

I. Introduction

The Establishment of the Committee The Public Accounts Committee is established under Rule 72 of the Rules of Procedure of the Legislative Council of the Hong Kong Special Administrative Region, a copy of which is attached in *Appendix 1* to this Report.

2. **Membership of the Committee** The following Members are appointed by the President under Rule 72(3) of the Rules of Procedure to serve on the Committee:

Chairman : Dr Hon Philip WONG Yu-hong, GBS

Deputy Chairman : Hon TAM Heung-man

Members : Hon LAU Kong-wah, JP
Hon Andrew CHENG Kar-foo
Hon Abraham SHEK Lai-him, JP
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon Albert Jinghan CHENG

Clerk : Ms Miranda HON Lut-fo

Legal Adviser : Mr Jimmy MA Yiu-tim, JP

3. As Hon TAM Heung-man, Hon Andrew CHENG Kar-foo and Hon LAU Kong-wah had declared their personal interest in respect of the chapter on “Control and monitoring of District Council expenses and related activities”, and Hon Albert Jinghan CHENG had also declared his personal interest in respect of the three chapters relating to the English Schools Foundation, the Committee agreed that they be relieved from taking part in the examination of these chapters respectively. Details of the first three members’ declarations are given in the Chairman’s opening remarks at the Committee’s public hearing on 8 December 2004, in *Appendix 5*. Details of Hon Albert Jinghan CHENG’s declaration are set out in the Committee’s Report on the chapter on “School administration of the English Schools Foundation”, on page 126.

II. Procedure

The Committee's Procedure The practice and procedure, as determined by the Committee in accordance with Rule 72 of the Rules of Procedure, are as follows:

- (a) the public officers called before the Committee in accordance with Rule 72 of the Rules of Procedure, shall normally be the Controlling Officers of the Heads of Revenue or Expenditure to which the Director of Audit has referred in his Report except where the matter under consideration affects more than one such Head or involves a question of policy or of principle in which case the relevant Director of Bureau of the Government or other appropriate officers shall be called. Appearance before the Committee shall be a personal responsibility of the public officer called and whilst he may be accompanied by members of his staff to assist him with points of detail, the responsibility for the information or the production of records or documents required by the Committee shall rest with him alone;
- (b) where any matter referred to in the Director of Audit's Report on the accounts of the Government relates to the affairs of an organisation subvented by the Government, the person normally required to appear before the Committee shall be the Controlling Officer of the vote from which the relevant subvention has been paid, but the Committee shall not preclude the calling of a representative of the subvented body concerned where it is considered that such a representative could assist the Committee in its deliberations;
- (c) the Director of Audit and the Secretary for Financial Services and the Treasury shall be called upon to assist the Committee when Controlling Officers or other persons are providing information or explanations to the Committee;
- (d) the Committee shall take evidence from any parties outside the civil service and the subvented sector before making reference to them in a report;
- (e) the Committee shall not normally make recommendations on a case on the basis solely of the Director of Audit's presentation;
- (f) the Committee shall not allow written submissions from Controlling Officers other than as an adjunct to their personal appearance before the Committee; and

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- (g) the Committee shall hold informal consultations with the Director of Audit from time to time, so that the Committee could suggest fruitful areas for value for money study by the Director of Audit.

2. **The Committee's Report** This Report by the Public Accounts Committee corresponds with the Reports of the Director of Audit on:

- the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 2004; and
- the results of value for money audits (Report No. 43),

which were tabled in the Legislative Council on 24 November 2004. Value for money audits are conducted in accordance with the guidelines and procedures set out in the Paper on Scope of Government Audit in the Hong Kong Special Administrative Region - 'Value for Money Audits' which was tabled in the Provisional Legislative Council on 11 February 1998. A copy of the Paper is attached in *Appendix 2*.

3. In addition, this Report takes stock of the progress of the action taken by the Administration on the recommendations made in the Committee's Report Nos. 40, 40A and 41 and offers the Committee's views on the action taken. These are detailed in Parts III to V of this Report.

4. **The Government's Response** The Government's response to the Committee's Report is contained in the Government Minute, which comments as appropriate on the Committee's conclusions and recommendations, indicates what action the Government proposes to take to rectify any irregularities which have been brought to notice by the Committee or by the Director of Audit and, if necessary, explains why it does not intend to take action. It is the Government's stated intention that the Government Minute should be laid on the table of the Legislative Council within three months of the laying of the Report of the Committee to which it relates.

**III. Report of the Public Accounts Committee
on Report No. 40 of the Director of Audit on the Results
of Value for Money Audits and Supplemental Report of the
Public Accounts Committee on Report No. 39 of the Director of Audit
on the Results of Value for Money Audits [P.A.C. Report No. 40]**

Laying of the Report Report No. 40 of the Director of Audit on the results of value for money audits was laid in the Legislative Council on 30 April 2003. The Committee's subsequent Report (Report No. 40) was tabled on 9 July 2003, thereby meeting the requirement of Rule 72 of the Rules of Procedure of the Legislative Council that the Report be tabled within three months of the Director of Audit's Report being laid.

