

Operation of Trading Funds

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Executive Summary

Nature and purpose of trading funds

1. The concept of trading funds originated from the United Kingdom (UK) in the early 1970s and was introduced in Hong Kong by the enactment of the Trading Funds Ordinance in 1993. A trading fund is a financial and accounting framework established by law to enable a government department, or part of a department, to adopt certain accounting and management practices common in the private sector.
2. A trading fund operates on a self-financing basis and does not need to seek funding from the legislature to finance its daily operations after its establishment. The principal criterion in deciding whether a department could operate as a trading fund is that it should be capable of breaking even within a reasonable period of time.
3. Trading funds are established with the intention that an institutional change would provide the appropriate flexibility in resources management and nurture a new working culture to improve services in terms of both quality and cost-effectiveness.

Operation of selected trading funds

4. Five trading funds are selected for this study, including three from Hong Kong (the Land Registry Trading Fund, the Post Office Trading Fund and the Electrical and Mechanical Services Trading Fund) and two from the UK (the Ordnance Survey Trading Fund and Her Majesty's Land Registry Trading Fund).
5. All of the five selected trading funds except the Post Office have managed to reduce both the number of civil servants and their total number of staff after attaining the trading fund status. Although the size of staff has been kept in check, staff costs continue to rise and account for more than half of their operating expenses. In Hong Kong, the pay and conditions of civil servants are fixed centrally across the board whilst, in the UK, the chief executives of the trading funds are empowered to set the pay and grading structure for civil servants under the Director grade.
6. There is a growing trend for the trading funds in the UK to draw on more commercial experience from the private sector to improve the quality of services. In the UK, the chief executives and some other senior posts are recruited through open competition, and their Non-Executive Directors come from the private sector as well whilst, in Hong Kong, the general managers of trading funds are selected from the pool of civil servants.
7. All of the trading funds under study have achieved and exceeded most of the service performance targets and have established various channels to communicate with their major customers. Nonetheless, there is no formal participation of third parties or service users in setting the performance targets.

8. With the exception of the Electrical and Mechanical Services Trading Fund, the provision of most services and products by the selected trading funds is, to a large extent, a monopoly. Market competition is not available.
9. In Hong Kong, while the revision of fees and charges of the Land Registry Trading Fund requires the vetting of the Legislative Council, the Post Office is only required to get such approval for fixing some of its fees and charges. The other three selected trading funds, including the ones in the UK, do not require approval of the legislature for setting their fees and charges.
10. Two of the five selected trading funds failed to break even and to attain the target rate of return for different lengths of time. The remaining three have all exceeded their target rates of return.
11. The Framework Agreement of a trading fund aims to define clearly the respective responsibility between the head of the trading fund and the head of the corresponding parent ministry/department/bureau. In the UK, copies of the Framework Documents are placed in the libraries of both Houses of Parliament whilst, in Hong Kong, there is no arrangement for making the Framework Agreements publicly available.
12. In Hong Kong, the introduction of the Accountability System for Principal Officials has led to a division of labour within a bureau over the policy of a trading fund. On the working level, while the Bureau Secretary is responsible for the overall policy, the Permanent Secretary has taken up duties of administrative and executive natures. The general manager of the trading fund reports directly to the Permanent Secretary on the operational matters and seeks policy direction from the Bureau Secretary through the Permanent Secretary.
13. A review of status is conducted every five years for the two UK trading funds studied to determine if they should operate in the existing status or should work under an alternative structure to meet their objectives more effectively. In Hong Kong, no regular review of similar nature is conducted.

Alternatives to enhance efficiency

14. Apart from establishing trading funds, the UK has introduced executive agencies in the late 1980s to enhance efficiency and quality of services. Executive agencies enjoy most of the flexibility of trading funds, but they are not self-financing and not subject to market competition.
15. Besides hiving off departments to establish trading funds and executive agencies, both governments of the UK and Hong Kong have developed other means to enhance efficiency. Government departments are given more flexibility and freedom to manage their resources in recent years. In the UK, spending plans and a firm allocation of resources are set for three years to give government departments greater certainty and flexibility over their budgets. In Hong Kong, the introduction of the Save & Invest Account, the One-Line Vote, the Non-Civil Service Contract Staff Scheme and the Voluntary Retirement Scheme serves similar purposes.

Operation of Trading Funds

Part 1 - Introduction

1. Background

1.1 The Panel on Financial Affairs was briefed by the Government during its meeting on 3 June 2002 that the Government proposed to establish a Rating and Valuation Department (RVD) Trading Fund. The Government believed that the proposal could bring benefits to both RVD and the community (Table 1). The target was to bring the proposed trading fund into operation on 1 July 2003.

Table 1 - Key benefits of the proposed RVD Trading Fund suggested by the Government

To RVD	To the community
<ul style="list-style-type: none">• Operate on a more commercial basis in delivering quality, speedy and innovative services and in developing new services.• Drive a more customer-focused service culture and achieve significant and sustainable improvements in efficiency and cost effectiveness.• Secure greater efficiency and higher productivity which should lead to cost and manpower reductions over time.• Move early to accountability for full costs.• Motivate management and staff, behind a shared vision and identity, to focus on quality of service and sustained service improvement.	<ul style="list-style-type: none">• Respond promptly and effectively to rising customer demands for improved and new services.• Exploit RVD's property information database to support a more informed and transparent property market.

1.2 During the same meeting, the Panel on Financial Affairs requested the Research and Library Services Division to conduct a research on the operation of trading funds to facilitate the Panel's discussion on the proposed RVD Trading Fund.

2. Scope of research

2.1 This research covers the following trading funds in Hong Kong:

- Land Registry Trading Fund;
- Electrical and Mechanical Services Trading Fund; and
- Post Office Trading Fund.

2.2 As the trading fund concept originates from the United Kingdom (UK), this research also examines two trading funds in the UK:

- Her Majesty's Land Registry; and
- The Ordnance Survey (the national mapping agency of Great Britain).

2.3 The selected trading funds are considered comparable to RVD. Both the Land Registry of Hong Kong and its counterpart in the UK provide support services and possess a comprehensive database. The nature of services and the competitive edge of these two trading funds are comparable to RVD. Similar to the Electrical and Mechanical Services Trading Fund, most of the proposed RVD Trading Fund's income comes from government bureaux, government departments and public bodies. As for the Post Office, it has tried to utilize the financial flexibility of trading funds in exploring its commercial potential. The Ordnance Survey, the government department responsible for the official surveying and topographical mapping of Great Britain, serves as another example of trading fund operations in the UK.

2.4 The selected trading funds are examined in the following aspects:

- Staffing;
- Market structure;
- Fees and charges;
- Financial targets and attainment;
- Service targets and attainment; and
- Public accountability.

3. Methodology

3.1 This research adopts a desk research method, which involves internet research, literature review and analysis, and correspondence with related parties. Interviews are also conducted with the officials of some of the relevant authorities.

Part 2 - Trading funds: origin and development

4. Trading funds as part of the management reform of the United Kingdom

Management reform proposal

4.1 The concept of trading funds came originally from the UK. Both the 1968 Report of the Fulton Committee on the Civil Service (the Fulton Report) and the Conservative Administration's 1970 White Paper 'The Reorganization of Central Government' advocated the concept of units of accountable management.¹ The Fulton Report raised questions about the need for more 'accountable management', which meant holding individuals and units responsible for performance measured as objectively as possible.²

4.2 The Fulton Report envisaged that "*accountable management could be more effectively introduced when an activity is separately established outside a government department...*"³. This recommendation paved the way for the creation of trading funds and executive agencies. The Government Trading Funds Act (1973 Act) was enacted in 1973, but the implementation of this Act never really took off in the 1970s.

Creation of executive agencies and expansion of the trading fund regime

4.3 Efficiency enhancement of the public sector became one of the UK government's top priorities in the late 1970s. The Efficiency Unit, established in 1979, published a report called 'Improving Management in Government: The Next Steps' (the Next Steps Report) in 1988. The Next Steps Report recommended that "*agencies should be established to carry out the executive functions of government within a policy and resources framework, approved by the minister responsible for their area of work.*"

¹ The House of Commons debate on the Second Reading of the Government Trading Bill, 8th January 1990, Col. 729.

² Richard Chapman, "The Experience of Public Sector Management in the United Kingdom in the 1980s and Implications for Hong Kong" in Jane C. Y. Lee and Anthony B. L. Cheung eds. *Public Sector Reform in Hong Kong*, Hong Kong: The Chinese University Press, 1995.

³ The Civil Service, Report of the Committee 1966-68, Chairman Lord Fulton, London: HM Stationery Office, 1986, paragraph 188, quoted by Chapman, Richard, "The Experience of Public Sector Management in the United Kingdom in the 1980s and Implications for Hong Kong" in Jane C. Y. Lee and Anthony B. L. Cheung eds. *Public Sector Reform in Hong Kong*, Hong Kong: The Chinese University Press, 1995.

4.4 Based on the recommendation of the Next Steps Report, executive agencies were established with the intention of improving management in the civil service, and providing better value for money and better service to the public. Executive agencies are similar to trading funds in many aspects, but they remain vote-financed and operated at a less commercial extent than the latter.

4.5 The UK government believed that executive agencies would be able to operate in a more efficient way under the commercial regime of a trading fund. Two years after the issue of the Next Steps Report, the Government Trading Act 1990 was introduced to amend the 1973 Act, widening its scope to make the trading funds regime applicable to more agencies. The 1973 Act as amended enables agencies whose operations directed by statute and fees fixed by regulations to attain the status of trading funds. Since the 1973 Act was enacted, 23 trading funds have been established and four of them have been privatized, resulting in the current 19 trading funds.⁴

5. Introduction of trading funds in Hong Kong

Public Sector Reform in Hong Kong

5.1 The establishment of trading funds in Hong Kong was part of the Public Sector Reform initiative. In the late 1980s, the Hong Kong Government was faced with increasing demands for both human and financial resources. The Government decided to transform the public sector in the hope that more commitments could be taken at less cost. The Finance Branch introduced a number of financial management reforms and this 'value for money' concept was later expanded into a co-ordinated programme of the public sector reform.⁵

5.2 The Efficiency Unit was set up to develop the reform programme. One of the focuses of the reform proposals was to find the right mode of agency to deliver services in an effective and efficient manner.

5.3 The 1989 discussion of the public sector reform resulted in the enactment of the Trading Funds Ordinance on 10 March 1993. The trading fund concept was introduced in Hong Kong with the intention that an institutional change would provide the appropriate means and nurture a new working culture to improve services in terms of quality and cost-effectiveness.

⁴ In addition to the 19 trading funds, there are two trading funds, which are the respective responsibility of the Scottish Executive and the Northern Ireland Assembly.

⁵ Finance Branch, Public Sector Reform discussion document, February 1989 is available on the Efficiency Unit's web-site: http://www.info.gov.hk/eu/eng/aconsph/spch/info3/us6_con.htm.

Nature and legal basis of trading funds

5.4 The Government defines a trading fund as a financial and accounting framework established by law to enable a department, or part of a department, to adopt certain accounting and management practices common in the private sector.⁶ A trading fund is self-financing and does not need to seek annual funding from the Legislative Council (the Council) to finance its operations.

5.5 The Trading Funds Ordinance 1993 (the Ordinance) (Cap. 430) states that a trading fund is an accounting entity within the Government but does not have a separate legal existence.⁷ It remains part of the Government in the sense that its assets would remain government assets and its staff would remain civil servants.

5.6 A Framework Agreement should be concluded between the responsible Bureau Secretary and the general manager of a trading fund to cover commercial and non-commercial objectives, financial targets, operating targets and other matters of concern, such as the pricing mechanisms.

5.7 The Ordinance enables certain services of the Government to be financed under trading funds on the recommendation of the Financial Secretary, subject to the approval of the Council.

5.8 Under the Ordinance, a trading fund is established by a resolution of the Council. The Government appropriates to the fund assets employed in the designated operations and may provide cash injections in terms of investment capital and loans from the Capital Investment Fund and the Loan Fund respectively.

5.9 Trading funds normally pay an amount between 30% and 50% of their profits after taxation as dividends to the Government and make a payment in lieu of profits tax to the Government.

⁶ Finance Branch and Efficiency Unit, Legislative Council Brief-Trading Funds Bill 1992, November 1992.

⁷ Section 2 of the Trading Funds Ordinance.

6. Criteria for a trading fund

6.1 For both the UK and Hong Kong, the principal criterion in deciding whether a government department can operate as a trading fund is that it should be capable of funding the full cost of its operations from the revenue raised from the sale of its services.⁸

United Kingdom

6.2 Before a trading fund can be established in the UK, it must satisfy a number of statutory and administrative tests. In particular, the Government Trading Fund Act states that “*the operations in question consist substantially in the provision of goods or services in the United Kingdom otherwise than to departments of the government*”. HM Treasury elaborates this provision as requiring “*more than half*” of the goods and services to be provided to customers other than government departments.

6.3 In addition, the parent department and HM Treasury will consider whether a trading fund status would introduce the maximum degree of competition and establish a genuine customer-contractor relationship before they determine an agency should become a trading fund.⁹

Hong Kong

6.4 The arrangement of trading funds is considered appropriate for:¹⁰

- (a) Core services carried out by the Government as a matter of policy on a partial or full cost recovery basis;
- (b) Government support services normally provided to other government departments where a charge can be raised; and
- (c) Commercial services provided for the general public at a charge.

6.5 Before a trading fund can be established, a number of conditions, the first two being statutory requirements, have to be satisfied, and they are:¹¹

⁸ Reply from the Efficiency Unit of Hong Kong and Central Accountancy Team of HM Treasury, Guide to the establishment and operation of Trading Funds, January 2001.

⁹ It is required by section 4 of the White Paper “*The Financing and Accountability of Next Steps Agencies*”.

¹⁰ See note 1.

¹¹ Finance Branch and Efficiency Unit, Legislative Council Brief-Trading Funds Bill 1992, November 1992.

- (a) Financing by a trading fund operation will improve the efficiency and effectiveness of the management of the operation and meets an appropriate standard of service;¹²
- (b) Within a reasonable period of time, the operation should be able to break even taking one year with another;¹³
- (c) *“The revenue of the fund consists principally of receipts in respect of goods and services provided in the course of the fund’s operation”*;¹⁴
and
- (d) *“It is suitable to be so designated (i.e. areas resembling commercial activities and not providing social services which require substantial public funding)”*¹⁵.

