

**Information Paper for the
Bills Committee on Public Officers Pay Adjustment Bill**

**2002 Civil Service Pay Adjustment :
Impact on the Subvented Sector**

Purpose

In response to Members' questions on this subject, the Administration has prepared this paper to explain the impact of the 2002 Civil Service Pay Adjustment on the subvented sector.

Impact on subventions

2. Many subvented organisations receive recurrent government subvention which is price adjusted annually according to formulae including a factor of civil service pay adjustment. For these organisations, their subvention is increased when civil service pay is increased. In accordance with this adjustment mechanism, we will reduce government subventions to reflect the revised factor of civil service pay adjustment, if civil service pay is cut with effect from 1 October 2002.

3. For other subvented organisations who receive subventions determined on the basis of formulae without a factor of civil service pay adjustment, their subventions will not be affected by a civil service pay increase or civil service pay reduction. Examples of such organisations include the Employees Retraining Board whose subvention is adjusted annually according to movement of the Consumer Price Index, and Hong Kong Trade Development Council whose annual subvention is set at 60% of the total amount of trade declaration charge on imports, domestic exports and re-exports received in the preceding financial year.

4. At Annex A is a list of the organisations receiving recurrent subventions from the Government and a summary of how the subventions will be affected by a reduction in civil service pay.

Impact on the pay of subvented staff

5. Government subvention to an organisation is a separate matter from the organisation's pay to its staff. Subvented sector staff are employees of the subvented organisations, and the employment relationship is governed by the relevant law and the private contract between the employee and the organisation as the employer. Each subvented organisation is an independent employer and together they employ over 150,000 staff in the subvented sector. There are large variations among the organisations, and in some cases among different groups of staff of the same organisation, in remuneration policies, staff categories and contract terms. Given this variety, a reduction in civil service pay may have different implications for different subvented organisations.

6. There are other factors which may determine the impact of a civil service pay cut on the pay of those employees whose remuneration is paid for by government subvention (hereafter referred to as "subvented staff"). In general, subvented organisations have to take into account the following factors when considering whether it is necessary to cut the pay of their subvented staff following a pay cut in the civil service -

- (a) whether there is any established government policy linking the pay of their subvented staff to civil service pay or civil service pay adjustment. For instance, the pay for academic, clinical and senior administrative staff of the UGC-funded institutions is linked to civil service pay, in accordance with criteria approved by the Finance Committee of Legislative Council. The pay of staff in the Hospital Authority (HA) is determined by the HA Board in accordance with the Hospital Authority Ordinance. In exercising its authority, the HA Board has regard to the principles endorsed by the Executive Council in 1990. The pay of teachers occupying established posts in the aided schools is pegged to civil service pay points according to the relevant Codes of Aid;
- (b) for subvented staff who are not subject to specific government policies on their remuneration, whether their remuneration packages will remain no better than those for comparable civil service ranks after an adjustment of civil service pay. This is a matter of compliance with the general subvention principle that the terms of service for subvented staff

should be no better than those of comparable civil service ranks. We have attached at Annex B relevant extracts from the Miscellaneous Subventions - Guidelines on the Management and Control of Government Subventions explaining this principle of “no better than”. An illustration of how the principle operates is at Annex C;

- (c) the Administration’s decision to allow organisations some leeway to phase in adjustments necessary for compliance with the requirements in (a) and (b) above (please also see paragraph 7 below), provided that the subvented organisations manage to absorb the cost of such phasing in arrangement; and
- (d) for subvented staff whose remuneration packages remain at levels lower than those of comparable civil service ranks after a reduction in civil service pay, the organisation may decide not to reduce the pay of the concerned subvented staff if it can manage financially, taking into account any reduction in subvention as a result of a reduction in civil service pay.

7. As regards paragraph 6(c), if a subvented organisation needs to revise a remuneration package for it to remain compliant with the requirements under the remuneration policies/subvention principle in paragraph 6(a) and (b) above, we expect the organisation to apply that revised package to their new recruits to the subvented posts with immediate effect. As for serving staff, we will allow flexibility if the subvented organisations decide not to cut the remuneration of existing contracts out of contractual considerations, on the understanding that this is a transitional arrangement for time-limited contracts and that the situation will be rectified upon contract renewal. That said, this flexibility will not be a justification for exemption from any downward adjustment in subvention following a civil service pay cut (see paragraph 2 above). In other words, where subvention has been reduced, the subvented organisations wishing to grandfather the remuneration of any of their publicly-funded employees for the remaining duration of these employees’ existing contracts will have to absorb the costs of grandfathering within the reduced subvention or with their reserves accumulated from unspent subventions. Of course, as illustrated at Annexes B and C, there will be no conflict with the “no better than” principle if the subvented organisations use private funds to support the “excess” cost in a package which is better than that for comparable civil service ranks, both for existing and new contracts.