2. **The Government Minute** The Government Minute in response to the Committee's Report No. 40 was laid in the Legislative Council on 15 October 2003. A progress report on matters outstanding in the Government Minute was issued on 23 October 2004. The latest position and the Committee's further comments on these matters are set out in paragraphs 3 and 4 below.

3. **Subvention for staff emoluments of The Legislative Council Commission** (Chapter 2 of Part IV of P.A.C. Report No. 40). The Committee was informed by the **Secretary General of the Legislative Council Secretariat**, in his letter of 26 November 2004 in *Appendix 3*, that:

- the Exchange of Letters (EoL) between the Administration and The Legislative Council Commission (LCC), which set out the general principles and guidelines governing the administrative arrangements for the LCC and its working relationship with the Administration, as well as the existing funding arrangements for the LCC, had been reviewed; and
- the EoL had been amended to reflect the updated funding arrangements since the last revision in 1997, such as the replacement of the baseline approach for funding by the Operating Expenditure Envelope approach. The revised EoL was signed by the LCC and the Administration in November 2004.

4. The Committee noted the above result of the review of the EoL between the Administration and the LCC.

IV. Supplemental Report of the Public Accounts Committee on Report No. 40 of the Director of Audit on the Results of Value for Money Audits [P.A.C. Report No. 40A]

Laying of the Report Report No. 40 of the Director of Audit on the results of value for money audits was laid in the Legislative Council on 30 April 2003. The Committee's supplemental report (Report No. 40A) on Chapters 8, 9 and 10 of the Director of Audit's Report was tabled on 19 November 2003.

2. **The Government Minute** The Government Minute in response to the Committee's Report No. 40A was laid in the Legislative Council on 3 March 2004. A progress report on matters outstanding in the Government Minute was issued on 23 October 2004. The latest position and the Committee's further comments on these matters are set out in paragraphs 3 to 8 below.

3. **University Grants Committee funded institutions - Governance, strategic planning and financial and performance reporting** (Chapter 1 of Part IV of P.A.C. Report No. 40A). The Committee was informed that:

Corporate governance of institutions

Review of the governance structure of the University of Hong Kong

- the University of Hong Kong (HKU) was carrying out in phases other measures, such as enhancing communications between the management and members of the HKU;

Amendment to the University of Hong Kong Ordinance regarding the statutory roles of the Council and Court of the University of Hong Kong

- the HKU had been working on amendments to the University of Hong Kong Ordinance so that the role of its Court would be more accurately defined and consistent with the HKU statutes in the Ordinance;

"Fitness for purpose" reviews of the governance structures of the other seven institutions

- the City University of Hong Kong (CityU) Council had established an Implementation Committee to follow up the CityU Review Committee's recommendations. According to the implementation plans approved by the CityU Council in March 2004, the various recommendations would be carried out in 2004 and 2005;

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- the Lingnan University (LU) Council completed a review of the membership and terms of reference of its standing committees in April 2004;
- The Chinese University of Hong Kong (CUHK) had implemented the recommendations stated in the interim report, including the establishment of an Executive Committee and an audit committee;
- the Task Force formed under The Hong Kong Institute of Education (HKIEd) Council completed the review of the HKIEd's governance structure in early 2004. The HKIEd had implemented the recommendation of the Task Force to streamline the structure of Council Committees by dissolving some Committees and subsuming some Sub-committees under other Committees;
- the Governance and Management Review Committee of The Hong Kong Polytechnic University (PolyU) completed its review of institutional governance and management structure in June 2004;

Membership, attendance and attendance records in relation to Council meetings

- the CityU Council had approved the recommendations of its Review Committee on University Governance and Management to downsize the CityU Council so that there would be a clear majority of lay members. The Council, in consultation with the Administration, had been examining the necessary legislative amendments to the City University of Hong Kong Ordinance to implement the recommendations;
- to involve the external members in more aspects of the work of the CityU, the CityU Council had approved the recommendation of restructuring its committees so that lay members would be in the majority. The recommendation had been implemented starting from the 2004-05 academic year;
- the CUHK Council decided in February 2004 to publish the information on the attendance of each Council member on the CUHK's website;
- the HKIEd Council decided in February 2004 that, in order to enhance transparency, each Council member's attendance record at the Council and Council Committee meetings would be uploaded onto the HKIEd's website on an annual basis;
- the PolyU published the attendance records of its Council members on the PolyU's website in September 2004;

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- The Hong Kong University of Science and Technology (HKUST) Council resolved at its meeting in May 2004 that there would not be a quorum at any Council meeting unless external members constituted a majority. This new rule had been implemented with effect from that meeting;
- the HKUST Council also agreed to publish the attendance records of Council members at Council meetings in the 2003-04 Annual Report of the HKUST;
- the HKU Council agreed in April 2004 that the record of attendance of Council members should be made public;

Proposal to set up an audit committee — City University of Hong Kong, Hong Kong Baptist University, The Chinese University of Hong Kong, and the University of Hong Kong

- the CUHK, the CityU and the HKU established their own audit committees in December 2003, March 2004 and April 2004 respectively;