7. Trading funds versus traditional government departments

7.1 The main difference between trading funds and traditional government departments is on resource allocation.

United Kingdom

7.2 The key characteristics of trading funds of the UK are summarized as follows¹⁶:

- (a) Trading funds operate off-vote. They do not need to seek funding from Parliament each year to finance their operations;
- (b) Trading funds are self-financing. They have powers to keep and carry over agreed levels of cash balances from one year to another and create reserves;
- (c) Trading funds fix fees and charges in accordance with the key financial target, which is normally to earn an average rate of return on capital employed of at least six or eight per cent depending upon whether fees are fixed by regulation or the trading funds are competing with private sector suppliers;

¹² S3, Trading Fund Ordinance (Cap. 430).

¹³ Ibid.

¹⁴ Finance Branch and Efficiency Unit, Legislative Council Brief-Trading Funds Bill 1992, November 1992.

¹⁵ Ibid.

¹⁶ Central Accountancy Team of HM Treasury, Guide to the establishment and operation of Trading Funds, January, 2001.

- (d) Charges, unless otherwise agreed, are for the full cost of services provided, and trading funds do not normally aim to make a 'profit';
- (e) The revenue should not be insufficient to meet a trading fund's expenses and other financial objectives, taking one year with another over a period of three years;
- (f) Trading funds are expected to pay a dividend to the capital invested by the government; and
- (g) Trading funds are not liable to corporation tax on its profits.¹⁷

Hong Kong

Traditional government departments

7.3 Under the vote accounting system, government departments have to take part in the annual Resource Allocation Exercise (RAE) to compete for resources. The introduction of new services or improvement of services are constrained by 'new money' available each year. Although a new envelope approach¹⁸ has been introduced by the Government to allocate and control the recurrent part of the operational expenditure for the coming four financial years, the capital expenditure RAE will continue to be conducted in the usual manner.

7.4 Departments have to spend within their budgets. They cannot, in general, transfer the use of funding from one subhead¹⁹ to another in order to meet fluctuating and sometimes unpredictable demands for their services. Even when extra resources are available, their allocation is subject to the approval of the Finance Committee of the Council.

7.5 In the past, if a department underspent in one year, their savings, in the normal course of events, would have to be clawed back by the Finance Bureau for reallocation.²⁰ Departments were implicitly penalized for not using up their approved budgets. Their spending limits might be reduced in the following year, which often led to a last minute spending spree and a possible waste of resources.²¹

7.6 There is generally no cross charging for ancillary services provided by one department to another. Consequently, there is no incentive for the service provider to improve efficiency, and for the user department to make more economical use of the services.

¹⁷ Reply from HM Treasury.

¹⁸ For details of the envelope approach, see paragraph 45.11.

¹⁹ Subhead is the individual item within the Estimate of each department or bureau.

²⁰ 'Save & Invest Account' was introduced along with the Enhanced Productivity Programme in 1999 to allow bureaux and departments to keep half of the unspent departmental expenses.

²¹ Ibid.

Trading funds

7.7 The Government considers that the major benefits of establishing trading funds are enhancement of efficiency and improvement in the quality of services. These benefits are prompted by three elements of trading funds:

- (a) Flexibility in both human and financial resources management, such as:
- Trading funds operate on a self-financing basis. Their staff cost and other expenses are paid out of the revenues of the trading funds²²;
 - Operating surpluses are retained as reserves and need not be handed back to the Government for central reallocation.²³ Trading funds can re-invest their reserves to enhance existing services and explore new business opportunities;²⁴
 - Trading fund managers are given freedom in the provision of services, provided that they raise sufficient revenue to cover costs; and
 - Certain staffing controls applicable to government departments remain, such as the creation of directorate posts. Nevertheless, as long as financial and performance targets are met, trading funds are not subject to non-directorate establishment ceilings.
- (b) The new customer/service provider relationship
- Trading funds provide services to all customers in the private and public sectors on a partial or full cost recovery basis. A real customer/service provider relationship would develop, which, in turn, should “*promote a customer-led rather than production driven regime*”;²⁵ and
 - Trading funds are exposed to direct price and performance comparison, which is expected to help improve service standards and cost-effectiveness.

²² Section 5(2) of the Trading Funds Ordinance.

²³ Section 5(3) of the Trading Funds Ordinance.

²⁴ However, section 9 of the Trading Funds Ordinance prohibits the general manager from borrowing for the trading fund from the private sector except in the way of temporary overdraft facilities up to the limit that the Financial Secretary approves.

²⁵ Finance Branch and Efficiency Unit, Legislative Council Brief-Trading Funds Bill 1992, November 1992.

- (c) It is a statutory requirement that the general manager of a trading fund shall manage a trading fund with the objectives of:²⁶
- Providing an efficient and effective operation that meets an appropriate standard of service;
 - Within a reasonable period of time, meeting expenses and financing liabilities of the trading fund out of its income, taking one year with another; and
 - Achieving a reasonable return, as determined by the Financial Secretary, on the fixed assets employed.

²⁶ Section 6 of the Trading Funds Ordinance.

Part 3 - Land Registry Trading Fund of Hong Kong

8. Background

8.1 The Land Registry (LR) Trading Fund was established by a resolution passed by the Council on 30 June 1993 under the Trading Funds Ordinance. On 1 August 1993, the LR Trading Fund commenced operation, becoming one of the first two government departments operating on a trading fund basis.

8.2 LR is responsible for the registration of land documents and provides search of land registers and records to facilitate the orderly conduct of land transactions.

8.3 The Land Registrar (the Registrar), a civil servant, is the General Manager of the LR Trading Fund. He is accountable to the Secretary for Housing, Planning and Lands through the Permanent Secretary (Planning and Lands) for managing and operating the business of LR and achieving its performance targets and financial objectives as set out in the Framework Agreement and the Corporate and Business Plans.

9. Staffing

Staffing flexibility and private sector expertise

9.1 The Registrar has delegated authority to determine the non-directorate establishment of LR. He also has the authority to recruit non-civil service contract staff²⁷ and structure their pay and conditions of employment in a way different from the prevailing provisions and requirements, after consultation with the Secretary for the Civil Service and the Secretary for Financial Services and the Treasury.

9.2 LR is employing five information technology professionals and one accounting assistant recruited from the open market on non-civil service contract terms.²⁸ Meanwhile, LR has not recruited for any other senior positions through open competition.

9.3 The Registrar, like heads of other government departments, had only limited power to discipline officers below Point 14 of the Master Pay Scale in the past. With effect from 1 November 2002, Permanent Secretaries as well as heads of departments and trading funds have been empowered to impose punishment (other than dismissal) on officers below Point 34 of the Master Pay Scale or equivalent.

²⁷ The non-civil service contract staff scheme was introduced in 1999. Before 1999, the trading funds could employ temporary staff on non-civil service terms to allow them to be more responsive to fluctuations in business volume.

²⁸ Three of them are paid at a level equivalent to senior government positions.

Size and costs of staff

9.4 The LR Trading Fund is mainly staffed by civil servants subject to the normal civil service terms and conditions of employment. The LR Trading Fund started operation with a total strength of 630 staff — 591 civil servants²⁹ and 39 non-civil service temporary staff.³⁰ While the total number of staff was down by 2.6% to 613 in 2001-02³¹ (including 88 non-civil service contract staff), the number of civil servants employed was reduced by 11.2% to 525 during the same period³².

9.5 It has been one of LR's long-term objectives to employ 15% of its staff on temporary or contract terms. LR did recruit a large number of non-civil service temporary staff in 1996-97 and 1997-98 to cope with the surging demand for services due to the booming property market while keeping overall staff costs as low as possible. As at 31 March 2002, the number of non-civil service staff employed was 88, accounting for 14.3% of the total workforce.

9.6 There is a limitation in expanding the ratio of non-civil service contract staff. In a report on EPP Savings, LR stated that as the Civil Service Bureau could not absorb the surplus general grades staff, LR could not further increase the ratio of contract staff.³³

9.7 Staff costs have accounted for the largest share of the operating costs of the LR Trading Fund (consistently over 60%) since its establishment. Staff costs in 2000-01 were HK\$221 million, up 35.3% from 1994-95.

10. Market structure

10.1 Under the Land Registration Ordinance (Cap. 128) and Regulations, LR is responsible for registering all documents affecting land. LR is also responsible for processing applications for the incorporation of property owners under the Building Management Ordinance. Owing to the statutory provisions, the LR Trading Fund is a monopoly over land registration and incorporation of owners.

10.2 LR is also the only statutory organization to maintain a Land Register, providing a comprehensive data bank of property information and land records. This gives LR a monopolistic advantage in providing the public, as well as government departments and agencies, with such information.

²⁹ While the number of civil servants actually employed was 591 as at 1 August 1993, the establishment was 612 at that time.

³⁰ As at 1 August 1993.

³¹ As at 31 March 2002.

³² The establishment of civil servants as at 31 March 2002 was 553.

³³ The Financial Services and the Treasury Bureau (the then Finance Bureau), "Enhanced Productivity Programme: 2000-01" Booklet, Report on EPP- The Land Registry Trading Fund.

11. Fees and charges

11.1 LR reviews the level of fees and charges annually during the preparation of the Business and Corporate Plan and discusses any proposals with the Secretary for Housing, Planning and Lands. The pricing policies of LR are based upon full cost recovery and the achievement of a target return on average net fixed assets (ANFA) of 10%, the prescribed rate of return as determined by the Financial Secretary.

Table 2 - Average increase in price

Year	Average increase in fees and charges of the LR Trading Fund
1994	Fee standardization ³⁴
1995	17%
1996 ³⁵	10%

11.2 The adjustment of fees and charges requires the negative vetting of the Council, in the form of subsidiary legislation. After the establishment of the LR Trading Fund, fees and charges were revised in three occasions (See Table 2), and have been frozen since 1996.

12. Financial targets and attainment

12.1 In accordance with the general provisions of the Trading Funds Ordinance and the Framework Agreement, LR has set the following financial targets:

- (a) To manage its financial affairs in such a way that it has the capacity to meet expenses incurred in the provision of its services and financial liabilities within a reasonable period of time;
- (b) To achieve a reasonable annualized rate of return on ANFA, as determined by the Financial Secretary. The prescribed rate is 10% per annum; and
- (c) To make prompt repayment of loans and payment of interests to the Government for funds borrowed at the time of setting up the trading fund, and for the financing of capital projects.

³⁴ On 15 July 1994, a fee standardization exercise was carried out to bring the New Territories fees in line with those of the Urban Land Registry. The exercise involved increases in various fees.

³⁵ A reduction in registration fee due to the simplification of the tier structure and the corresponding fee revision, combined with increases in other fees resulted in an overall net increase of 10%.

12.2 The rate of return on ANFA is calculated as a percentage of operating profit and interest income after notional tax to ANFA. Interest expenses are not included in the calculation of this rate of return.

12.3 Other than the first eight months of its operation³⁶, the LR Trading Fund has exceeded the target rate of return on ANFA of 10% all the way through (See Table 3). LR has explained that the high rate of return on ANFA in 2000-01 was due to the fact that most assets were fully depreciated in 2000-01 and thus ANFA fell HK\$157 million (29%) from its peak level in 1997-98.

Table 3 - Rate of return of LR

	93/94 ³⁷	94/95	95/96	96/97	97/98	98/99	99/00	00/01
Target rate of Return	10%	10%	10%	10%	10%	10%	10%	10%
Actual rate of Return	9%	10.3%	14.7%	29.1%	37.3%	14.8%	23.6%	25.7%

12.4 The operating costs in 2000-01 were HK\$112 million (49%) higher than those in 1994-95, the first full financial year after attaining the trading fund status. At the same time, the operating profit in 2000-01 was HK\$45 million (106%) higher than that in 1994-95.

12.5 Except for the first year of its operation as a trading fund where payment of dividend was not recommended³⁸, LR has been paying a dividend to the Government equivalent to 30% of its profit after taxation since 1994-95.

13. Service targets and attainment

Targets and performance

13.1 The main services provided by the LR are:

- (a) Registration of documents affecting land under the Land Registration Ordinance (Cap.128);
- (b) Provision of land search services and copies of the Land Registers and related records; and

³⁶ The figures under 1993-94 are calculated for a period of eight months from 1 August 1993 to 31 March 1994. If the eight-month performance was projected onto a 12 month basis, the rate of return in 1993-94 would be 13.5%.

³⁷ Ibid.

³⁸ Dividend was not recommended in view of the large capital expenditure committed and uncertainties of the property market.

- (c) Registration of owners' corporations under the Building Management Ordinance (Cap. 344).

13.2 The LR Trading Fund has introduced performance pledges for its major services since its commencement in August 1993. These pledges are reviewed annually. LR has so far achieved and exceeded most of its performance pledges. For instance, the pledged time taken for the registration of land documents was 26 days in 1993-94. In 2000-01, the service standard was raised to within 20 days.

13.3 Nonetheless, a small number of the service standards have taken some years of revision to higher standards.

Staff incentive scheme

13.4 A Performance Incentive Scheme has been in place since 1 January 1997 where awards are in kind and not in cash. The Scheme is operated on two levels of competitions - departmental-wise and team-based - under which staff are rewarded for meeting performance targets, achieving service improvement and realizing savings. The awards are given in the form of a free annual dinner and other non-cash means such as supermarket coupons.

Customer feedback

13.5 One of the aims of establishing a trading fund is to nurture a more customer-oriented working culture to enhance the quality of services. Three LR Customer Liaison Groups meet regularly and provide feedback on the performance of LR and ideas for service improvements. The Land Registry Joint Standing Committee, comprising representatives from LR and the Law Society of Hong Kong, also meets regularly to discuss and exchange views on land registration matters and LR's services provided to legal practitioners.

13.6 A Customer Satisfaction Survey was conducted by LR in 1996, 2001 and 2002 respectively to provide an assessment of customers' needs and satisfaction level on its performance. The 2001 Customer Satisfaction Survey showed that 46.5% of the user groups are very satisfied and 41.9% are quite satisfied with LR's services.

New and enhanced services and products

13.7 The major new services introduced by LR after attaining the trading fund status are:

- (a) Computerization of New Territories Land Registers;

- (b) Direct Access Services - Users can search any land registers and land documents via computer terminals at their offices and also place orders for copies of land documents;
- (c) Document Imaging System - users can obtain online retrieval of land documents over the counter or by fax;
- (d) Cross District Search services;
- (e) Street Index on Compact Disc;
- (f) New Territories Lot/Address Cross Reference Table on Compact Disc; and
- (g) Colour Imaging of Plans.

13.8 The planned services to be introduced by LR in the coming future are:

- (a) Development of an Integrated Registration Information System to enable the lodgement of deeds for registration at a central registration office without geographical restriction and to conduct land search through the Internet by early 2004; and
- (b) Introduction of a land title registration system to provide certainty of title around the year-end of 2005.