Implementation of pay cuts in the subvented sector

8. If, after considering its own circumstances and the factors in paragraphs 6 above, a subvented organisation decides that it is necessary to reduce the pay of its staff following a civil service pay cut, it must give due regard to its contractual obligations and the law, including in particular the Employment Ordinance which governs private employment contracts and any other laws relevant to the organisation.

9. For contracts that do not carry an express provision to allow for unilateral reduction of pay, the organisation may seek the consent of the affected employees to the reduction. Depending upon the factors set out in the Employment Ordinance, unilateral variation of contract terms could subject the employer to statutory claims. If an individual employee refuses to consent to a pay cut and the conditions which would allow unilateral variation are not met, the organisation may consider terminating the contract in accordance with the provisions of the Employment Ordinance, the contractual terms and any other statutory provisions applicable to the organisation. Subvented organisations are encouraged to seek legal advice and to contact the Labour Relations Division of the Labour Department on what they should do to comply with the Employment Ordinance and to minimise disputes. They are also encouraged to make reference to a booklet issued by the Labour Department entitled “Guidelines on what to do if wage reductions and retrenchments are unavoidable”.

10. The proposed civil service cut may lead to financial and personnel management issues for subvented organisations. Given so, the Administration has considered whether it should introduce legislative provisions enabling subvented organisations to lawfully reduce the pay of their staff without having to seek their consent, while protecting the organisations from claims from employees. After careful consideration, the Administration has decided against such legislation. The major consideration is that unlike civil service employment, employment in the subvented sector, like employment in the rest of the private sector, is governed by the Employment Ordinance. The Ordinance sets out clearly the rights and obligations of, and protection available to, employees and employers. It provides for variation of contract terms through mutual consent and termination of contracts under prescribed conditions. Therefore, we think it is undesirable to legislate for a pay cut in the subvented sector, and in so doing,

override the rights and obligations under the Employment Ordinance. We also believe that such a move is unnecessary, since in the vast majority of cases the Employment Ordinance will already provide an adequate framework for the subvented organisations and their employees to resolve issues that might arise from the cut in civil service pay and subventions.

11. Individual subvented organisations will have to make their own management decisions on how to cope with the proposed reduction in civil service pay and subventions, and if necessary on how to implement a pay cut in a lawful manner. We think the situation will be manageable generally if both the management of the subvented organisations and their subvented staff act in a reasonable manner and seek to resolve disputes through constructive discussions. In this regard, we hope the flexibility that we are allowing under paragraph 7 above will help to contain the problem arising from existing contractual obligations. It is also incumbent upon subvented staff to consider the prospect of a pay cut in an objective and rational manner, taking into account the potential effect on the people they serve, the financial position of the subvented organisations, their own pay rises in previous years with reference to civil service pay, the sentiments of the community and the overall interests of Hong Kong. In this regard, we are encouraged that some staff representatives from the subvented sector have publicly expressed their willingness to sail through difficult times together with the civil service and the rest of the community.

12. In the event that a subvented organisation has to terminate the employment of individual employees who refuse to give consent to a pay cut, it will have to assess the amount of termination compensation with reference to statutory provisions in the Employment Ordinance and the terms of the employment contracts. In this regard, we note that individual subvented organisations have accumulated some reserves or have other sources of income which may help them tide over the short-term difficulties. We do not preclude the possibility of the Administration offering some short-term tide over financial assistance if individual organisations have genuine difficulties shouldering the termination compensation, subject to the merits of each case and Government's budgetary considerations. Naturally, we have to ensure the proper use of public funds in such circumstances.

13. Since the announcement in the 2002 Budget Speech on an assumed civil service pay reduction for budgetary purposes, the Controlling Officers have been keeping the subvented organisations under their purview informed of the latest

position and the implications for them in the event civil service pay is reduced. The Controlling Officers will continue to be in close touch with the organisations.