Proposal to conduct periodic reviews of the effectiveness of governing bodies

- the Review Committee on University Governance and Management of the CityU submitted a Code of Practice to the CityU Council for consideration in July 2004. Aiming at enhancing the effectiveness of the Council, the Code of Practice covered responsibilities of Council members, conduct of Council business, governance framework and legal status of the CityU, as well as financial affairs and staffing matters;
- the HKIEd Council had completed its review of governance structure and concluded that any review of the effectiveness of its governing body would be conducted as and when necessary, and in the light of the development of/changes in the Institute as well as the Hong Kong higher education sector as a whole;
- the HKUST Council agreed in May 2004 that periodic reviews of the HKUST governing body (i.e. the Council itself) should be conducted as and when appropriate;
- the HKU Council had agreed to carry out reviews of its own effectiveness once every five years, with the framework of the first review to be determined in the 2004-05 academic year; and

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Performance reporting of institutions

Performance-based funding scheme for the 2005-06 to 2007-08 triennium

- the University Grants Committee (UGC) had established a Performance and Role-related Funding Scheme Assessment Panel to consider the self-assessment documents submitted by the UGC-funded institutions and to assess their performance against role. The Panel carried out an assessment exercise in August 2004, and sought to test and verify the conclusions made by the institutions. Evaluation was carried out according to criteria and benchmarks suggested by the institutions. The UGC had accepted the findings and conclusions made by the Panel and would feature this element in its 2005-06 to 2007-08 triennial funding recommendations to the Administration.

4. The Committee wishes to be kept informed of further development on the subject.

5. **University Grants Committee funded institutions — General administrative services** (Chapter 2 of Part IV of P.A.C. Report No. 40A). The Committee was informed that:

Provision of senior staff quarters

University Grants Committee Working Group on Housing Arrangement After Deregulation of University Salaries

- the Administration and the Secretary-General, University Grants Committee (UGC) were examining the joint proposal put forward by the UGC-funded institutions regarding the funding arrangements for staff housing benefits after the deregulation of university salaries. Subject to their deliberations, the proposal would be submitted to the Working Group on Housing Arrangement After Deregulation of University Salaries for consideration;

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Occupancy position of senior staff quarters in September 2004

- the occupancy position of senior staff quarters (SSQ) in UGC-funded institutions (except Lingnan University (LU) which did not have SSQ) was tabulated as follows:

Institution	Occupancy of senior staff quarters as at January 2004 (as reported in the Government Minute of March 2004)	Occupancy of senior staff quarters as at September 2004
City University of Hong Kong (CityU)	81%	88%
Hong Kong Baptist University (HKBU)	56%	70%
The Chinese University of Hong Kong (CUHK)	85%	88%
The Hong Kong Institute of Education (HKIEd)	95%	70%
The Hong Kong Polytechnic University (PolyU)	57%	70%
The Hong Kong University of Science and Technology (HKUST)	98%	96%
University of Hong Kong (HKU)	93%	96%

- after the implementation of positive measures to make beneficial use of vacant SSQ, the occupancy rate of SSQ in all institutions had increased, except for the HKUST which nonetheless maintained a high occupancy rate, and the HKIEd the vacant quarters of which were expected to be filled up by new recruits who would report for duty in the next few months;

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Actions taken by institutions to improve the vacancy position of senior staff quarters, and to address the rent-charging practices for senior staff quarters staff receiving Private Tenancy Allowance or Home Financing Allowance

- the Housing Working Group of the CityU had completed a comprehensive review which covered, among others, the housing stock and accommodation issues for staff, visitors and students. To maximise the usage of SSQ, the CityU planned to convert an entire block of its SSQ, i.e. the To Yuen Building (18 units), for office use in 2005. In addition, the CityU had successfully leased nine vacant units to non-CityU personnel since July 2004. The CityU would take into consideration the need to retain adequate units for accommodating eligible staff and lease surplus vacant quarters to reduce the vacancy position. The CityU would continue to charge market rents in leasing the vacant SSQ to its staff receiving Home Financing Allowance (HFA)/Private Tenancy Allowance (PTA);
- to optimise the use of existing quarters and improve their occupancy, the HKBU had made use of its SSQ as housing benefits for eligible staff. A total of six newly recruited staff were allocated staff quarters when they assumed duty in August and September 2004. In addition, the HKBU had made efforts to lease the vacant staff quarters to HKBU staff and in the open market. In the past few months, five units of the SSQ were leased out. The HKBU would continue to charge market rents in leasing the vacant staff quarters to HKBU staff and/or in the open market;
- the CUHK continued to implement measures to improve the vacancy situation of its SSQ. These included leasing SSQ to HFA and PTA recipients and other interested senior staff members; offering SSQ as the only form of housing benefit available to new staff appointed under the deregulated environment; and extending some SSQ units with relatively lower occupancy rate for lease by the retirees at market rent. As a result, the occupancy rate of SSQ increased from 85% in January 2004 to 88% in September 2004;
- regarding the CUHK's rent-charging practice, PTA recipients and other residents were charged at market rental level for occupancy of SSQ. As for HFA recipients, they were only allowed to rent vacant SSQ at market rates not exceeding 115% of their entitlements, and the rental to be paid would be the amount of their individual HFA entitlements, regardless of whether the market rents (subject to the above ceiling) were higher or lower than the HFA entitlements. This was to ensure that there was no major under-recovery of market rents in overall terms on the one hand, and to provide staff with more certainty over the rent payable and in turn to achieve a higher occupancy rate

