly sub-degree places in the next triennium. The Administration sees the merit in the argument and agrees, in principle, that student mix and student unit cost by levels should be taken into account in determining funding for the UGC sector in future, **subject to the availability of resources**.

Measures to Lessen the Financial Burden on Institutions

13. To ameliorate the possible financial constraints of the UGC-funded institutions in the next triennium -

³ As HKIED is not subject to the unit cost reduction, the sum is worked out to be close to but not exceeding 2.5%.

- (a) We have recommended to the Finance Committee a new mechanism so that institutions can carry over up to 20% of their recurrent grants to the next triennium. With this, the institutions will be able to keep surpluses amounting to a few billion dollars in total which otherwise would have to be returned to Government. Likewise, with the new mechanism, it will be possible for the UGC to distribute to the institutions any savings it can achieve by the end of the triennium, as additions to the block grant. The UGC expects to have around \$250m available.
- (b) The Administration has agreed that the UGC may retain the savings arising from the lowering of the entry salary scales in the light of the adjustment to the Civil Service Entry Pay for the next triennium. The UGC has taken a decision that for the coming triennium such savings could be kept and deployed by the institutions when achieved. The savings, which are estimated to be in the range of \$49m, could be kept and deployed by the institutions when achieved.
- (c) The Administration will endeavour to identify savings during the next triennium for further allocation to the UGC, should the UGC sector encounter any genuine financial difficulties. The amount cannot be quantified at this moment.

Funding for the Whole Higher Education Sector

14. Government has been investing heavily in education. Education is the biggest public expenditure item. About 23% of the recurrent Government expenditure is spent on education, and of this, one third is devoted to higher education.

15. As announced by the Chief Executive in his 2000 Policy Address, we will support the progressive increase in post-secondary education opportunities. Our target is that, within 10 years, 60% of our senior secondary school graduates will have access to post-secondary education. We envisage that the expansion will come from self-financing programmes outside the UGC sector. In achieving this target, we plan to provide capital assistance to the potential providers and financial assistance to the students. We will present a package of initiatives to the Legislative Council Panel on Education in the first half of 2001. Subject to the Council's approval, additional funds will be provided in support of the post-secondary education sector.

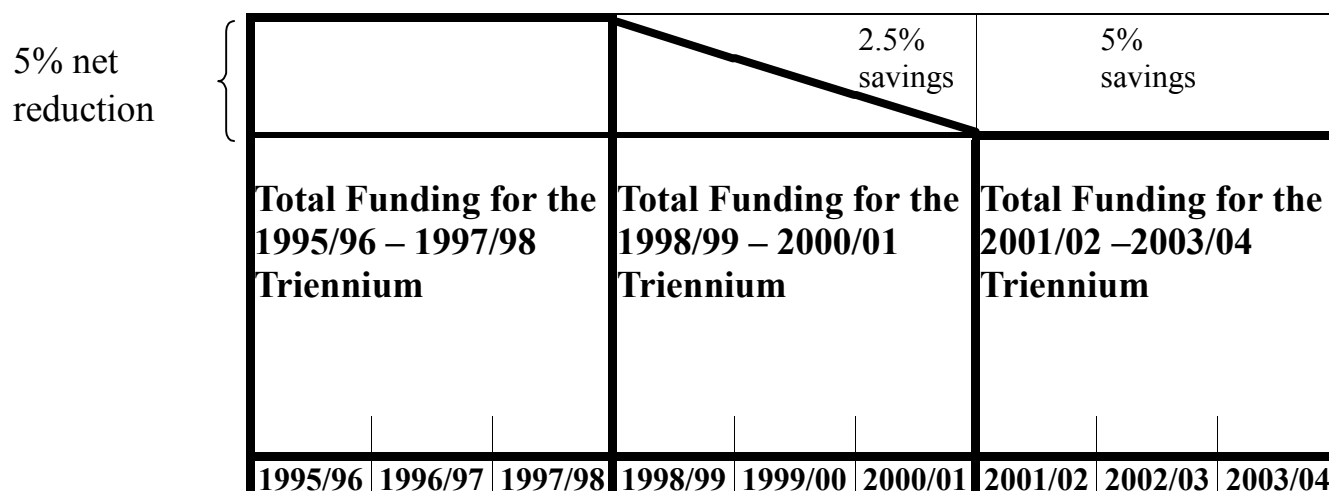
Quality Assurance

16. A prerequisite of productivity enhancement programmes is that quality must not suffer. This is particularly so for the education sector. The UGC takes on itself the responsibility of ensuring this and has introduced various measures towards the goal of quality assurance, for example, the Teaching and Learning Quality Process Review and the Management Reviews. For the next triennium, the UGC has set aside \$700m as Performance-related funding for further distribution to the institutions after a broad-based assessment exercise and further dialogue with the institutions.

17. There have been concerns about the possibility of large classes because of funding constraints. At present, the student-teacher ratio of our local institutions ranges from 10 to 16, with an average of 12.4. This ratio is broadly in line with the tertiary education sector in comparable economies.

Diagram to illustrate the effect of reduction in average student unit cost

Average Student Unit Cost



NOTES

1. For simple illustration, it is assumed that the student number will be maintained at the same level over the three triennia.
2. The Government agreed that half of the savings from the 10% unit cost reduction should be retained by UGC for the development of Areas of Excellence, etc. The net reduction for the entire UGC sector is therefore about 5%.
3. With student unit cost reduced gradually over the current triennium, the total funding provided for the current triennium will be 2.5% lower than the previous triennium. The funding to be available in the next triennium will also be 2.5% less than that of the current triennium.