14. Individual organisations may have their unique problems, and we will try to render assistance suited to the problems. For example, the institutions funded by the University Grants Committee (UGC) have raised with us the unique problems of implementing a pay cut in respect of certain categories of staff whose employment, according to the statute of some universities, can only be terminated with a “good cause” which carries a restricted meaning. In the event that individual staff members under this category refuse to accept a pay cut, the institutions may not have the choice of terminating their appointments as the claims for breach of contract and damages by the staff who are protected by “good cause” could be substantial. The Administration fully appreciates the unique situation of the UGC-funded sector and has already started examining with the institutions and the UGC the nature and extent of the problem with a view to identifying a unique solution to resolve the problem. Meanwhile, we are awaiting institutions’ further analysis of the categorisation of staff and their contract terms.

Finance Bureau
14 June 2002

Annex A

| Categories of subvented organisations | No. of organisations in the category | No. of staff (as of Dec 2001) | Approved provision in 2002-03 Estimates (\$ million) | Estimated full year effect of reduction in funding if civil service pay is reduced with effect from 1.10.2002 (\$million) |
|---|--------------------------------------|-------------------------------|--|---|
| Hospital Authority | 1 | 49 655 | 29,880.6 | 642.5 |
| Schools | 1 200* | 48 069 | 26,998.0 | 557.6 |
| UGC-funded institutions | 8 | 19 535 | 11,945.2 | 375.0 |
| Non-government organisations in the welfare sector | 186 | 22 131 | 7,070.7 | 157.5 |
| Vocational Training Council | 1 | 3 532 | 2,031.7 | 52.8 |
| NGOs in the health sector | 9 | 712 | 279.0 | 4.6 |
| Legislative Council Commission | 1 | 322 | 246.6 | 4.7 |
| Hong Kong Sports Development Board | 1 | 273 | 189.7 | 2.6 |
| Hong Kong Academy for Performing Arts | 1 | 271 | 177.2 | 3.2 |
| Office of the Ombudsman | 1 | 94 | 97.8 | 1.9 |
| Equal Opportunities Commission | 1 | 84 | 80.7 | 1.3 |
| Office of the Privacy Commissioner for Personal Data | 1 | 44 | 37.1 | 0.5 |
| Other subvented organisations whose funding will be reduced | 12 | 1 752 | 1,286.4 | 14.8 |
| Subvented organisations whose funding will not be reduced | 20 | 5 534 | 1,200.7 | 0 |
| Total : | | 152 008 | 81,521.4 | 1,819.0 |

*Estimated figure

**Miscellaneous Subventions -
Guidelines on the Management and Control of Government Subventions**

Relevant extracts on terms of service

“ 1.3 It is accepted that given the wide range of disparate organisations receiving subventions, the guidelines may not be universally applicable. If a Controlling Officer considers that a subvented organisation should be exempted from certain parts of these guidelines, he should seek the advice of Finance Branch. If it is subsequently agreed that an exemption should be granted, the Controlling Officer may so inform the subvented organisation in writing. In some cases, the Ordinance governing the operation and control of a subvented organisation may depart from these guidelines. In such cases the guidelines are of course subservient to the relevant Ordinance.”

“ 3.30 As a general rule, the terms of service for subvented posts may not be superior to those offered by the Government to comparable grades in the Civil Service. This does not mean that an organisation's terms of service must always be the same as the Government's; and Government is not obliged to increase its subvention to enable an organisation to maintain its terms of service at any particular level. Where the terms of service for subvented posts exceed the equivalent Government conditions, a subvention should be payable only up to the estimated equivalent cost of meeting the level of the Government's conditions.”

“ 3.31 In examining an organisation's terms of service, the Controlling Officer should -

- (i) study the organisation's grading structure, salary scales and fringe benefits and ensure that the total benefits available to staff do not exceed those that would be made available to comparably graded civil service staff. In reaching judgements on this issue, Controlling Officers may find it helpful to examine salaries and

benefits separately;

- (ii) in all instances ensure that the organisation's total expenditure on staff does not exceed the cost that would be incurred if the organisation were staffed by civil servants in comparable grades; and
- (iii) keep abreast of terms of service offered by the organisation and any changes to these conditions. “

“ 3.32 Where there is any doubt on the comparability of ranking and terms of service, the Controlling Officer should seek advice from Finance Branch and Civil Service Branch. The Controlling Officer may engage the services of management consultancy firms to advise on such issues. The recommendations of the consultants are not binding on the Government.”

“ 3.33 Any adjustments to the terms of service for existing subvented posts and any proposals relating to the terms of service for new subvented posts must receive the prior agreement of the Controlling Officer who must seek the advice of Finance Branch on any proposals.”