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on the other hand. So far, the total rents collected based on HFA entitlements were no less than the total market rents for all SSQ involved;

- it was currently a standing arrangement for new appointees of the PolyU who were eligible for housing benefit to be provided with SSQ only if available. The number of vacant units dropped from 29 in early 2004 to 20 in September 2004. The PolyU would continue to charge HFA recipients occupying SSQ their maximum HFA entitlements (which were considered by a professional surveyor to be no less than the market rents);
- the HKIED offered SSQ as the only form of housing benefits to new staff recruited after 1 July 2003. Taking into account the estimated number of new recruits for the 2004-05 academic year, all vacant SSQ would be filled up in the next few months. The HKIED would continue to charge market rents in leasing the vacant SSQ to its staff receiving HFA/PTA;
- the HKUST had continued to actively engage property agents in leasing vacant SSQ. Around 40 units of SSQ were leased out at market rate by September 2004. As for the rent-charging practice for HFA recipients occupying SSQ, the occupants were charged their HFA rates. While in some cases the HFA rates were greater than the market rent and in some cases lower, the total sum of rental collected from all these occupants involved was no less than the total market rents to be fetched from these flats;
- the HKU had continued implementing positive measures to reduce the vacancy rate of SSQ such as conducting periodic review of rental levels of SSQ and actively engaging estate agents to lease out SSQ in the open market. These measures had proved to be successful and the occupancy rate of SSQ increased from 93% in January 2004 to around 96% by September 2004. The HKU would continue to charge market rents in leasing the vacant SSQ to its staff receiving HFA/PTA;

Task Force to ensure optimal use of the vacant senior staff quarters

- the Task Force under the chairmanship of the Secretary-General of UGC met in end April 2004 to discuss the occupancy position of SSQ and the related measures, and the rent-charging practices for HFA staff occupying SSQ. The Task Force requested the institutions to try their best to explore ways to ensure that the rents paid by HFA recipients reflected the market rates;

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- the Task Force was delighted to note that all institutions had implemented improvement measures to reduce the vacancy rate of SSQ. Institutions with relatively low occupancy rate of SSQ were requested to make reference to the experiences of sister institutions and to further carry out proactive measures to put vacant SSQs to gainful use. Institutions were also invited to consider the possibility of setting up a common pool of SSQ among themselves so that staff in one institution could apply and live in vacant staff quarters of another institution if they so wished. The Task Force would continue to monitor the occupancy position of SSQ;

Provision of junior staff quarters

Reviews by the institutions on the operational need for junior staff quarters

- the CityU had reviewed the operational need for junior staff quarters (JSQ) and concluded that, out of its nine JSQ, seven were occupied by essential staff to meet operational need and the remaining two had been leased out on a short-term basis to visiting staff and/or research fellows. The CityU's Housing Working Group would periodically review the matter;
- while there was no vacant JSQ in September 2004, the LU was nonetheless conducting a review on the operational need of JSQ, which was planned for completion by the end of 2004. The LU expected that the majority of the JSQ would be phased out by June 2005 and would be converted into units suitable for occupation by visiting lecturers or staff eligible for housing benefits;
- the CUHK had suspended the allocation of JSQ to its staff members to pave the way for alternative use or redevelopment of JSQ, details of which would be considered together with the master development plan of the CUHK. A JSQ Working Group had been set up for this purpose, and it was expected to give a clearer direction by June 2005;
- the HKIEd had set up a working group to closely monitor the operational need for JSQ. There were six vacant JSQ out of a total of 26 by September 2004. As there was shortage of office space, the HKIEd would explore the possibility of converting vacant JSQ into office use and for non-UGC-funded projects/activities, etc. and levy appropriate charges;

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- regarding the HKUST, out of a total of 158 JSQ, 97 units were allocated to staff based on operational need. For the remaining 61 units, 57 were released in September 2004, including 45 allocated to research staff and 12 leased out in the open market. The overall occupancy rate for the JSQ was thus 97%. The HKUST would continue to monitor the situation to ensure a high occupancy rate of JSQ;
- apart from reserving JSQ for staff to live in or near the main campus for discharging duties related to security, safety, emergency maintenance, etc., the HKU continued to re-model JSQ for use by students and visiting scholars. Out of a total of 165 JSQ, the number of JSQ designated for occupancy by students and visiting scholars increased from 75 in December 2003 to 84 by September 2004;