14. Public accountability

14.1 The Framework Agreement sets out the respective responsibilities of the Bureau Secretary and the Registrar. The Framework Agreement is normally reviewed by the Bureau Secretary in consultation with the Registrar every three years. The Secretary for Housing, Planning and Lands is responsible for:

- (a) Formulating and reviewing the Government's policies and aims with respect to the registration of land;
- (b) Setting the policy objectives of LR;
- (c) Ensuring the timely consideration and approval of the Annual Business Plan and the Medium Range Corporate Plan of LR; and
- (d) Speaking for the Government on policy matters relating to LR.

14.2 Since the introduction of the Accountability System, the responsibilities of the previously civil service ranked Secretary under the Framework Agreement are taken up by the politically appointed Bureau Secretary. On the working level, there is a division of labour between the politically appointed Bureau Secretary and the Permanent Secretary (Planning and Lands). While the Bureau Secretary is responsible for the overall policy, the Permanent Secretary (Planning and Lands) has taken up duties of an administrative and executive nature. The Registrar reports directly to the Permanent Secretary on operational matters and seeks policy direction from the Bureau Secretary through the Permanent Secretary.

14.3 The Registrar is responsible for:

- (a) Managing and operating the business of LR and achieving the performance targets of LR;
- (b) Setting the performance targets for LR, having regard to the business objectives of LR, and keeping the Bureau Secretary informed of any proposed change in such targets before introduction;
- (c) Preparing and submitting to the Bureau Secretary an Annual Business Plan and a Medium Range Corporate Plan;
- (d) Preparing and delivering to the Bureau Secretary the annual reports and accounts;
- (e) Providing answers to queries on matters relating to the day-to-day management of LR;
- (f) Advising on policy and legislative issues concerning land registration and the registration of title to land; and
- (g) Providing to the Bureau Secretary any information he might reasonably request as regards the performance and plans of LR.

14.4 LR is subject to an annual audit of its accounts by the Director of Audit. LR is required to table its annual report, certified financial statements and the report of the Director of Audit before the Council on an annual basis. LR is also subject to any value for money audit by the Director of Audit, which examines the economy, efficiency and effectiveness of LR in discharging its functions. Both the Registrar and the Bureau Secretary answer to the Public Accounts Committee (PAC) of the Council when PAC considers the value for money audit report prepared by the Director of Audit.

14.5 The related Panels of the Council also monitor the performance of LR and any related policy matters. The Registrar, the Bureau Secretary or both will attend Panel meetings when required to brief Members on matters of public concern and answer their questions regarding the operation of LR.

Part 4 - Post Office Trading Fund

15. Background

15.1 The Post Office (PO) Trading Fund was established by a resolution passed by the Council on 19 July 1995 under the Trading Funds Ordinance. On 1 August 1995, the PO Trading Fund commenced operation.

15.2 The Post Office is responsible for providing postal services and services supporting electronic commerce. The Postmaster General, a civil servant, is the General Manager of the PO Trading Fund. A Framework Agreement was agreed between the Postmaster General and each of the two Bureau Secretaries responsible for different areas of work of the PO Trading Fund. The Framework Agreements set out the performance targets and financial objectives of the PO Trading Fund.

16. Staffing

Staffing flexibility and private sector expertise

16.1 The arrangement with regard to the flexibility in human resources management of the PO Trading Fund is similar to that of the LR Trading Fund. Please refer to paragraphs 9.1 and 9.3 for details.

16.2 PO has recruited nine managers with commercial sector experience into the Business Development Branch on contract terms since 1997-98. Overall, it is now employing 45 non-civil service contract staff at managerial or comparable positions who were recruited through open competition.³⁹ In open recruitment, all candidates, be they civil servants or not, are subject to the same selection process and standard.

³⁹ Among the 45 non-civil service contract staff, 14 are managers of the Business Development Branch; six are managers for business development and project management for the Certificate Authority project; four are managers for productivity services; three are financial managers; three are Training Officers for a three-year training programme and 13 are computer managers and officers providing information technology support to various projects; and two are managers for public relations and training administration respectively.

Size and costs of staff

16.3 The PO Trading Fund started operation with a total strength of 6 114 staff — 5 504 civil servants and 610 non-civil service temporary staff⁴⁰. The total number of staff was 7 406 as at 31 March 2002, representing an increase of 21.1% from 1995, whilst the number of civil servants employed was up 4.5% to 5 750⁴¹ and the items handled by PO were up 17% during the same period.

16.4 Meanwhile, the number of non-civil service temporary staff and contract staff jumped 17% since the commencement of the trading fund operation, accounting for 22.3% of the total workforce in 2001-02.⁴²

16.5 Staff costs have accounted for the largest share of the operating costs of the PO Trading Fund since its establishment. Other than the first year of trading fund operation, staff costs have consistently made up of more than 60% of the operating costs of PO. Staff costs in 2000-01 were HK\$2,298 million, up 14.3% from 1996-97, the first full year after commencement of the trading fund operation.

17. Market structure

17.1 PO has an exclusive privilege under the Post Office Ordinance to provide local and overseas letter services in Hong Kong. This exclusive privilege comes with a social obligation, which requires PO to maintain a universal postal service in Hong Kong and to charge all customers basically the same postage rates.

17.2 According to the Postmaster General, the postal service faces increasing competition from private operators “*who are aggressively competing in the business area of documents and goods as they are for the international courier and airmail businesses.*”⁴³

17.3 According to the Director of Audit, in recent years, PO’s share in local mail traffic in business districts and densely populated residential areas has faced competition not only from local couriers but also from utility companies which deliver their own bills. Electronic communication and electronic payment services compete against the postal service as well.⁴⁴

⁴⁰ As at 1 August 1995. Since 1999, the PO Trading Fund has been allowed to employ staff on non-civil service contract staff terms.

⁴¹ The establishment of civil servants as at 31 March 2002 was 5 774.

⁴² As at 31 March 2002.

⁴³ P. C. Luk, “Post Office Trading Fund” in Anthony B. L. Cheung and Jane C. Y. Lee eds. *Public Sector Reform in Hong Kong into the 21st Century*, Hong Kong: The Chinese University of Hong Kong, 2001.

⁴⁴ Report No. 38 of the Director of Audit, March 2002.

18. Fees and charges

18.1 PO has different mechanisms for determining different categories of fees and charges. The Postmaster General determines the postage rates under section 4 of the Post Office Ordinance (Cap. 98), subject to any direction of the Chief Executive in Council. According to the Framework Agreement, the Postmaster General will consult the Secretary for Economic Development and Labour before deciding on the postage rates and the level of fees and charges. Meanwhile, the charges for ancillary postal services listed under section 3 of the Post Office Ordinance (Cap. 98) are prescribed by subsidiary legislation, subject to the vetting of the Council.

18.2 Under section 35 of the Electronic Transactions Ordinance (Cap. 553), the Postmaster General may determine and charge fees for providing the services of a certification authority or other related services. Vetting of the Council is not required.

18.3 The pricing policy of PO is to achieve a target rate of return on ANFA of 10.5%, with the gradual elimination of cross-subsidization among postal services as a long-term objective.

18.4 The Government, in moving the resolution for establishing the PO Trading Fund in 1995, undertook to maintain postage rates at levels reasonable and affordable to the public, by keeping increases broadly in line with inflation. The Government employs the Government Consumption Expenditure Deflator (GCED), which reflects changes in the costs of providing government services, instead of the Consumer Price Index (CPI), as the 'inflation' factor for postage rates adjustment.

18.5 Two months before the establishment of the PO Trading Fund, postage rates were raised by 14.7%. Since the commencement of the trading fund operation, the postage rates have been increased twice. In view of the substantial surpluses generated in both 1996-97 and 1997-98, PO froze postage rates between September 1996 and March 2002.

Table 4 - Average increase in postal rates

	Average increase of postage rates	Average increase of Composite CPI ⁴⁵	Postage rate for local letter up to 30g (HK\$)
1995	14.7%	9.1%	1.2
1996	8.7%	6.3%	1.3
1997	-4% ⁴⁶	5.8%	1.3
1998	-17% ⁴⁷	2.8%	1.3
1999	Nil	-4.0%	1.3
2000	Nil	-3.8%	1.3
2001	Nil	-1.6%	1.3
2002	6.5%	-3.0%	1.4

18.6 PO originally planned to raise the postage rates by 6.5% in October 2001, which included both increases and reductions for different services. Taking into account the economic situation and views of the public and the major users, PO deferred the implementation of the revision to 1 April 2002.

19. Financial targets and attainment

19.1 PO has set financial targets similar to those for the LR Trading Fund manifested in paragraph 12.1. The prescribed rate of return of the PO Trading Fund was set at 12% per annum in 1995 and has been tuned down to 10.5% since 1996. Target revenue and expenditure have also been adopted as indicators of PO's financial performance.

19.2 Since the establishment of the PO Trading Fund, PO has only managed to meet and exceed its prescribed rate of return at 10.5% in 1996-97 and 1997-98 when there was an upsurge in demand for Hong Kong stamps.

⁴⁵ See Note 17.

⁴⁶ A new local postage rate structure in 1997 resulted in a weighted average rate reduction of 4% for local mail.

⁴⁷ A new bulk air mail rate structure in 1998 resulted in a weighted average rate reduction of 17% for bulk mail.

Table 5 - Rate of return of the PO Trading Fund

	95/96 ⁴⁸	96/97	97/98	98/99	99/00	00/01
Target rate of return	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%
Actual rate of return	9%	47.8%	41%	3.1%	2.1%	1.8%

19.3 Operating losses were recorded in 1998-99, 1999-2000 and 2000-01 due to a fall in the volume of mail and income from philately. However, the PO Trading Fund still managed to achieve a positive rate of return, as the interest income more than made up for the operating loss, resulting in a small overall profit.

19.4 The amount paid by PO as dividend to the Government was 30% of its profits after taxation in 1995-96, 40% in 1996-97 and has been 50% since 1997-98, regardless of the operating losses.⁴⁹ The operating costs in 2000-01 were 8.7% higher than those in 1996-97, the first full financial year after the commencement of the trading fund operation.

19.5 PO kept its actual expenditure within target from 1996-97 to 2000-01. On the other hand, it managed to meet and exceed its revenue target only in 1996-97 and 1997-98. Although it tuned down its target revenue since then, it failed to meet the target in the following three years.

19.6 The unit cost of handling per local mail item was HK\$1.40 in the last eight months of 1995-96, and HK\$1.59 in 2000-01, up 13.6%. Meanwhile, productivity measured by items per man-hour rose from 108 items in the last eight months of 1995-96 to 116 items in 2000-01, an increase of 7.4%.

19.7 Report No. 38 of the Director of Audit, released in 2002, found that there was room for improvement in the financial performance of PO in three areas, namely the postshop service, the e-post and the remittance service.

19.8 The Director of Audit also advised PO to address the threats posed by the overseas postal administration, the local couriers and the increasing use of electronic-mail service. According to PO's estimation in 2001, the loss of annual revenue due to overseas mailers bypassing the international mail system amounted to HK\$24 million.⁵⁰

⁴⁸ The figures are for the first eight months of the trading fund operation.

⁴⁹ As PO had still made an overall profit, it was required to pay dividends to the Government.

⁵⁰ Report No. 38 of the Director of Audit, March 2002.

20. Service targets and attainmentTargets and performance

20.1 The main services provided by PO are:

- (a) Receiving, collecting, sending, dispatching and delivering postal articles as specified in the Post Office Ordinance (Cap. 98);
- (b) Providing Speedpost and other courier services;
- (c) Retailing stamps and postal related products through counter outlets and appointed agents;
- (d) Philatelic services;
- (e) Remittance services;
- (f) Other services prescribed by the Acts of the Universal Postal Union;
- (g) Ancillary postal services which are incidental to or supportive of the major services;
- (h) Agency services of government departments, public bodies and public utilities, which are compatible with postal related services;
- (i) Letting out of accommodation that is not immediately required to provide postal services if the letting out does not affect the provision of postal services;
- (j) Provision of a public certification service;
- (k) Provision of services to support the development of public key infrastructure applications; and
- (l) Provision of other services to support electronic commerce.

20.2 PO has introduced performance pledges for its major services since the commencement of its trading fund operation. These pledges are reviewed annually. PO has so far achieved and exceeded most of its targets. However, some of the pledged performance standards have not been revised for some years.

Staff incentive scheme

20.3 A Staff Recognition Fund was established in 1998, being financed by the revenue of the PO Trading Fund. It sponsors staff recognition activities, staff competitions and distribution of souvenirs to staff as a recognition of the commitment and contribution of staff in delivering efficient and quality service, and to reinforce the customer-focused culture. Awards are not in cash but in kind, including gift coupons.

Customer feedback

20.4 A number of channels are in place to collect customer feedback, including Customer Surveys, Customer Liaison Groups, Customer Visits, Account Management, Market Research and Regular Mystery Shopper Survey Programme.

20.5 In the 2000-01 annual survey of the public perceptions of services provided by PO, 'satisfied' and 'very satisfied' customers accounted for over 96% of the respondents, compared with over 94% in the 1996-97 survey. Comparing the two surveys, the 'very satisfied' customers increased from 24% to 42% for the general public, from 23% to 40% for business users and from 15% to 59% for philately customers.

New and enhanced services and products

20.6 The major new services introduced by the PO Trading Fund are:

- (a) Launching PayThruPost service for settling government bills and public utility bills;
- (b) Simplifying customs declaration forms for sending parcels overseas;
- (c) Introducing Personal Greeting stamps and embossed stamps;
- (d) Developing mobile certificates to support secure mobile electronic commerce;
- (e) Establishing the first public Certification Authority in Hong Kong and issuing e-Cert since January 2000;
- (f) Setting up a 24-hour Speedpost acceptance service at Air Mail Centre;
- (g) Extending service boundary of LocalCourierPost; and
- (h) Introducing Speedpost-Freight service.

21. Public accountability

21.1 There are two Framework Agreements for the PO Trading Fund. The first Framework Agreement sets out the respective responsibilities for the Secretary for Economic Development and Labour and the Postmaster General. Their responsibilities are similar to those described for the Secretary for Housing, Planning and Lands and the Land Registrar in the Framework Agreement of the LR Trading Fund (See paragraphs 14.1 and 14.3), except that the responsibility of setting performance targets for the PO Trading Fund rests with the Bureau Secretary, in consultation with the Postmaster General.

21.2 In the Framework Agreement between the Postmaster General and the Secretary for Commerce, Industry and Technology, the Bureau Secretary is responsible for the policy framework within which PO is to provide services to support electronic commerce. The Postmaster General is responsible for the following duties in the provision of services to support electronic commerce:

- (a) Managing and operating the business of PO and achieving the performance targets of PO;
- (b) Providing answers to queries on matters relating to the day-to-day management of PO; and
- (c) Providing the Bureau Secretary with any information he might reasonably request as regards the performance and plans of PO.