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An Elaboration on the Subvention Principle of “No better than”

Clauses 3.30 - 3.33 of the “Miscellaneous Subventions - Guidelines on the Management and Control of Government Subventions” issued by FB in 1988 sets out general guidelines on the terms of service for subvented staff. The major principle is set out in Clause 3.30, which states that -

“As a general rule, the terms of service for subvented organisations may not be superior to those offered by the Government to comparable grades in the Civil Service”.

This note explains how the general principle of “no better than” is being implemented.

Status of the subvention guidelines vis-à-vis statutory provisions/decisions of the Executive Council and Legislative Council

2. The subvention guidelines on terms of service, including the application of the “no better than” principle, should not lead to conflicts with existing statutory provisions and decisions of the Executive Council or Legislative Council on terms of service for concerned subvented staff. If there are such conflicts, the statutory provisions and decisions of the Executive Council or Legislative Council would prevail over the subvention guidelines, unless a move is taken to amend those statutory provisions and decisions.

Whether the posts are funded by recurrent subvention

3. The main objective of the subvention guidelines is to ensure that the Government’s recurrent subvention to an organisation is used cost-effectively to deliver an agreed programme of activities. It follows that the principle of “no better than” applies only to posts that are fully or partly funded by the Government. It does not apply to posts in a subvented organisation which are funded entirely by the organisation’s other sources of income, e.g. donations.

Whether there are comparable civil service grades

4. As is clear from clause 3.30 of the subvention guidelines, the principle of

“no better than” does not apply to subvented posts for which there are no comparable civil service grades, as justified by the subvented organisations and agreed by the Administration, e.g. faculty members of UGC-funded institutions, Research and Development Directors employed by Hong Kong Applied Science and Technology Research Institute.

Other exemptions

5. The subvention guidelines also allow for exemptions from the principle of “no better than” for reasons other than those specified in paragraphs 2 to 4 above, provided that the subvented organisations are able to justify the exemption to the satisfaction of the Administration.

Approaches for assessing compliance with the rule of “no better than”

6. For cases where the rule of “no better than” should apply, the Controlling Officer will assess whether the remuneration packages offered for different groups of staff in a subvented organisation are no better than the staff cost for the comparable groups of staff in the civil service. In practice, there are various approaches representing different degree of control, as illustrated below -

(a) Comparison by individual components in a remuneration package

Under this approach, the remuneration package for a subvented post must not carry components that are not provided under civil service terms, and that the pay and on-cost for individual fringe benefits must individually be no better than those for the comparable civil service grade.

(b) Comparison by total cost of comparable components in a remuneration package

Under this approach, the Controlling Officer will identify individual components in the remuneration package and then compare the total cost of those components with the total cost of comparable cost components for corresponding civil service post. Subject to such total costs being comparable, the cost of individual component for the subvented post may exceed that for the comparable civil service grade.

(c) Comparison with reference to total cost of a comparable post in the Government

It is not necessary to identify the individual components of remuneration packages for both the subvented post and the comparable civil service grade under this approach. The only criterion to be applied is whether the total cost of the remuneration package for a subvented post is no better than the total cost of the comparable civil service post.

7. Where the approaches in paragraph 6(b) or 6(c) above are adopted, a change to the individual terms and conditions for comparable civil service grades does not necessarily mean that the subvented organisation has to make corresponding adjustment to the same component in its remuneration package for a subvented post, provided that the total cost for the subvented post is still no better than that for comparable civil service grade under approach (b) or (c), whichever is applicable.

Where the terms of service are better than those for comparable civil service grade

8. If it is revealed that the terms of service for a subvented post do not meet the “no better than” requirement under the relevant approach (paragraph 6 above) applicable to the organisation, as a general approach the subvented organisation is required to rectify the imbalance as follows -

- (a) adjust the terms of service for new recruits so that the package becomes no better than that for the comparable civil service rank, and rectify the cases of serving staff upon renewal of contracts; or
- (b) where the subvented organisation prefers to offer a better package for both new recruits and serving staff, it should use its own resources (other than subvention or reserves built up from savings in subvention) to fund any excess over the equivalent government remuneration. This is in accordance with clause 3.30 of the subvention guidelines which states that -

“Where the terms of service for subvented posts exceed the equivalent Government conditions, a subvention should be payable only up to the estimated equivalent cost of meeting the level of the Government’s conditions.”

The resultant savings in subvention should be returned to the Government or redeployed to deliver the agreed programme of activities with prior agreement of the relevant Controlling Officers.

Finance Bureau

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