Provision of guest quarters

Institutions to improve the vacancy position of guest quarters

- the CityU continued to promote guest quarters (GQ) occupancy. The average occupancy rate for the first half of 2004 was 80%;
- the number of the HKBU's GQ units had been reduced from 20 to 18 since 1 July 2004. By September 2004, around half of the GQ units were occupied. In the event that the demand for staff quarter increased and there were still vacancies in GQ, more units of GQ would be converted into staff quarters for occupation;
- four of the LU's GQ were renovated in mid-July 2004 to become two larger quarters for occupation by visiting lecturers and staff eligible for housing benefits. The LU intended to convert some more GQ units into staff quarters by July 2005;
- through promotion efforts to departments/units, the occupancy rate of the CUHK's GQ during the summer vacation in 2004 stayed at around 70%. The occupancy rate might pick up after the regular term commenced;
- the average occupancy rate of the HKIEd's GQ in the 2004-05 academic year would be around 52% after excluding some GQ which would likely be converted into SSQ. To improve GQ occupancy, the HKIEd had started leasing them to staff, alumni and students at appropriate charges for short-term stay;

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- with continual efforts of monitoring and promotion, such as on-going collection of customer feedback, frequent review of pricing strategy and regular distribution of publicity materials to departments, the occupancy of the PolyU's GQ had been satisfactory. The average occupancy rate was 92% in July 2004 and stayed at over 80% in August and September 2004;
- the occupancy rate of the HKUST's GQ was 85% by September 2004. The HKUST undertook to monitor its occupancy position on an on-going basis;
- the HKU commenced a substantial renovation project of its GQ (the Robert Black College) in December 2003 to enhance its marketability. Two-thirds of the works had been completed, with the remaining works to be finished by October 2004. Since the College had to be partially closed during the renovation period, the occupancy of GQ was expected to improve after completion of works;

Student hostels

Institutions to improve the vacancy position of student hostels

- the CityU's student hostels continued to enjoy a high occupancy level at an average of 99% during term-time of the 2003-04 academic year and 85% during summer vacation in 2004. With a view to enhancing the occupancy rate during vacation time, the CityU had vigorously promoted summer letting and collaborated programmes with external organisations, internal departments, student organisations, community groups, alumni and short-stay visitors. A flexible weekly rental scheme had been designed to attract more students to stay in student hostels during the summer vacation. With the continued efforts of the CityU to promote hostel residence, its occupancy rate was 90% in September 2004;
- the HKBU had made increasing efforts to promote the value of hall life education among undergraduate students since May 2003. It had also conducted special promotion campaigns to attract associate degree and full-time taught postgraduate students. Non-teaching visiting research scholars, students of the CityU not provided with hall places and short-term exchange research students had also been accommodated in hostels to increase their occupancy rates. With the continued efforts of the HKBU to promote hostel residence, the occupancy rate would be close to 100% at the beginning of the 2004-05 academic year;

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- the LU had undertaken various measures to promote occupancy of student hostels. The LU had, for instance, speeded up maintenance works of student hostels during the summer break so that hostel rooms could be made available for occupation at the start of the new term. The student hostels were fully occupied in September 2004;
- the CUHK's undergraduate student hostels were fully occupied in September 2004. The occupancy rate of graduate student hostels during the summer of 2004 was 85%, and reached 95% by September 2004;
- the HKIEd continued to take positive measures to improve the occupancy position of student hostels, such as extending hostel residence to parents of non-local students, participants of professional training programmes organised by the HKIEd, associate degree students, etc. Moreover, strategic marketing efforts would be made to let out student hostels to schools and corporations for summer camps or staff functions during vacation. With the continued efforts of the HKIEd to promote hostel residence, the occupancy rate was about 70% in September 2004;
- the extensive publicity and promotion, various hall functions and schemes (e.g. the Hall Resident Service Award Scheme and the Hall Education Through Campus Work Scheme) organised by the PolyU had been fruitful. The average occupancy rate of the student hostels during term time in the 2003-04 academic year was 87%, which was 21 percentage points higher than the average occupancy rate of 66% of the previous year. The occupancy rate for September 2004 was even higher at over 95%;
- the occupancy rate of student hostels in the HKUST remained at 99% during semester time by September 2004. The HKUST would try to maintain this high occupancy rate;
- the HKU's Report on Hall Education, which aimed at re-examining and re-appraising the philosophy of hostel education, was approved by its Senate in February 2004. The Report had set the framework for future direction of hall education;
- as a result of positive measures undertaken by the HKU to boost occupancy of its hostels, the average occupancy rate of student hostels was around 98% in September 2004;

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- to further promote hostel occupancy, the HKU implemented the following measures for summer letting in the 2003-04 academic year:
 - (a) all current students and non-residents were invited to apply for summer residence in March 2004;
 - (b) the Office of Student Affairs coordinated commercial letting for local and overseas individual visitors, and academic/cultural programmes in summer 2004, and had begun accepting advance bookings by groups since early 2004; and
 - (c) departments were encouraged to organise summer hall programmes for students who were not residents during the residential year, and to introduce special programmes for students from the Mainland, overseas universities and local secondary schools to reside in halls;

Review of the existing policy on students' grants and loans

- the Administration constantly reviewed its policy on students' grants and loans, taking into account new developments in the sector and comments from relevant parties. The advisory committee that advised the Administration on the operation of the Local Student Finance Scheme had, based on the findings of a student expenditure survey, put forward a number of recommendations to improve the types and levels of grants and loans for needy students, including the recommendation to provide needy students with an accommodation expenses loan so as to enable them to live in student hostels. The Administration was examining these recommendations and would come to a view soon; and

Outsourcing of institutions' services

Institutions to widen the scope for outsourcing their services

- all institutions had taken measures to outsource their services as appropriate and would continue to look for such opportunities in future.