21.3 Since the introduction of the Accountability System, the responsibilities of the previously civil service ranked Secretaries under the Framework Agreements are taken up by the politically appointed Bureau Secretaries. On the working level, there is a division of labour between the politically appointed Bureau Secretaries and the Permanent Secretaries⁵¹. While the Bureau Secretaries are responsible for the overall policy, the Permanent Secretaries have taken up duties of an administrative and executive nature. The Postmaster General now reports directly to the Permanent Secretaries on operational matters and seeks policy direction from the Bureau Secretaries through the Permanent Secretaries.

21.4 Each Framework Agreement is reviewed by the respective Bureau Secretary, in consultation with the Postmaster General, every three years or more often if necessary by mutual agreement of both parties. The Postmaster General is responsible for preparing and submitting to each Bureau Secretary an Annual Business Plan and a Medium Range Corporate Plan setting out the short and long-term strategies for achieving business and policy objectives in the corresponding areas.

⁵¹ The Permanent Secretary for Economic Development and Labour and the Permanent Secretary for Commerce, Industry and Technology.

21.5 PO is subject to annual audit of its accounts by the Director of Audit. PO is required to table its annual report, certified financial statements and the report of the Director of Audit before the Council on an annual basis. PO is also subject to any value for money audit by the Director of Audit, which examines the economy, efficiency and effectiveness of PO in discharging its functions. Both the Postmaster General and the Bureau Secretaries answer to the Public Accounts Committee (PAC) when PAC considers the value for money audit report prepared by the Director of Audit.

21.6 The related Panels of the Council also monitor the performance of PO and any related policy matters. The Postmaster General, the Bureau Secretary or both will attend Panel meetings when required to brief Members on matters of public concern and answer their questions regarding the operation of PO.

Part 5 - Electrical and Mechanical Services Trading Fund

22. Background

22.1 The Electrical and Mechanical Services Trading Fund (EMSTF) was established by a resolution passed by the Council on 26 June 1996 under the Trading Funds Ordinance. On 1 August 1996, EMSTF commenced operation.

22.2 EMSTF is the trading arm of the Electrical and Mechanical Services Department (EMSD), providing electrical and mechanical services to customers on commercial lines.

22.3 The regulatory functions and the advisory services of EMSD remain vote-funded and continue to be under the purview of the Director of Electrical and Mechanical Services (the Director). Meanwhile, EMSD continues to play the role of a regulatory body and a law enforcement department with regard to electricity, gas, lift and escalator safety, and a number of related electrical and mechanical safety areas. In addition, EMSD is responsible for promoting energy efficiency and conservation, and providing technical support to the Administration in the development and implementation of energy efficiency policy.

22.4 The Director is the designated General Manager of EMSTF. He is accountable to the Secretary for the Environment, Transport and Works for managing the business of EMSTF and achieving its performance targets and financial objectives set out in the Framework Agreement.

23. Staffing

Staffing flexibility and private sector expertise

23.1 The arrangement with regard to the human resources management flexibility of EMSTF is similar to that of the LR Trading Fund. Please refer to paragraphs 9.1 and 9.3 for details.

23.2 EMSD staff deployed to the trading fund continue to be civil servants subject to normal civil service terms and conditions of employment. The Director is also a civil servant.

23.3 In response to staff concerns, the then Secretary for Works made a specific commitment in the Framework Agreement that should there be surplus staff arising from the trading fund operation, the Director would make full use of re-deployment, re-training and natural wastage to deal with the situation. No existing staff would be made redundant or forced to retire early because of the implementation of EMSTF.

23.4 Subject to the agreement of the Secretary for the Civil Service, the Director has the discretion to fill by open recruitment certain designated posts fully funded by EMSTF. The Framework Agreement specifies that in such cases, preference is given to serving officers with the necessary managerial and business skills. Appointment is on such terms and conditions agreed with the Secretary for the Civil Service.

23.5 So far, all top management posts have been filled by internally promoted officers who are considered as fully competent in discharging their duties by EMSTF. Members of both the Executive Board⁵² and the Management Board⁵³ of EMSTF are filled by senior staff of EMSD and the Environment, Transport and Works Bureau, without any non-executive director from the private sector.

Size and costs of staff

23.6 EMSTF commenced operation with a total strength of 4 786 staff, all of whom were civil servants. The size of staff was down by three per cent to 4 635⁵⁴ in 2001-02. During the same period, the number of civil servants employed was reduced by 16.5% to 3 996 in 2001-02⁵⁵, with 147 of them reduced through the voluntary retirement scheme. EMSTF employed some 600 non-civil service temporary and contract staff to replace civil service staff through natural wastage and to meet short-term needs, representing more than 13% of the total workforce as at 31 March 2002.

23.7 In order to contain staff size, EMSTF has been outsourcing the low-end service works to the private sector and concentrating on the provision of high-value services. The percentage of outsourced works rose from 26.1% in 1996-97 to 32.3% in 2001-02.⁵⁶

23.8 Staff costs have accounted for the largest share of the operating costs of EMSTF since its establishment, consistently making up of around 60% of the operating costs. Staff costs of 2000-01 were HK\$1,616 million, up 8.5% from 1997-98 while business volume rose by 19.5%, from HK\$2,654 million to HK\$3,171 million in the same period.

⁵² The Executive Board, chaired by the Permanent Secretary for the Environment, Transport and Works (Transport and Works) and composed of the Deputy Secretary of the Bureau, the Director, his deputy, and the Departmental Secretary of EMSD, meets quarterly to determine policies and oversee the operations of EMSTF.

⁵³ The Management Board is chaired by the Director and composed of his deputy, three Assistant Directors, the Finance Manager, the Staff Relations Officer and the Departmental Secretary. It meets monthly and is responsible for managing the daily operations of EMSTF.

⁵⁴ Thirty-five temporary staff from hire-of-service contract were included in the total staff of 4 635. EMSTF paid an agency/agencies to hire the service of these 35 temporary staff instead of directly hiring them. At the commencement of its operation, all 4 786 staff were employed directly by EMSTF.

⁵⁵ During the same period, the establishment of civil servants was reduced from 5 366 to 4 571, down 14.8%.

⁵⁶ Reply from EMSTF.

24. Market structure

24.1 Government departments and statutory bodies were obliged to use EMSTF's services for the first three years following the setting up of EMSTF. This monopolistic setting was intended to allow EMSTF to improve its capability to compete for clients in the open market.

24.2 Starting from 1 August 1999, government bureaux, departments and autonomous bodies began to untie from using services provided by EMSTF in four phases over a three-year period.

24.3 With the completion of the untying programme in August 2002, all of EMSTF's clients can opt for suppliers in the private sector or retain the services of EMSTF to meet part or all of their needs. According to EMSTF, no single client completely discontinues the employment of its services. The business loss from clients discontinuing its services was slightly over 2% of its total business volume so far but the loss was offset by the increase in business volume as a whole in the same period.

25. Fees and charges

25.1 The pricing policy of EMSTF is to achieve a target rate of return on ANFA of 13.5%. The Director is responsible for developing pricing and charging policies for the trading services. Revision of the fees and charges does not require approval of the Executive Council or the Legislative Council, nor does it require any prior consultation with the Bureau Secretary.

25.2 Most of EMSTF's revenue comes from service packages tailor-made to meet customer needs. EMSTF states that its charges are market-driven and often dependent on the equipment details and customer requirements.⁵⁷ It also adjusts prices in accordance with specific negotiations with individual clients on a case-by-case basis.

25.3 EMSTF suggests that the recent winning of several important contacts through open tender bidding is an indication that their charges are competitive in the open market.⁵⁸ Up to 2002, EMSTF has offered an accumulative 19.4% reduction in real terms after achieving an accumulative productivity improvement of 22.5%.

⁵⁷ Reply from EMSTF.

⁵⁸ Ibid.

26. Financial targets and attainment

26.1 In accordance with the general provisions of the Trading Funds Ordinance and the Framework Agreement, EMSTF has set the following financial targets:

- (a) To manage its financial affairs so as to ensure that it has the capacity to meet the expenses incurred in the provision of its services and financial liabilities within a reasonable time;
- (b) To achieve a reasonable return, as determined by the Financial Secretary, on the annualized rate of return on ANFA employed. The prescribed rate is 13.5% per annum; and
- (c) To improve productivity by five per cent per annum for the first three years of trading fund operations.

26.2 EMSTF managed to attain a rate of return twice to thrice of the target rate of 13.5% from 1997-98 to 2000-01. For instance, the actual rate of return in 2000-01 was as high as 52.5% while the forecast rate was only 30.1%.

Table 6 - Rate of return of EMSTF

	96/97 ⁵⁹	97/98	98/99	99/00	00/01
Target rate of return	13.5%	13.5%	13.5%	13.5%	13.5%
Actual rate of return	16.8%	28.8%	36.1%	37.1%	52.5%

26.3 EMSTF explains that the gap between projections and actual performance resulted from the fluctuating demand for services. For instance, the Government increased its budget for infrastructure in 2000-01, which in turn brought more business opportunities to EMSTF.

26.4 Apart from this surge in demand for service, the higher-than-expected interest income of HK\$104 million in 2000-01 was another factor contributing to the exceptionally high rate of return.

26.5 Since its establishment, EMSTF had achieved an accumulative 22.5% improvement in productivity⁶⁰ up to 2001-02. Meanwhile, EMSTF has been paying a dividend, 30% of its profit after taxation, to the Government since its commencement.

⁵⁹ The figures are for the first eight months of the trading fund operation.

⁶⁰ Productivity is measured in terms of the absorption of new businesses without an increase in resources and with a proper control of expenditure.

27. Services targets and attainment

Targets and performance

27.1 The main services provided by EMSTF are:

- (a) Operating, continuously monitoring and maintaining the electrical, mechanical, electronic and building services systems and equipment in use at major installations, such as office buildings, hospitals, airports, and civil venues;
- (b) Maintaining electrical, mechanical, electronic and building services systems and equipment according to accepted maintenance programmes;
- (c) Maintaining vehicle fleets according to accepted maintenance programmes;
- (d) Providing design, procurement, project management and other technical consultancy services in relation to electrical, mechanical, and electronic systems and vehicle fleets; and
- (e) Operating and maintaining the refuse incineration plant to agreed operational parameters

27.2 A number of Service Level Agreements (SLAs) are established between EMSTF and its customers. Under the SLAs, customers will pay EMSTF a fixed annual fee in return for a full range of services covering either all systems at specific locations or a group of systems or equipment.

27.3 EMSTF is currently having some 91 major SLAs with various clients. Individual clients, venues and facilities may have different service level requirements and performance indicators. The overall compliance of service performance targets shows that the actual performance has exceeded the targets over the years.

Staff incentive scheme

27.4 A Staff Encouragement Scheme was introduced during the establishment of EMSTF in 1996, with the intention of motivating staff to improve their productivity. When EMSTF has met or exceeded the target rate of return of 13.5%, 90% compliance of the service performance targets, and recorded improvement in customer satisfaction in a particular year,⁶¹ each eligible staff will receive an award in the form of supermarket coupons valued around HK\$450.

⁶¹ Customer satisfaction index higher than or equal to the mean index of the previous three surveys and satisfaction level of 95% or higher for regular feedback measurement.

Customer feedback

27.5 Results of the customer satisfaction surveys have indicated that customers' satisfaction level is rising. Given the top score being eight, EMSTF recorded a score of less than five before 1998, and registered a score of 5.77 in 2002.

27.6 Client managers at Assistant Director level have been appointed to look after the interests and concerns of individual clients. There are regular meetings between the client managers of EMSTF and the senior management of its customers to review the performance of services and collect feedback. EMSTF launched its first customer newsletter in December 1999 to keep customers informed of the latest news regarding its operations.

New and enhanced services and products

27.7 The major improvements in services made by EMSTF are:

- (a) Establishment of Integrated Service Teams to enable one-stop single contact by clients for different disciplines of engineering services;
- (b) Implementation of international standards in operation, including the ISO 9001 quality management system, ISO 14001 environment management system and OHSAS 18001 occupational health and safety assessment series;
- (c) Reorganization of divisions into Strategic Business Units to provide customer-focused services;
- (d) Regionalization of operations by setting up new district depots to enable staff to report directly at clients' venues in order to save travelling time;
- (e) Establishment of Work Improvement Teams Scheme and Business Process Improvement Teams to review and improve operational efficiency regularly; and
- (f) Embarkation of Total Quality Management System.

27.8 The major new services provided by EMSTF are:

- (a) Launching the Energy Management Programmes which help customers to reduce their electricity bills by analyzing their consumption patterns, and applying the most economical rates with the power utilities; and
- (b) Launching information technology services which provide a total engineering solution to its clients.

28. Public accountability

28.1 The Framework Agreement governs the relationship and respective responsibilities of the Director and the Secretary for the Environment, Transport and Works, and specifies the objectives and targets of EMSTF. The Bureau Secretary may at any time, in consultation with the Director and with others in the Government as appropriate, vary the contents of the Agreement.

28.2 The Bureau Secretary oversees the operation of EMSTF and is responsible for:

- (a) Formulating and reviewing government policies and aims in respect of the trading services under the trading fund;
- (b) Reviewing the strategic and financial objectives of the trading fund;
- (c) Specifying, in consultation with the Director, the performance targets of the trading fund; and
- (d) Approving and, in consultation with the Director, reviewing the Corporate and Business Plan.

28.3 After the introduction of the Accountability System for Principal Officials in July 2002, the Bureau Secretary is assisted by the Permanent Secretary (Transport and Works) in overseeing the operation of EMSTF. According to EMSTF, on the working level, the Permanent Secretary has taken up responsibilities of an executive nature, such as the responsibilities specified in paragraphs 28.2(c) and 28.2(d).

28.4 The Director is responsible for:

- (a) Managing and operating EMSTF effectively and efficiently and achieving the strategic and financial objectives set by the Bureau Secretary;
- (b) Managing the fixed assets appropriated to EMSTF and ensuring timely maintenance, renewal, expansion or disposal of such assets;
- (c) Preparing and submitting to the Bureau Secretary the updated Corporate and Business Plan, including his proposals for the development of the trading services;
- (d) Developing pricing and charging policies for the trading services and billing and collecting the charges levied;
- (e) Managing the revenue received from the trading service charges and the trading fund capital and other assets appropriated to EMSTF;

- (f) Preparing and delivering to the Bureau Secretary an annual report and accounts in accordance with the requirements set out in the Framework Agreement; and
- (g) Providing any information the Bureau Secretary may request regarding the operation of EMSTF.

28.5 After the introduction of the Accountability System, the Director of the EMSTF is accountable to the Secretary for the Environment, Transport and Works through the Permanent Secretary (Transport and Works). The Director reports directly to the Permanent Secretary on operational matters and reports to the Bureau Secretary through the Permanent Secretary on strategic and policy matters.

28.6 EMSTF is subject to an annual audit of its accounts by the Director of Audit. EMSTF is required to table its annual report, certified financial statements and the report of the Director of Audit before the Council on an annual basis. EMSTF is also subject to any value for money audit by the Director of Audit, which examines the economy, efficiency and effectiveness of EMSTF in discharging its functions. Both the Director and the Bureau Secretary answer to the Public Accounts Committee (PAC) of the Council when PAC considers the value for money audit report prepared by the Director of Audit.

28.7 The related Panels of the Council also monitor the performance of EMSTF and any related policy matters. The Director, the Bureau Secretary or both will attend Panel meetings when required to brief Members on matters of public concern and answer their questions regarding the operation of EMSTF.

Part 6 - Ordnance Survey Trading Fund of the United Kingdom

29. Background

29.1 The Ordnance Survey (OS) is the national mapping agency of Great Britain, which records and provides the definitive record of features of the natural and built environment and of many official boundaries.

29.2 It was established as an executive agency in 1990 and began operating as a trading fund on 1 April 1999 after Parliament passed the Ordnance Survey Trading Fund Order in March 1999.

29.3 The Director General of OS is the Chief Executive of the OS Trading Fund. The Director General is accountable to the Deputy Prime Minister for the performance of OS in accordance with the Framework Document and the corporate business plan. The Deputy Prime Minister has ministerial responsibility for OS.

29.4 Stage 1 of the Quinquennial Review proposed in December 2001 that OS should change its status to a government-owned company to give it more freedom. After consideration, the UK government announced in July 2002 that OS would not be turned into a government-owned public limited company, but should be offered more freedom to develop its business on a trading fund basis.

30. Staffing

Staffing flexibility and private sector expertise

30.1 The Director General is appointed by the Deputy Prime Minister through open competition. The four Non-Executive Directors of the 12-member Strategy Board come from the private sector as well. The Strategy Board⁶² is responsible for determining the long-term strategy for OS, monitoring the external business environment and internal performance, and oversight of the successful discharge of the remit assigned to OS by Ministers. It comprises the Director General, seven Executive Directors and four Non-Executive Directors.

⁶² There are two corporate boards in OS, the Strategy Board and the Operating Board. The latter is responsible for all operational matters at the corporate level and the implementation of the strategy determined by the Strategy Board. It does not have any Non-Executive Director but comprises all seven Executive Directors of OS and the Head of Strategy.

30.2 Non-Executive Directors are recruited from the private sector for the business, commercial and other skills they bring to OS. They are appointed by the responsible Minister after successfully passing a panel interview. Candidates are identified by a mix of advertising, head-hunting and examination of a register of potential candidates held centrally by the UK government.

30.3 Besides the Director General, OS also recruits Directors and Senior Managers through head-hunting and direct advertising. Applicants are solicited from both the public and private sectors. Existing staff can apply for posts at all levels as well and are treated on an equal basis as other applicants. At present, there are 65 Senior Managers within a total of 1 850 employees.

30.4 The Director General has authority for pay bargaining under delegation by central departments and is responsible for setting the terms and conditions of service for all OS staff below Director level.

30.5 The Director General has full powers in matters relating to the conduct and discipline of all employees, including dismissal, loss of pay and posting. A system of grievance and appeals procedures is available to staff, including the right of appeal to the Director General and to the Civil Service Appeals Board.

30.6 OS employs interim managers, contract staff and temporary staff for sales, marketing and information technology positions to help launch specific products or projects. All of them are not employed on full civil service terms but at market rates.

30.7 OS has found it difficult to attract and retain key staff within the constraints of civil service pay and conditions.⁶³ There is difficulty especially in the recruitment of senior staff at or above managerial level, and in the recruitment of marketing and sales, and information technology personnel.

Size and costs of staff

30.8 The size of staff in OS has been fairly constant. It employed around 1 800 full-time employees⁶⁴ from 1999-2000 to 2001-02. It had as many as 200 temporary staff working shifts in the past two years.

30.9 Staff costs have accounted for the largest share of OS' operating costs. In the first year of its operation as a trading fund, 57.3% of the operating costs were staff costs. In 2001-02, staff costs still accounted for 48.4% of the total operating expenses. Staff costs in 2001-02 were £56 million, up 5.8% from 1999-2000, while operating costs rose 25% during the same period.

⁶³ Quinquennial Review of Ordnance Survey, December 2001.

⁶⁴ The figure refers to the average monthly number of whole-time equivalents.

Early retirement schemes

30.10 The UK government granted £6 million to OS in each of the first three years since the establishment of the trading fund to fund the early retirement programmes.⁶⁵ This was an initiative to contain staff costs in order to allow OS to sustain adequate profitability into the future.

31. Market structure

31.1 OS has no direct competition in the provision of national geo-reference database based on physical surveying. However, the Quinquennial Review completed in December 2001 stated that, with the advent of technology, it was feasible to obtain cheaper alternative to OS data for some applications and it was reasonable to assume that the degree of monopoly that OS enjoyed would steadily be eroded. In addition, OS is also facing competition from the private sector in the provision of products such as maps.

32. Fees and charges

32.1 OS is responsible for its own pricing and licensing policies under the Treasury Fees and Charges Guide which permits the concept of market pricing. OS claims that market forces have the greatest impact upon its pricing and licensing policies. However, the Quinquennial Review of OS concluded that given its near monopoly status, it had been difficult for OS to establish a true market price for its services.

32.2 OS has adjusted the prices of some of its services and products during the past three years, with both increases and reductions.⁶⁶ The revision of fees and charges does not require parliamentary approval. However, OS cannot employ pricing and licensing policies that are in conflict with the Competition Law. In particular, OS cannot charge predatory prices that undercut competitors by failing to recover the costs of production plus a return on investment.

32.3 Pricing and licensing policies are also subject to audit by Her Majesty's Stationery Office, which has recently introduced a Fair Trader Scheme for trading funds. Additionally, the Office of Fair Trading may review OS' pricing and licensing policies if it receives and investigates a complaint that gives it cause for concern.

32.4 OS operates a 'user pays' business model. It recouped a steadily increasing proportion of its operating costs, from 93% in 1999 to 98% in 2000.

⁶⁵ The schemes were largely aimed at volunteers. Compulsory redundancies were no more than five.

⁶⁶ The average increase or decrease is not available.

33. Financial targets and attainment

33.1 OS undertakes commercial and non-commercial activities. It is required to balance the public interest in maintaining a consistent and accurate topographic survey across the whole of Great Britain, whilst earning revenues in a commercial and competitive market place and reducing dependence on taxes.

33.2 The public interest in mapping is met through a tightly specified and monitored agreement between OS and the central government, i.e. the National Interest Mapping Service Agreement (NIMSA) which was inaugurated in April 1999. Under NISMA, the government provides an annual income to OS to fund mapping activities that are identified as being essential to the national interest but unlikely ever to be commercially viable.

33.3 For the commercial activities provided by OS, the long-term financial target is to achieve an average annual return on capital employed (ROCE)⁶⁷ of at least 9% of net assets employed over the period from 1 April 1999 to 31 March 2004.

33.4 In the Framework Document, it is stated that the long-term targets may also include a reduction in the ratio of general business overhead costs to total operating costs year on year. Growth in OS business compared to the associated growth elsewhere in the public and private sectors, such as growth of Gross Domestic Product, may also be included as long-term targets.

33.5 Apart from long-term targets, there are major annual targets:

- (a) To break even taking one year with another;
- (b) To achieve a prescribed revenue target; and
- (c) To increase revenue generated per member of staff year on year.

33.6 One of the financial objectives of OS is to achieve an average annual rate of return of at least 9% over the period of 1 April 1999 to 31 March 2004. OS achieved an average annual ROCE of 10.7% over the first three years. OS also succeeded in achieving and exceeding the prescribed revenue target by a narrow margin in all three years since the commencement of the trading fund operation (See Table 7).

33.7 However, in 2001-02, OS suffered a loss and recorded a rate of return of -9.1%. OS states that the loss recorded in 2001-02 was the result of its deliberate decision to invest for the future rather than holding back to balance the books. The investment in 2001-02 was £35 million, compared to £19 million in the year before.

⁶⁷ Return on capital employed is calculated as a percentage of an operating surplus before the payment of interest and dividends to the average net assets in real terms.

Table 7 - Rate of return and performance of other financial targets of OS

	99/00	00/01	01/02
Revenue target	£83.4 million	£82.3 million	£85.6 million
Achieved revenue	£85.0 million	£86.1 million	£86.6 million
Target return on sales	Not less than 5%	Not less than 5%	Not applicable ⁶⁸
Achieved return on sales	14.7%	9.4%	Not applicable
Revenue per £1 of labour cost	£1.87	£1.8	£1.82
Target rate of return ⁶⁹	9%	9%	9%
Achieved rate of return	10.7% ⁷⁰		

33.8 OS is not required to pay corporate tax on its profits. It is also not required to pay dividends to the government capital for the first five years of operation as a trading fund.

34. Service targets and attainment

Targets and performance

34.1 The main services provided by OS are:

- (a) Provision of mapping and geographical or spatial data in the form of maps and computer files;
- (b) Working closely with the private sector partners to offer value-added products and services;
- (c) Provision of advice and technical services, notably to the Department for International Development in support of the British aid programme and provision of services overseas to customers such as the European Union and the World Bank; and
- (d) Introduction of new geographical information and mapping-related products and services.

⁶⁸ Targets were set against return on sales in the first two years of the trading fund operation of OS but not in the third year.

⁶⁹ These target rates of return refer to an average annual return on capital employed of at least 9% over the period of 1 April 1999 to 31 March 2004.

⁷⁰ The average rate of ROCE achieved from 1999-2000 to 2001-02 was 10.7%. The rate of ROCE for each of the three years is not available.

34.2 The long-term target is to promote and enhance the quality and currency of the National Topographic Database in line with customer requirements. As for annual targets, there are targets regarding output, quality of service, efficiency, web site, as well as environmental protection. For instance, in 2001-02, OS introduced a target of reducing carbon emissions from the OS Headquarters by at least one per cent year on year. Overall, the OS Trading Fund has managed to achieve and exceed all the targets since its commencement.

Staff incentive scheme

34.3 OS has a performance bonus which is payable to all staff based upon meeting the organization's performance targets. If OS exceeds its revenue target, the maximum bonus is 20% of the excess above the target. If one of the other performance targets is not achieved, the percentage awarded is reduced to 10%. If two other targets cannot be met, there will be no performance bonus.

Customer feedback

34.4 Eight special interest committees representing different groups of users with common interests meet twice yearly to provide inputs concerning the products and services of OS.

34.5 A customer satisfaction survey is conducted on an annual basis. The survey in 2001 found that some 85% of customers rated the quality of OS' services as excellent to good.

New and enhanced services and products

34.6 The major new services and products provided by OS are:

- (a) Get-a Map, a free on-line mapping service;
- (b) Web-based support programme for business partners to develop business ideas and software using the core data of OS;
- (c) New Global Positioning System services;
- (d) Free maps of local area for every 11-year-old in Great Britain to support the national curriculum in schools;
- (e) Our Favourite Places, the first online and interactive national travel guide produced by children for children;
- (f) Highly detailed mapping of rural areas to help tackle the spread of foot-and-mouth disease;

- (g) Development of a digital mapping database called the OS MasterMap which provides an accessible and flexible way to link information across and between both public and private bodies; and
- (h) Digital National Framework which enables OS to transform itself technically to go into e-business.

35. Public accountability

35.1 The Framework Document sets out the aims and objectives of OS, and the boundaries between policy and service delivery functions. It also describes the monitoring, accountability and reporting procedures between the OS Trading Fund and the Office of the Deputy Prime Minister. If at any time it becomes apparent to the Deputy Prime Minister or to the Ordnance Survey Management Board that any part of the Framework Document is no longer appropriate, the Director General will prepare a revised text which will be agreed on with the Office of the Deputy Prime Minister, and with HM Treasury and the Cabinet Office.

Minister

35.2 The Deputy Prime Minister determines the policy and financial framework within which OS operates and approves the corporate business plan. He delegates the authority of the day-to-day management of OS to the Director General.

35.3 The Deputy Prime Minister is answerable to Parliament for all matters concerning OS and deals with questions of policy and enquiries from Members of Parliament (MPs) and Members of the European Parliament (MEPs) who specifically seek a ministerial response.

35.4 The Deputy Prime Minister decides who should represent him at Departmental Select Committee hearings. In practice, where a Committee's interest is confined to the day-to-day operations of OS, the Deputy Prime Minister normally appoints the Director General to answer on his behalf.

Director General

35.5 The Director General is responsible for the day-to-day management of OS and making periodic reports to the Deputy Prime Minister on the trading fund's performance and progress. She prepares a corporate business plan which covers strategic issues over a period of at least three years, and is reviewed no less than annually by the Deputy Prime Minister.

35.6 MPs and MEPs are encouraged to communicate directly with the Director General on day-to-day operational matters. The Director General's letters in reply to Parliamentary Questions are published in the Official Report of Parliament.

35.7 The Director General is appointed as the Accounting Officer of OS and is responsible for the proper, effective and efficient use of public funds. Accordingly, she may be required to appear before the Public Accounts Committee.

35.8 The Director General is the official advisor to the UK government on all survey, mapping and geographical information matters and may thus be called upon by any government department for such advice.

Publication of documents

35.9 The Framework Document requires copies of the Framework Document and any subsequent amendments to be placed in the libraries of the Houses of Parliament. The Framework Document can be downloaded from OS' web site or from OS' Customer Information HelpLine.

35.10 Both the annual report and the audited accounts of OS are laid before both Houses of Parliament. Its corporate business plan is not published for reasons of commercial confidentiality.

Part 7 - HM Land Registry Trading Fund of the United Kingdom

36. Background

36.1 HM Land Registry (HMLR) is responsible for keeping a register of title to freehold and leasehold land throughout England and Wales. Its main purpose is to register title to land in England and Wales and to record dealings once the land is registered.

36.2 Its status was changed to an executive agency in July 1990 and then a trading fund in April 1993 after Parliament approved the HM Land Registry Trading Fund Order in March 1993.

36.3 The Chief Land Registrar is the Chief Executive of HMLR and is directly accountable to the Lord Chancellor for the performance of HMLR in accordance with the aims and objectives set out in the Framework Document. The Lord Chancellor has ministerial responsibility for HMLR.