6. The Committee wishes to be kept informed of further development on the subject.

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7. **University Grants Committee funded institutions — Staff remuneration packages and stipends** (Chapter 3 of Part IV of P.A.C. Report No. 40A). The Committee was informed that:

Pay structure

Institutions' reviews of their pay structure

- the City University of Hong Kong (CityU) Council approved the adoption of a new set of salary scales and pay rise system with effect from 1 July 2004. The main features were as follows:
 - (a) the new salary scales were applicable to new appointees of both academic and non-academic staff who were offered appointment on or after 1 July 2004. The new appointees would receive reduced starting and maximum salaries. Moreover, the salary scales for each grade of staff would cover a range of fixed incremental steps. Increments would not be given automatically but would be subject to the new pay rise system. Serving staff would remain on existing salary scales of their respective grades and the existing salary scales should apply in case of promotion; and
 - (b) the new pay rise system was applicable to both serving staff and new staff appointed on superannuable or gratuity-bearing contract terms. Each year, the CityU's Budget Committee would decide whether a pay rise exercise should be conducted for that particular year, having regard to the budgetary situation of the CityU. A pay rise in the form of increment along the salary scale might be given to staff whose current salary was within the salary range, subject to the performance of the staff concerned;
- the Hong Kong Baptist University (HKBU) Council approved in June 2004 a new pay and reward structure for both academic/teaching and non-teaching staff, which was being implemented in stages with effect from 1 July 2004. The main features of the new pay and reward structure included:
 - (a) rationalised and streamlined pay structures for academic/teaching and non-teaching staff on the basis of internal equity of different job requirements and external comparability with the pay levels of comparable jobs in the market;

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- (b) replacement of the current system of fixed amount of annual salary increment by a more flexible salary adjustment mechanism based on staff performance subject to the financial situation of the HKBU, changes in market pay levels and cost-of-living adjustment; and
- (c) establishment of a performance management system which would be linked to salary increase and reward/recognition of staff performance; and introduction of one-off and more flexible award/special allowance as means of reward/recognition of staff performance and/or special contribution to the HKBU;

In recognition of the need to strike a balance between achieving the overall objective of the new structure and addressing staff concerns, the new pay and reward structure was applicable to newly-appointed staff, i.e. those appointed on or after 1 July 2004 for teaching staff and on or after 1 January 2005 for non-teaching staff. As for serving staff, the new pay and reward structure would start to apply to teaching staff and non-teaching staff on 1 July 2005 and 1 January 2006 respectively;

- Lingnan University (LU) implemented a new set of rank and salary structures in October 2003 for application to new appointees and to serving staff upon promotion. The academic rank structure was rationalised and simplified to map out a clear career path for academic staff, and the ranks and salary scales of all non-academic posts were updated and attuned to reflect more accurately the level of responsibilities;
- The Chinese University of Hong Kong (CUHK) introduced revised pay levels for its non-teaching grades in March 2004. The pay adjustment was applicable to new recruits appointed on or after 1 March 2004, and to serving staff upon movements (e.g. contract renewal, re-appointment to a different post/department, conversion to regular terms and promotion). The pay levels for teaching staff would continue to be subject to a salary administration system introduced since July 2003;
- The Hong Kong Institute of Education (HKIEd) had commissioned a consultancy to evaluate the duties of its non-teaching position and to benchmark their salaries with the market. The Institute was also reviewing the pay structure of teaching positions, drawing reference to similar pay structures locally and in overseas. It was expected that the review recommendations would be submitted to the HKIEd Council for consideration within the 2004-05 academic year;

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- The Hong Kong Polytechnic University (PolyU) implemented a new pay and compensation package which was applicable to new employees appointed from 1 April 2004 onwards. Features of the new package included:
 - (a) remunerating new employees on their respective salary ranges according to their job bands under a broad-banding system. Salary ranges were drawn up with reference to salaries in the relevant market segments; and
 - (b) abandoning the “automatic” granting of annual salary increment. Salary adjustment, if any, would be determined after an across-the-board salary review for all staff and would be based on considerations that included, but were not limited to, the outcome of the periodical performance review of individual staff, their respective salary levels within the salary range, the financial situation of the PolyU, prevailing pay trends in the relevant market segment, etc;
- The Hong Kong University of Science and Technology (HKUST) had established a Working Group to oversee the review of the grading and salary structure for non-academic staff. The review was scheduled for completion by 2005;
- the University of Hong Kong (HKU) Council had been examining the recommendations of the review of pay structure for academic staff. A Sub-Group on Non-Academic Staff Salaries had commenced its review, and aimed to submit the recommendations to the HKU Council during the 2004-05 academic year;

Disclosure guidelines on the remuneration of senior staff of institutions

- the University Grants Committee (UGC) issued guidelines in December 2003 requiring institutions to disclose in their financial statements the number of higher paid staff whose total annual remuneration exceeded \$1.8 million irrespective of the funding sources, to enhance the transparency and accountability of the institutions;