36.4 The Quinquennial Review of HMLR completed in June 2001 concluded that HMLR should retain its trading fund status.

37. Staffing

Staffing flexibility and private sector expertise

37.1 The Chief Land Registrar is recruited through open competition and appointed by the Lord Chancellor. Some of the senior posts are also recruited through open competition, with the objectives of bringing in commercial experience and fresh ideas.

37.2 The Non-Executive Directors of the Land Registry Board also come from the private sector. HMLR is run by a Management Board comprising two divisions, the Land Registry Board (the LR Board) which is responsible for determining HMLR's policies and strategy, and the Business Development and Information, Communication and Technology Group⁷¹. The first Non-Executive Director from the private sector was appointed to the LR Board on 1 January 2001. Currently, there are two Non-Executive Directors out of a total of six Board Members. In addition, there are five senior officers of HMLR serving as Associate Board Members who attend meetings of the Board.

⁷¹ The Business Development & Information and Communications Technology Group is co-chaired by the Director of Finance and Director of Information Systems. It is responsible for promoting business development of HMLR and reporting to the Management Board on business issues.

37.3 The staff of HMLR are civil servants employed on terms and conditions of service consistent with the rules and principles set out in the Civil Service Management Code. Contract staff are rarely used, while HMLR uses overtime to manage workload.

37.4 The Chief Land Registrar is responsible for the appointment of the staff of HMLR and the determination of their tenure and other conditions of appointment. HMLR conducts its own pay bargaining and has introduced its own pay and grading structures subject to its specific requirements. The Chief Land Registrar has full powers in matters relating to the conduct and discipline of all employees, including dismissal.

Size and costs of staff

37.5 In the first year of its operation as a trading fund, the average number of staff employed by HMLR stood at 9 042, which was reduced continuously over the years to 7 801 in 2000-01⁷² (13.7% lower than that in 1993-94).

37.6 There was a recruitment moratorium for HMLR following the 1989 slump in the property market. Since 1997, its recruitment policy has been only replacing staff who has left or retired. Between 1989 and 1997, it lost an average of some 400 people each year through resignation and retirement.

37.7 Over the years, the size of the operational staff has been cut by 14.9%, whilst the number of managers, and administration and information technology staff has increased.

37.8 According to the Quinquennial Review completed in 2001, HMLR generally experienced no difficulty in recruitment except for the most senior and specialist levels, and in the London area as well.

37.9 Staff costs have accounted for the largest share of the operating costs of HMLR. Staff costs have been kept at around 70% of the operating costs over the years. Staff costs in 2000-01 were £183 million, up 29% since 1993-94.

38. Market structure

38.1 As HMLR is defined by statutes as the organization to register title to land in England and Wales and to record dealings such as sales and mortgages once the land is registered, its operations are monopolistic in nature.

⁷² The figure refers to the average number of full-time employed civil servants.

39. Fees and charges

39.1 The Framework Document states that one of HMLR's strategic objectives is to achieve a continuing reduction in the real value of fees charged to the public by progressively reducing unit costs. HMLR is also required to ensure that the fees charged reflect the appropriate costs of services it provides and the expenditure required to meet its principal aims.

39.2 The pricing policy is full cost recovery and to achieve the prescribed return on capital employed (ROCE). It is also the policy of HMLR to pass back any surplus to customers directly, in fee reductions, or indirectly, by providing new or improved services. A three-year agreement was reached in 1996 to enable surplus income generated between 1993 and 1995 to be applied to fee reductions. Meanwhile, HMLR reduced its fees by an accumulative 40.6% from 1993-94 to 2000-01.

39.3 For revision of fees and charges, HMLR needs the approval of HM Treasury subject to the advice of the Land Registration Rule Committee. The Committee is a statutory body, chaired by a High Court judge, whose members are appointed by the Lord Chancellor, with the Chief Land Registrar as a permanent member. It makes recommendations on any revision to the Lord Chancellor who will sign a Statutory Instrument together with two of the Lord Commissioners of the Treasury⁷³ to give effect to the change.

40. Financial targets and attainment

40.1 The Lord Chancellor, with the concurrence of HM Treasury, has set an objective for HMLR to achieve a rate of ROCE of at least 6% a year⁷⁴, on average, over the period of 1 April 2000 to 31 March 2005.⁷⁵ HMLR has achieved the target rate of return since the commencement of its operation as a trading fund.

40.2 The rate of ROCE of 5% in 1998-99 was the lowest rate being achieved and HMLR explained that it reflected the effect of the fee reduction in 1997.

⁷³ The role of the Lords Commissioners is in essence to relieve both the Prime Minister and the Chancellor of the Exchequer of the task of signing certain documents requiring the approval or consent of HM Treasury, such as Treasury Warrants, statutory instruments and certain Treasury Guarantees.

⁷⁴ Return on capital employed is calculated as a percentage of an operating surplus before the payment of interest and dividends to the average net assets in real terms.

⁷⁵ The target rate set for the period from April 1993 to 31 March 1998 was at least 6% as well. However, there was an agreement with HM Treasury to reduce the target between 1 April 1996 and 31 March 1999 to allow larger fee reduction.

40.3 HMLR has also met targets on cost per unit in real terms and in cash terms. The cost per unit in real terms has been reduced by 15% since 1995-96 and the cost per unit in cash terms has been reduced by 3.5% during the same period.

Table 8 - Rate of return of HMLR

	93/94	94/95	95/96	96/97	97/98	98/99	99/00	00/01
Target cost per unit in real terms	Not applicable		£28.7	£27.84	£26.67	£25.91	£25.13	£25.09
Cost per unit in real terms			£27.48	£27.08	£26.52	£25.66	£22.40	£23.45
Target cost per unit in cash terms	Not applicable		£30.92	£30.70	£30.27	£30.06	£30.15	£30.57
Cost per unit in cash terms			£29.60	£29.87	£30.10	£29.77	£26.88	£28.57
Target rate of return	6%	6%	6%	3%	2%	3%	6%	6%
Actual rate of return	29%	26%	12%	22%	12%	5%	19%	12%

41. Service targets and attainment

Targets and performance

41.1 The main functions of HMLR are:

- (a) To keep a register of title to freehold and leasehold land throughout England and Wales;
- (b) On behalf of the Crown, HMLR guarantees title to registered estates and interests in land;
- (c) To register certain third-party rights under the Land Charges Act 1972 and the Agricultural Credits Act 1928; and
- (d) To provide access to up-to-date and guaranteed land information, enabling confident dealings in property and security of title.

41.2 HMLR has achieved and exceeded most of the major performance targets. A few of the service standards have not been revised for a number of years,⁷⁶ while most of the others have been gradually tightened over the years.

⁷⁶ For example, the 'Percentage of all registrations processed in 25 days' has been set at 80% since 1997-98.

Staff incentive scheme

41.3 Under the annual bonus scheme, HMLR may award its staff up to 2.5% of the permanent wage bill (including national insurance) when it has achieved its cost per unit target. The amount of award is assessed on achievements against individual key performance indicators.

41.4 HMLR is required to introduce a new performance pay regime in accordance with Cabinet Office guidelines and based on the new arrangements for the Senior Civil Service.

Customer feedback

41.5 HMLR has conducted an annual customer survey since the time before the setting up of the trading fund. The survey of 2000-01 showed that over 99% of the customers were either 'very satisfied' or 'satisfied' with the full range of services provided by HMLR while 95.2% were 'very satisfied' or 'satisfied' with the speed with which HMLR dealt with registrations.

41.6 HMLR holds two user panels with major customers each year, and holds regular meeting with the Law Society, the Council of Mortgage Lenders and other representative groups.

41.7 An Independent Complaints Reviewer has been appointed since 1998 to investigate complaints of mal-administration where the complainant is not satisfied with HMLR's internal complaint procedure.

New and enhanced services and products

41.8 The major new services provided by HMLR are:

- (a) Regular publication of the Land Registry Residential Property Price Report;
- (b) Receiving applications for official searches by telephone;
- (c) Computer property database which enables the register to be readily accessed by property address;
- (d) 'Land Registry Direct' which allows electronic delivery of certain applications and on-line ordering of other services;
- (e) E-conveyancing which gives all applications and searches 'real time priorities';

- (f) Property Price Data, Land Registry forms, and fees information can be viewed and downloaded through WAP;
- (g) Index Map Imaging System;
- (h) On-line access to the land register; and
- (i) Charge certificates following the registration of mortgages in paperless electronic form.

42. Public accountability

42.1 The Framework Document sets out the aims and objectives of HMLR, and the accountability and reporting patterns between the HMLR Trading Fund and the Lord Chancellor. The Framework Document is reviewed every five years, or more frequently if changes are sought by the Lord Chancellor or the Chief Land Registrar in the light of experience of its operation or changes in circumstances.

Lord Chancellor

42.2 The Lord Chancellor is accountable to Parliament for HMLR. He is represented in the House of Commons by the Parliamentary Secretary to the Lord Chancellor's Department. The Lord Chancellor encourages MPs to write directly to the Chief Land Registrar on matters concerning the day-to-day operation of HMLR, and normally asks the Chief Land Registrar to reply to correspondence on such matters that he himself receives from MPs.

42.3 The Lord Chancellor or the Parliamentary Secretary responds substantively to Parliamentary Questions and correspondence on matters which relate to HMLR and which go beyond the delegations he has made to the Chief Land Registrar.

42.4 The Lord Chancellor, with the advice and assistance of the Lord Chancellor's Department and HMLR, determines the financial and other performance targets set out in HMLR's corporate and business plans. He is responsible for:

- (a) Setting and reviewing strategic objectives;
- (b) Setting long and short-term financial objectives and other performance targets;
- (c) Setting HMLR's fees in accordance with the relevant statutory provisions;

- (d) Approving HMLR's submission to HM Treasury under the Public Expenditure Survey;
- (e) Monitoring the achievement of targets;
- (f) Appointing and approving the conditions of service of the Chief Land Registrar; and
- (g) Approving any future revisions to this Framework Document.

Chief Land Registrar

42.5 The Chief Land Registrar, as the Head of Department and the Chief Executive, normally gives evidence on behalf of the Lord Chancellor when the affairs of HMLR are being discussed by Parliamentary Committees.

42.6 The Chief Land Registrar is appointed as the Accounting Officer for the HMLR Trading Fund. As the Accounting Officer, the Chief Land Registrar can be summoned for examination by the Public Accounts Committee.

42.7 The Chief Land Registrar submits a corporate plan and a business plan for the Lord Chancellor's approval on an annual basis. The Lord Chancellor's approval provides formal authority for the Chief Land Registrar to act in accordance with the plans. The Chief Land Registrar also meets twice yearly with the Lord Chancellor to discuss HMLR's strategy and performance and provides a monitoring report in advance of each meeting.

42.8 The Chief Land Registrar is responsible for the management of its day to day operations, in particular:

- (a) Ensuring that HMLR fulfils the statutory requirements placed on it by the Land Registration Acts;
- (b) Providing strategic development, direction and leadership of HMLR, including the preparation and submission to the Lord Chancellor of HMLR's corporate and business plans and the annual report and Trading Fund Accounts; and
- (c) Ensuring that HMLR meets or surpasses the performance targets set by the Lord Chancellor.

Publication of documents

42.9 Copies of the Framework Document and any subsequent revisions are placed in the libraries of the Houses of Parliament and are provided upon request. The annual business plan and the corporate plan are also published.

Part 8 - Alternatives to enhance efficiency and quality of services

43. Executive agencies of the United Kingdom

43.1 Executive agencies are introduced with the objective of delivering government services more efficiently and effectively within available resources. The UK government may consider those executive agencies having the potential of earning enough revenue to meet their expenses as trading fund candidates. Executive agencies are in many ways similar to trading funds, but unlike trading funds, executive agencies are not self-financing. They still seek annual funding from Parliament and do not have to achieve a prescribed financial return. In addition, they are not subject to and thereby not benefited from market competition.

43.2 Features of executive agencies shared by trading funds are:

- (a) Executive agencies remain part of the civil service and the government system, but they have greater delegated authority on financial, pay and personnel matters;
- (b) A framework document agreed between an executive agency and the parent department sets out the financial targets and service performance targets of the agency. Performance is reported through the publication of annual reports;
- (c) The delivery of services is separated from policy work;
- (d) Chief executives of executive agencies have, in theory, complete discretion to manage in ways they believe appropriate for the delivery of the services;
- (e) Chief executives, often recruited by open competition, are employed on a fixed term contract, usually containing a clause on performance related pay;⁷⁷
- (f) Ministers do not have hands-on and day-to-day responsibility, but remain ultimately accountable to Parliament for the performance of the agencies; and
- (g) Abolition, privatization, contracting-out, and merger of given government functions are all options considered before an agency is set up. These options are normally reviewed by the agency every five years.⁷⁸

⁷⁷ According to the Next Steps Briefing Note from the Cabinet Office, 66.6% of the agency chief executive appointments were made by open competition and 31 external candidates fill the places, which represent 22.5% of total appointments of chief executives in September 1998.

⁷⁸ UK 2002, The Official Yearbook of the UK.

44. New mechanism for controlling public spending of the United Kingdom

44.1 Besides hiving off departments or functions of departments to establish trading funds and agencies, the UK government has also developed other public spending control measures to enhance efficiency.

44.2 The Labour Government in 1997 regarded the annual resource allocation exercise as unsatisfactory for putting emphasis on bargaining over inputs rather than an analysis of outputs and efficiency. It was suggested that excessive departmentalism and short-termism were the results of such budgetary measure.⁷⁹

44.3 The Comprehensive Spending Review (CSR) was conducted by the Labour Government to thoroughly examine an effective use of public money.

44.4 The CSR has led to significant changes in the framework for planning and controlling public spending, giving departments and executive agencies greater certainty and flexibility over their budgets, thereby enabling planning and management of resources over the medium term. The major changes are:⁸⁰

- (a) Three-year spending plans, known as Spending Reviews, are introduced, including a thorough review of departmental objectives to find the best way of delivering policy objectives;
- (b) The annual exercise which departments can bid for extra funds is replaced by a firm allocation of resources set for three years through Departmental Expenditure Limits (DELs);⁸¹
- (c) Allowing under-spending within DELs in a given year to be carried over to the following year, so as to assist departments in managing their budgets and avoid wasteful end-of-year spending surges;
- (d) Departments are allowed to keep and spend a number of receipts that are at present surrendered for central allocation as revenue; and
- (e) New Public Service Agreements prepared by departments listing specific output targets and efficiency targets⁸² that departments will deliver with the money provided.

⁷⁹ Stability and Investment for the Long Term- Economic and Fiscal Strategy Report 1998, presented to Parliament by the Chancellor of Exchequer, June 1998.

⁸⁰ Ibid.

⁸¹ Where expenditure such as social security benefit payments cannot be planned on a multi-year basis, it is covered by Annually Managed Expenditure (AME) which is subject to annual scrutiny as part of the Budget process. Over half of the total expenditure is managed through Departmental Expenditure Limits and the remainder is AME.

⁸² In the 2000 Spending Review, three-year efficiency targets range between three per cent and ten per cent are set.

45. New mechanism for enhancing efficiency and controlling public spending of Hong Kong

Enhanced Productivity Programme (EPP)

45.1 In the 1998 Policy Address, the Chief Executive of the Hong Kong Special Administrative Region announced the EPP, which required bureaux and departments to deliver productivity gains amounting to 5% of their operating expenditure within three years.

Save & Invest Account

45.2 Save & Invest Account was introduced along with the EPP to allow the bureaux and departments to share the fruits of the productivity gains. At the moment, half⁸³ of the unspent cash-limited departmental expenses for a year will be saved in a separate account.⁸⁴ The savings made in a particular year can be used for the subsequent three years before they lapse and can be drawn upon throughout the year.⁸⁵

45.3 In the upcoming financial year, the Government will widen the scope of unspent expenses that can be carried forward by including a certain percentage of non cash-limited and non-departmental expenditure. However, the period of time that the savings of a particular financial year can be used will be shortened. A certain percentage of unspent recurrent expenditure of a particular year will be identified in the following financial year and the savings can only be carried forward to the year after. In other words, a percentage of the savings in recurrent expenditure for 2003-04 will be identified in 2004-05 and reflected in the expenditure Estimates for 2005-06. The savings will no longer be drawn throughout the year. Instead, the proposed spending of these savings has to be reflected in the Estimates.

45.4 Save & Invest Account provides “a more certain source of funding as bureaux/departments do not have to compete with each other for capital funding in the annual Resource Allocation Exercise”.⁸⁶ Except for the creation of civil service posts and the payment of allowances, bureaux and departments may draw from the Account to spend on any purposes, provided that such spending is within the scope of the relevant heads and subheads of expenditure.⁸⁷

⁸³ The percentage of unspent expenditure in 2003-04 that can be carried forward is not yet decided.

⁸⁴ Windfall savings and saving which clearly are not attributable to the effort of the bureaux/departments will not be credited to the Account.

⁸⁵ Bureaux and departments have to submit an application to the Financial Services and the Treasury Bureau. Any items exceeding HK\$10 million require the approval of the Finance Committee of the Council.

⁸⁶ Third issue of the EPP Newsletter.

⁸⁷ In the first year when the Save & Invest Account was introduced, savings were once limited to one-off initiatives leading to productivity gains. This restriction has been relaxed.

Non-Civil Service Contract Staff Scheme and Voluntary Retirement Scheme

45.5 The Non-Civil Service Contract Staff Scheme allows government departments to engage short-term non-directorate staff on non-civil service term. Under the Scheme, government departments have the flexibility to determine the number of contract staff, offer contracts of terms up to three years and design their own recruitment procedures. They can also decide on the level of pay, provided that the pay is no more than the minimum salary of comparable civil service rank.⁸⁸

45.6 A central redeployment mechanism is created to re-deploy surplus staff as a result of the effort of government departments in enhancing productivity and efficiency.

45.7 The first phase of the Civil Service Voluntary Retirement Scheme was introduced in June 2000, providing a compensation package for staff in 59 grades to leave the service before retirement age. Some 10 000 civil servants have taken up this option. The Government has promised not to refill the 10 000 posts left vacant with civil servants at least within the following five years, but allows the posts to be filled with non-civil service contract staff instead.

One-Line Vote

45.8 Under the One-Line Vote scheme, government departments have more flexibility in deploying their resources within the overall budget.

45.9 One-Line Vote means placing all recurrent expenditure of a department under a single new subhead (i.e. Operational Expenses) which operates on a cash-limited basis. A Controlling Officer is given autonomy in deploying the funds among the various components of expenditure within the single subhead, without the need to obtain approval from the Financial Services and the Treasury Bureau or the Finance Committee of the Council.⁸⁹

45.10 One-Line Vote was introduced to five departments on a pilot basis in 1999-2000 and has since been extended to 23 departments. The Government plans to extend the one-line vote arrangement to all departments in the 2003-04 Estimates.⁹⁰

⁸⁸ Circular No. 2/99 promulgated by the Civil Service Bureau, which is summed up in the second issue of EPP Newsletter, June 1999.

⁸⁹ Ibid.

⁹⁰ Reply from Efficiency Unit, 23 August 2002.

Operational Expenditure Envelope

45.11 On the 2002 RAE, the Government adopts an ‘envelope’ approach for the budgeting of the coming financial year, under which it tentatively allocates to each Bureau Secretary an envelope of the recurrent part of the operating expenditure, setting out the resources available. These resources are net of efficiency savings at the rate of 1.8% in 2003-04 and an additional one per cent each year from 2004-05 to 2006-07. Subject to any limitations laid down by the Finance Committee of the Council, each envelope recipient has the flexibility to deploy resources among his/her responsible policy areas when preparing the Estimates of Expenditure (i.e. One-Line Vote). Apart from that, the capital expenditure RAE will be conducted in the usual manner.⁹¹

⁹¹ Financial Affairs Panel, CB(1)2467/01-02(01).

Part 9 - Analysis

46.1 For the purpose of facilitating Members to consider the proposal of changing the Rating and Valuation Department to trading fund status, this research studies two major issues based on the review of the operation of selected trading funds in Hong Kong and in the United Kingdom (UK) (for an overall comparison of the attributes of selected trading funds, see Appendix I):

- (a) Does the experience of the existing trading funds demonstrate that they can achieve the major benefits anticipated?
- (b) Is the establishment of trading fund the only means to fulfil the mission of enhancing efficiency and improving services?

46.2 With regard to the second issue, this analysis explores the additional personnel and financial flexibility introduced to both government departments of Hong Kong and executive agencies⁹² of the UK in recent years.

47. Cost of services

Size of staff

47.1 All the five selected trading funds except the Post Office have managed to reduce both the number of civil servants and their total number of staff after attaining the trading fund status.

47.2 All trading funds studied have engaged contract staff and temporary staff to cope with the increase in business volume or the provision of new services, except for HM Land Registry of the UK which prefers to have existing employees working overtime to cope with the changes in demand for services.

⁹² Executive agencies are distinct units performing government administrative tasks but they remain as part of the civil service. Under individual Framework Documents, they have greater delegation of financial, pay and personnel matters, clearer responsibilities and objectives, which are similar to those of trading funds. Unlike trading funds, the budgets of executive agencies still need approval of Parliament and they are not required to be self-financing. See Part 8 for detailed features of executive agencies.

Authority on pay and conditions of service

47.3 Considering the trading funds under study, although the size of staff has been kept in check, staff costs continue to rise. Staff costs are the largest component of the operational costs of all the trading funds, accounting for more than half of their operational expenses. In spite of the flexibility of employing contract staff and temporary staff, all of the trading funds are mainly staffed by civil servants. In Hong Kong, the pay and conditions of service of civil servants are fixed centrally across the board. The high staff cost and the lack of authority in determining the terms and conditions of service of staff may constrain trading funds' ability to address challenges and competition, as suggested by the Postmaster General.⁹³

47.4 For non-civil service contract staff, the general managers of trading funds in Hong Kong have the flexibility to set their pay and contract gratuity as long as they do not exceed those of their civil servant counterparts. However, there is a limitation in expanding the proportion of non-civil service contract staff, as the Civil Service Bureau may not be able to absorb and re-deploy all of the surplus general grades staff.

47.5 In the UK, both the Ordnance Survey and HM Land Registry have the power to set the pay and grading structure for staff who are civil servants under the Director grade, as far as it is within the rules of the civil service. The problem they face is different from that of Hong Kong, that is, they have difficulties in recruiting senior staff and specialists, as the civil service pay and conditions of service are not competitive.

48. Improvement in the quality of servicesPrivate sector expertise

48.1 Trading funds in both Hong Kong and the UK are headed by civil servants and staffed mainly by civil servants. Nonetheless, there is a growing trend for trading funds in the UK to draw on more commercial experience and skills from the private sector to improve the quality of services.

48.2 The general managers of trading funds in Hong Kong are selected from the pool of civil servants, whilst their counterparts in the UK are recruited through open competition. In the UK, the chief executives and some other senior posts of both the Ordnance Survey Trading Fund and HM Land Registry Trading Fund came from the private sector. They joined the civil service on a fixed term contract.

⁹³ P.C. Luk, "Post Office Trading Fund" in Anthony B. L. Cheung and Jane C. Y. Lee eds. *Public Sector Reform in Hong Kong Into the 21st Century*, Hong Kong: 2001, Chinese University Press.

48.3 In Hong Kong, both the Post Office and the Land Registry recruit from the private sector for some of the managerial positions in areas of business development, e-commerce and information technology.

48.4 A Board of Directors is responsible for determining the strategies and monitoring the performance of each trading fund in the UK. Both the Ordnance Survey and HM Land Registry recruit Non-Executive Directors from the private sector to sit on the Board. In Hong Kong, only the Electrical and Mechanical Services Trading Fund has a formal Management Board and an Executive Board, but all their Board members are senior civil servants of the trading fund and its parent Bureau.

Service targets and attainment

48.5 All of the trading funds under study have achieved and exceeded most of the service performance targets. Nonetheless, the service standards set for some of the performance pledges have not been revised for some years or have taken a number of years before they are revised. There is no evidence of any formal participation of third parties or service users in setting these standards and targets, but the trading funds under study stated that they would consider customers' opinion on their performance.

48.6 All of the five trading funds under study have established various channels to communicate with their major customers and collect their opinions. Customer satisfaction surveys are conducted annually or periodically by the trading funds. The general ratings of satisfaction have been high for the trading funds.

49. Measuring cost-effectiveness of trading funds

Market structure

49.1 One of the objectives of establishing a trading fund is to achieve greater efficiency and cost-consciousness through exposing the service to competition or price comparisons. However, if there is no alternative service provider in a market, a trading fund operating as a monopoly is not exposed to any market competition.

49.2 With the exception of the Electrical and Mechanical Services Trading Fund, the provision of services and products by the selected trading funds under study is, to a large extent, a monopoly. The private sector is often not empowered by law to provide the same service.

Fees and charges

49.3 The cost-effectiveness of a trading fund should theoretically be reflected in the level of fees charged for its services. However, the level of fees charged by the trading funds studied is, to a large extent, unable to serve as a yardstick of measuring cost-effectiveness, because most of their services are monopolistic in nature. For instance, the Quinquennial Review of the Ordnance Survey concluded that given its near monopoly status, it had been difficult for the Ordnance Survey to establish a true market price for its services.

Financial targets and attainment

49.4 The financial targets and performance of the trading funds are indicators of cost-effectiveness and efficiency. In both Hong Kong and the UK, there are statutory provisions requiring a trading fund to break even taking one year with another within a reasonable period of time. Nonetheless, two out of the five selected trading funds failed to break even and to attain the target rate of return for different lengths of time.

49.5 The rate of return attained by a trading fund may fluctuate greatly. In particular, the rate of return achieved could be influenced by factors other than its performance in the provision of goods and services in a particular year.

49.6 Among the trading funds of Hong Kong under study, the Post Office has employed other financial indicators, including target revenue and expenditure, unit cost of handling per local mail item and item per man-hour. For the trading funds of the UK, HM Land Registry has set targets on cost per unit in real terms and in cash terms, while the Ordnance Survey has set targets on annual revenue. The Framework Document of the Ordnance Survey stated that long-term targets might also include a comparison of the growth in business of the trading fund with the growth in Gross Domestic Product.

50. Public accountability

Accountability to the legislature and to the public

50.1 The Framework Agreement of a trading fund aims to define clearly the respective responsibility and relationship between the head of the trading fund and the head of the corresponding parent ministry/department/bureau. The former is responsible for the daily operation of the trading fund, while the latter is responsible for policy matters.

50.2 In Hong Kong, with the introduction of the Accountability System, the general manager of a trading fund reports directly to the Permanent Secretary on operational matters and seeks policy direction from the Bureau Secretary through the Permanent Secretary.

50.3 In both Hong Kong and the UK, trading funds have been given the freedom and flexibility to operate their business without the legislature's close monitoring. Whether this autonomy is accompanied with direct accountability to both the public and the customers at large depends on the transparency of their operations and whether market competition is available (See paragraphs 49.1 - 49.3).

50.4 The Ministers/Bureau Secretaries and/or heads of the trading funds attend meetings to brief the legislature on matters of concern either on their own initiative or upon request. At the same time, trading funds are statutorily required to submit their annual reports and financial statements to the legislature.

50.5 In the UK, copies of the Framework Documents of trading funds and any subsequent revisions are placed in the libraries of the Houses of Parliament and are provided upon request. For the Ordnance Survey, the Framework Document is also accessible on its web site.

50.6 The Framework Agreements of the trading funds of Hong Kong are not accessible to the general public, although Members of the Council were given a draft framework agreement when they scrutinized the resolution to establish the trading fund status for both the Post Office and the EMS Trading Fund. There is no arrangement for making the Framework Agreements publicly available in Hong Kong.

51. Alternatives other than establishing trading funds

Review of status

51.1 A review of status is conducted every five years for the two UK trading funds studied to see if they should operate in their existing status or should work under an alternative structure to meet their objectives more effectively. In conducting the review, the views and needs of customers, staff, trade unions and other stakeholders are taken into account. In Hong Kong, no regular review of similar nature is conducted.

Other means to improve efficiency and cost-effectiveness of services

51.2 In the UK, the form of executive agencies allows government departments to operate with more flexibility and clearer objectives. Apart from the fact that executive agencies continue to be subject to vote accounting and can retain only some of their receipts to build up reserves, the flexibility they have is not much less than that of trading funds. (See Appendix II)

51.3 In Hong Kong, more flexibility and freedom have been introduced in recent years to government departments for the purpose of enhancing productivity and controlling public spending. The Non-Civil Service Contract Staff Scheme allows both trading funds and government departments to employ staff on non-civil service terms and to set the level of salary as far as it does not exceed that of the civil servants. In addition, the Voluntary Retirement Scheme allows downsizing of the civil service.

51.4 Government departments are allowed to carry over half of their savings or underspending⁹⁴ to another year after the introduction of the Save & Invest Account. Trading funds have to pay notional taxes and dividends out of their surplus before they can keep the rest as savings and build up reserves. The surplus trading funds retain might be less than the amount retained under the Save & Invest Account if they were still government departments, as suggested by the Post Office Trading Fund.⁹⁵

51.5 After the introduction of One-Line Vote to all departments in the 2003-04 financial year, virement of funds within a department no longer needs to get the prior approval of the Financial Services and the Treasury Bureau.