Institutions to enhance the transparency and accountability in the application of non-public funds

- the receipt and use of non-public funds, including those obtained from non-public sources, were accounted for in the financial statements of the institutions. The financial management, including budgeting and

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performance review, of activities funded by non-public sources was also subject to monitoring by the University Councils and their committees;

Review of the future role and functions of the Universities Joint Salaries Committee

- with the deregulation of salary in the UGC sector, members of the Heads of Universities Committee (HUCOM) agreed in April 2004 to dissolve the Universities Joint Salaries Committee (UJSC);

The Hong Kong Polytechnic University's review on the effect of section 9(3)(c) of The Hong Kong Polytechnic University Ordinance and its proper application

- the Governance and Management Review Committee of the PolyU had reviewed the Hong Kong Polytechnic University Ordinance and would submit its review report covering its recommendations on various sections of the Ordinance, including section 9(3)(c), to the PolyU Council for consideration before the end of 2004;

Provision of resources to The Hong Kong Institute of Education

- in recognition of the HKIED's initial development needs, additional funding support was given to the HKIED during its early years of establishment and the HKIED was exempted from the 10% unit cost reduction applicable to other UGC-funded institutions in the 1998/99 - 2000/01 triennium. Other than providing additional support in the initial years, the UGC had been adopting a funding mechanism which ensured that the HKIED was able to compete with other UGC-funded institutions on an equal footing. It had been an ongoing commitment of the UGC to ensure a fair and level playing ground in terms of allocation of funds to UGC-funded institutions;

Administration of leave

Institutions to address the problems associated with the excessive leave entitlements and the encashment of leave

- the CityU had sent periodical reminders to its various departments to clear staff's accumulated leave. Forfeiture of leave days not yet taken by the clearance deadline for existing staff, and reduced leave provisions for new staff, had also been strictly enforced;

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- under the newly approved pay and reward structure endorsed by the HKBU Council in June 2004, the following new measures, which were applicable to new staff, had been introduced to guard against excessive leave accumulation and leave encashment on leaving the service of the HKBU:
 - (a) staff were encouraged to take leave on an annual basis;
 - (b) only half of the annual leave entitlement might be carried forward to the following 12-month period in general; and
 - (c) payment of outstanding leave on leaving the service of the HKBU was confined to a period, which varied from not more than two calendar weeks to one calendar month for different staff grades;
- the leave arrangements for both academic and non-academic staff of the LU had been effectively administered and monitored under the established leave management scheme. For academic staff, those on the old leave terms were given 49 days of annual leave for both vacation and research purposes, and those on new leave terms were given a much reduced annual leave entitlement. Half of the annual leave provided to all academic staff should be taken during the summer breaks. Their unused leave would be forfeited upon termination of contract/employment. As for non-academic staff, those on old leave terms could accumulate leave up to 67 working days while those on revised terms could accumulate two years' entitlement. All unused annual leave in excess would be forfeited without compensation. These measures had effectively kept the accumulation of unused leave at a reasonable level;
- the CUHK continued to adopt the leave arrangement of migrating serving staff with long leave entitlements (i.e. those in service before 2002) to the Annual Leave Scheme 2002 on re-appointment/renewal of contract. The CUHK had introduced measures whereby other serving appointees would also migrate to this Annual Leave Scheme on re-appointment/renewal of contract. New recruits would also be provided with annual leave under the Annual Leave Scheme 2002;
- under the review of the pay structure, the HKIEd had commissioned a consultancy to review the contractual benefits for all staff, including vacation leave entitlement. Recommendation in this respect, together with others, would be submitted to the HKIEd Council for consideration within the 2004-05 academic year;

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- with the implementation of the new terms of service on 1 April 2004, new appointees of the PolyU were provided with leave provisions at levels comparable to those as provided in the labour market. The annual leave entitlements were 22 working days for academic, management and senior professional staff; 18 working days for executive and professional staff; and 14 working days for general staff. The maximum leave accumulation had been reduced from two years' entitlement to that of one year;
- the HKUST's policy of leave encashment had discontinued. Since September 2001, staff could only carry forward, from one year to the next, not more than 14 days of their annual leave. No payment would be made in respect of any untaken leave except on cessation of employment;
- the HKU's current review of non-academic staff salaries would address the problem of excessive leave entitlement in the long term. The review was expected to be completed in early 2005; and

Stipends for research postgraduate students

Institutions to improve the administration of stipends

- to improve the administration of research postgraduate stipends, the HUCOM agreed that the Postgraduate Administrators' Circle (PGAC) should be given the authority to approve a common band of stipend rates which allowed for deviations within a certain range for the HUCOM member institutions to follow. By doing so, it could uphold institutional autonomy on one hand, and avoid unhealthy competition on the other. Under the approved arrangement, the PGAC was required to provide an annual report to the HUCOM on the agreed stipend rate.