51.6 Traditional government departments are enjoying much more flexibility and authority on various personnel and financial matters to improve cost-effectiveness. The establishment of a trading fund brings in an additional requirement of self-financing and breaking even, which provides the incentive to improve efficiency. In addition, the establishment of a trading fund exposes the provision of public services to market competition, which may in turn, have an impact on the cost-control of and the fees charged by the trading fund.

52. Issues to be considered

52.1 The study of the five selected trading funds of Hong Kong and the UK has provided references to the operation of trading funds in various aspects.

52.2 Although the selected trading funds have kept the size of staff in check and exceeded most of the service performance and rate of return targets, it is difficult to assess whether they have provided cost-effective services when most of them operate as monopolies. Members may wish to consider whether other indicators should be taken into account along with the rate of return measure to evaluate the performance of trading funds. (Examples of these alternative indicators are given in paragraph 49.6.) Members may also wish to consider whether the Rating and Valuation Department would experience and benefit from any market competition if it attains the trading fund status.

⁹⁴ The Government has not yet decided whether the percentage of savings that can be carry over will remain at 50% in 2003-04.

⁹⁵ Reply of the Post Office Trading Fund.

52.3 Members may also wish to review the limitation of trading funds on personnel matters and consider whether this limitation will remain a constraint for the proposed Rating and Valuation Department Trading Fund in controlling costs.

52.4 One of the purposes of establishing trading funds is to provide services on a quasi-commercial basis to enhance efficiency and effectiveness. Members may wish to consider whether existing and future trading funds of Hong Kong can draw on more private-sector expertise on both directorate and managerial levels.

52.5 Members may wish to consider if a regular review of status should be conducted for the trading funds of Hong Kong as in the case of the UK trading funds.

52.6 Apart from establishing trading funds, Members may wish to consider whether the existing and upcoming flexibility and freedom given to the government departments of Hong Kong are sufficient to provide the means to enhance the efficiency and quality of their provision of services.

52.7 Members may also wish to take reference of the reforms introduced in the UK, and consider whether some features of executive agencies are appropriate for the government departments of Hong Kong.

Appendix I

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Background					
Year of establishment of the trading fund	1993	1995	1996	1999	1993
Staffing					
Change in the total number of staff after attaining trading fund status ⁹⁶	Reduced by 2.6% from August 1993 to March 2002	Increased by 21.1% from August 1995 to March 2002	Reduced by 3% from August 1996 to March 2002	Reduced by 1.3% from April 1993 to March 2001	Reduced by 13.7% from April 1999 to March 2002
Change in the number of civil servants employed after attaining trading fund status	Reduced by 11.2%	Increased by 4.5%	Reduced by 16.5%	More or less of the same magnitude as above ⁹⁷	More or less of the same magnitude as above ⁹⁸
Head of trading fund has authority to determine establishment	Yes, on the non-directorate level	Yes, on the non-directorate level	Yes, on the non-directorate level	Yes, below the level of senior civil servants	Yes, below the level of senior civil servants
Engaging non-civil service contract and temporary staff	Yes	Yes	Yes	Yes	Rarely
Percentage of non-civil service staff as at 31 March 2002	14.3%	22.3%	13.8% ⁹⁹	Not available	Not available

⁹⁶ The total number of staff refers to the sum of the number of civil servants employed and the number of non-civil service temporary and contract staff employed.

⁹⁷ Separate figures of the number of civil servants and the number of non-civil service staff are not available.

⁹⁸ Ibid.

⁹⁹ The non-civil service staff here include the temporary staff hired by hire-of-service contracts through agencies.

Appendix I (cont'd)

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Staff cost					
Staff costs as the largest share of the operating costs	Yes	Yes	Yes	Yes	Yes
Staff costs as a percentage of the operating costs in 2000-01	64.4%	63.3%	59.6%	48.4%	68.3%
Pay and conditions					
Head has authority to set pay and grading of its civil service staff	No	No	No	Yes, except for the Senior Civil Service	Yes, except for the Senior Civil Service
Private sector expertise					
Headed by a civil servant	Yes	Yes	Yes	Yes, but on contract terms	Yes, but on contract terms
Recruitment of Head	In-service appointment	In-service appointment	In-service appointment	Through open competition	Through open competition
Recruitment of other senior posts through open competition or from the private sector	Yes, six professionals ¹⁰⁰ are recruited through open competition and three of them are equivalent to senior government positions	Yes, 45 managerial positions (below directorate level) are recruited through open competition ¹⁰¹	No	Yes, Directors and Senior Managers are recruited through head-hunting and advertising	Yes, some senior posts are recruited through open competition
Governed by a Board	No	No	Yes	Yes	Yes
Non-Executive Directors are appointed to the Board	No	No	No	Yes, the four Non-Executive Directors come from the private sector	Yes, the two Non-Executive Directors come from the private sector

¹⁰⁰ All six are employed on non-civil service contract terms. Five of them are information technology professionals and the remaining one is an accounting assistant.

¹⁰¹ They are employed on non-civil service contract terms. In addition to these managers, consultants have been employed from time to time on a case by case basis.

Appendix I (cont'd)

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Service targets and attainment					
Attainment of performance pledges	Achieved and exceeded most of the targets	Achieved and exceeded most of the targets	Overall actual performance exceeded the targets ¹⁰²	Achieved and exceeded all the targets	Achieved and exceeded most of the targets
Major customer feedback mechanism	(a) Three Customer Liaison Groups (b) A Standing Committee comprising representatives from the Land Registry and the Law Society	(a) Customer Liaison Groups (b) Market research and a regular Mystery Shopper Survey Programme	Client managers are appointed	Eight special interest committees representing users	(a) Two user panels with top level customers (b) The Independent Complaints Reviewer is appointed to investigate complaints of mal-administration
Customer satisfaction survey	Conducted periodically	Conducted annually	Conducted every other year	Conducted annually	Conducted annually
Staff incentive scheme					
Staff incentive scheme to encourage improvement in the quality of services	Yes, a Performance Incentive Scheme where awards are in kind and not in cash	Yes, a Staff Recognition Fund to recognize the contribution of staff through competitions and activities but awards are in kind and not in cash	Yes, a Staff Encouragement Scheme with an award in the form of supermarket coupons	Yes, bonus up to 20% of the excess above the revenue target	Yes, bonus up to 2.5% of wage

¹⁰² The Electrical and Mechanical Services Trading Fund has different set of performance indicators and targets for different clients.

Appendix I (cont'd)

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Market structure					
Monopolistic in nature	Yes, the statutory registration service is a monopoly The searching service is not monopolistic but its comprehensive data base gives it an advantage	Monopoly in providing a local and overseas letter service in Hong Kong and in the issue of stamps Parcel delivery and courier services are not monopolistic	No, all government departments and public bodies have been free to choose suppliers since August 2002	Yes, the provision of natural geo-reference database is a monopoly No monopoly in the provision of maps	Yes, the statutory service of registration is a monopoly The searching service is not monopolistic
Fees and charges					
Fees adjustment required approval of legislature	Yes, by negative vetting of the Council	No, the Postmaster General may determine the postage rates and fees for services provided as a certification authority However, charges for ancillary postal services are subject to vetting of the Council	No, the Trading Fund makes the decision	No, the Trading Fund is responsible for its own pricing policy ¹⁰³	No, but it needs the approval of HM Treasury and the Land Registration Rule Committee before the Lord Chancellor signs with two Lord Commissioners of HM Treasury to give effect to the change
Revision in fees and charges since attaining the trading fund status	Increased three times	Increased three times and had two reductions	19.4% reduction in price in real terms up to 2002	Details not available (there were both price cuts and price increases)	Reduced by an accumulative 40.6% from 1993-94 to 2000-01

¹⁰³ The pricing is subject to the Treasury Fees and Charges guide, the audit of Her Majesty's Stationery Office and the investigation of the Office of Fair Trading.

Appendix I (cont'd)

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Financial targets and attainment					
Any operating deficit	No	Yes, an operating deficit was recorded in three years from 1998-99 to 2000-01 ¹⁰⁴	No	Yes, an operating deficit of £7.5 million was recorded in 2001-02 ¹⁰⁵	No
Target rate of return	10%	10.5% ¹⁰⁶	13.5%	9% ¹⁰⁷	6% ¹⁰⁸
Attained target rate of return	Yes, all the time	Sometimes. It failed to attain the target rate from 1998-99 to 2000-01	Yes, all the time	Yes, on average over the period of 1 April 1993 to 31 March 2002 but it recorded a loss and a negative rate of return in 2001-02	Yes, all the time
Actual rate of return	Ranging from 10.3% to 37.3%	Ranging from 1.8% to 47.8%	Ranging from 16.8% to 52.5%	Ranging from -9.1% to 39.4%	Ranging from 5% ¹⁰⁹ to 29%
Efficiency/productivity improvement					
Indicators of efficiency / productivity improvement	No	(a) Unit cost of handling per local mail item has increased 13.6% since 1995-96 (b) Productivity measured by items per man-hour has increased 7.4% since 1995-96	Achieved an accumulative 22.5% in productivity improvement	(a) Revenue target was achieved each year since 1999-2000 (b) Revenue per £1 of labour cost was reduced by 2.7% from 1999-2000	(a) Cost per unit in real terms is reduced by 14.7% compared to that in 1995-96 (b) Cost per unit in cash terms is reduced by 3.5% compared to that in 1995-96

¹⁰⁴ An operating deficit of HK\$149.8 million, HK\$76.8 million and HK\$31.5 million was recorded in 1998-99, 1999-2000 and 2000-01 respectively.

¹⁰⁵ The Ordnance Survey explained in its annual report that the loss was the result of its deliberate decision to invest for the future rather than hold back to balance the books.

¹⁰⁶ The prescribed rate was set at 12% per annum in 1995 but was tuned down to 10.5% in 1996.

¹⁰⁷ The target rate of return is an average annual return of at least 9% over the period of 1 April 1999 to 31 March 2004.

¹⁰⁸ The Lord Chancellor has initially set for HM Land Registry the objective of an overall average return for the period of 1 April 1993 to 31 March 1998 of at least 6% a year. However, from 1996-97 to 1998-99, a target rate of return of less than 6% was set to allow larger fee reductions. Since 1999-2000, the target has been an average of 6% over the five years ending 31 March 2005.

¹⁰⁹ The lower than 6% rate of return reflected the effect of fee reduction agreed between the HM Land Registry and the central government.

Appendix I (cont'd)

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Review					
Regular review of trading fund status	No	No	No	Yes, three years after it is established and then every five years a review will be conducted	Yes, every five years
Review of Framework Agreement	Normally reviewed every three years	Normally reviewed every three years	May at any time vary the contents of the Framework Agreement	Reviewed three years after the Framework Agreement is published and revised at any time when the text is no longer appropriate	Reviewed every five years or more frequently

Appendix I (cont'd)

An overall comparison of the attributes of selected trading funds in Hong Kong and in the United Kingdom

Attributes of Trading Funds	Hong Kong			United Kingdom	
	Land Registry Trading Fund	Post Office Trading Fund	Electrical & Mechanical Services Trading Fund	Ordnance Survey Trading Fund	HM Land Registry Trading Fund
Public accountability					
Establishment of trading fund needs approval of the legislature	Yes	Yes	Yes	Yes	Yes
Detailed approval of budget by the legislature	No	No	No	No	No
Who speaks for the policy matters relating to the trading fund	Secretary for Housing, Planning and Lands	Secretary for Economic Development and Labour and the Secretary for Commerce, Industry and Technology	Secretary for the Environment, Transport and Works	Deputy Prime Minister	Lord Chancellor and the Parliamentary Secretary to the Lord Chancellor's Department (representing Lord Chancellor) in the House of Commons
Head of the trading fund is responsible for the day-to-day operational matters and answers questions relating to such matters	Yes	Yes	Yes	Yes	Yes
Annual report and financial statement submitted to the legislature	Yes	Yes	Yes	Yes	Yes
Annual report published	Yes	Yes	Yes	Yes	Yes
Framework Agreement available to the public	No	No	No	Yes, on the web site, in the libraries of the Houses of Parliament and provided upon request	Yes, in the libraries of the Houses of Parliament and provided upon request

Appendix II

Comparison of the operation of government departments/executive agencies and trading funds in Hong Kong and in the United Kingdom

Attributes	Hong Kong		United Kingdom	
	Trading funds	Government departments	Trading funds	Executive agencies
Budget	On-going basis Required to submit to the parent bureaux a medium range corporate plan and an annual business plan	Annualized	On-going basis Required to submit to the parent department a medium-term corporate plan covering a three-year period and a short-term operating plan	Given a Departmental Expenditure Limit (DEL) for a three-year spending plan
Earnings/ savings	Retained as reserves but part of it is returned to the government as dividends on government investment	Returned to General Revenue in general but part of the unspent expenses may be saved under the Save & Invest Account for future usage	Retained as reserves but part of it is returned to the government as dividends on government investment	Underspending within DEL in a given year allowed to be carried over Allowed to keep some receipts but the rest has to be surrendered for central allocation as general revenue
Virement of funds between subheads	No need to obtain prior approval	May require approval of the Financial Services and the Treasury Bureau or the Finance Committee of the Council For departments with one-line vote, they may transfer the funds between subheads without prior approval	No need to obtain prior approval	Require the agreement of the Treasury

Appendix II (cont'd)

Comparison of the operation of government departments/executive agencies and trading funds in Hong Kong and in the United Kingdom

Attributes	Hong Kong		United Kingdom	
	Trading funds	Government departments	Trading funds	Executive agencies
Funding	Assets appropriated as government equity and loans Self-financing on operational revenue	On-vote	Assets appropriated as government equity and loans Self-financing on operational revenue	On-vote
Financial objective	Achieving target rate of return on capital invested	Spending within budgets	Achieving target rate of return on capital invested	Spending within budgets and some of the agencies have set a target rate of return
Charging	Part or full cost recovery or profit making	Free, subsidized, part or full cost recovery or tax loaded	Full cost recovery or profit making	Free, subsidized, part or full cost recovery or tax loaded
Staffing	Mainly civil servants	Mainly civil servants	Mainly civil servants but heads and some of the senior posts of the trading funds are recruited through open competition	Mainly civil servants but senior positions are recruited through open competition
Flexibility to employ non-civil service staff	Having the flexibility to engage staff under the Non-Civil Service Contract Staff Scheme and to employ temporary staff.	Same as trading funds	Having the flexibility to engage contract and temporary staff	Having the flexibility to engage contract and temporary staff
Exclusive staffing flexibility of trading funds	Not subject to Notional Annual Mid-point Salary control, establishment ceiling for non-directorate establishment, and vote funding control.	Not applicable	No	Not applicable

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