8. The Committee wishes to be kept informed of further development on the subject.

**V. Report of the Public Accounts Committee on the Reports
of the Director of Audit on the Accounts of the Government of the Hong Kong
Special Administrative Region for the year ended 31 March 2003 and the Results
of Value for Money Audits (Report No. 41) [P.A.C. Report No. 41]**

Laying of the Report The Report of the Director of Audit on the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 2003 and his Report No. 41 on the results of value for money audits were laid in the Legislative Council on 26 November 2003. The Committee's subsequent Report (Report No. 41) was tabled on 25 February 2004, thereby meeting the requirement of Rule 72 of the Rules of Procedure of the Legislative Council that the Report be tabled within three months of the Director of Audit's Report being laid.

2. **The Government Minute** The Government Minute in response to the Committee's Report No. 41 was laid in the Legislative Council on 19 May 2004. A progress report on matters outstanding in the Government Minute was issued on 23 October 2004. The latest position and the Committee's further comments on these matters are set out in paragraphs 3 to 48 below.

3. **Financial performance of the Post Office** (paragraphs 7 to 8 of Part III of P.A.C. Report No. 41). The Committee was informed that the Post Office (PO), together with the Economic Development and Labour Bureau and the Financial Services and the Treasury Bureau, continued to examine critically the challenges to the PO's operation as identified by the Committee. Apart from the PO's financial performance and operation as a trading fund, the studies had covered issues relating to the postal services market, including global developments and overseas experience. In view of the complexity of the many issues involved, more detailed studies on these were being undertaken.

4. The Committee wishes to be kept informed of the results of the comprehensive review of postal policy and services.

5. **Provision of slaughtering facilities for supplying fresh meat** (paragraphs 3 to 4 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

- the consultancy firm engaged by the Food and Environmental Hygiene Department (FEHD) to forecast the slaughtering throughput of livestock in the territory up to the year 2007 had completed its assignment. The forecasting period covered by the consultancy was originally up to 2010. It was shortened to 2007 to increase the reliability of the statistical analysis;

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- the study showed decreasing trends in the average consumption of fresh pork and fresh beef per person, which would reduce the daily number of pigs and cattle to be slaughtered in the coming few years. The study further revealed that it would be premature to propose centralising the slaughtering operation of livestock at the Sheung Shui Slaughterhouse (SSSH) unless the technical feasibility of increasing pig slaughtering throughput of the SSSH had been examined. The FEHD reported the details of the study and the findings to the Legislative Council Panel on Food Safety and Environmental Hygiene on 29 June 2004; and
- the Architectural Services Department (Arch SD) was examining the outcome of the study to ascertain whether it was technically feasible to centralise the slaughtering operation of livestock at the SSSH. The FEHD would consider the findings of the Arch SD and other factors before making recommendations on the way forward.

6. The Committee wishes to be kept informed of the progress made by the Arch SD in ascertaining the feasibility of centralising the slaughtering operating of livestock at the SSSH and the FEHD's recommendations on the way forward.

7. **Services provided by the Official Receiver's Office** (paragraphs 5 to 7 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Guidelines on liquidators' remuneration

- a set of guidelines on liquidators' remuneration for private insolvency practitioners (PIPs) drawn up jointly by the Official Receiver's Office (ORO) and the former Hong Kong Society of Accountants (now known as the Hong Kong Institute of Certified Public Accountants) had been submitted to the company judge for comments. The judge had expressed her initial views on the matter during a talk she gave to the Insolvency Interest Group of the HKSA in July 2003. The views were noted by PIPs who would have to take them into account when they submitted their applications for remuneration to the court in the future;
- furthermore, the High Court had taken into account certain parts of the guidelines and, on 3 May 2004, implemented two procedural guides concerning the taxation of bills for PIPs and the ORO to follow; and

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Consultancy study and fees of the Official Receiver's Office

- the question of fees and cost recovery rates would be reviewed after the enactment of the Bankruptcy (Amendment) Bill, which would be re-introduced into the Legislative Council (LegCo) in the 2004-05 session. The earlier Bankruptcy (Amendment) Bill 2003 introduced into the LegCo on 10 December 2003 had lapsed as no Bills Committee slot could be assigned. Other recommendations of the consultancy study including the proposed "cab rank" system and licensing of PIPs were being further considered.

8. The Committee wishes to be kept informed of further developments on the subject including the other recommendations of the consultancy study and the issues of fees and cost recovery rates in relation to insolvency cases.

9. **Recoverability of the outstanding advances to the United Nations High Commissioner for Refugees** (paragraphs 17 to 18 of Part IV of P.A.C. Report No. 41). The Committee was informed that through meetings and written correspondence, the Administration had continued to urge the United Nations High Commissioner for Refugees (UNHCR) to make renewed efforts to look for donations from other countries with a view to settling the outstanding advances, which remained at \$1,162 million. The Administration had also reiterated that Hong Kong community at large still expected recovery of the outstanding advances. The Administration would continue to pursue repayment of the outstanding advances.

10. The Committee wishes to be kept informed of the action taken by the Administration in pressing the UNHCR to repay as soon as possible the outstanding advances to the Government of the Hong Kong Special Administrative Region.

11. **Footbridge connections between five commercial buildings in the Central District** (paragraphs 19 to 22 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

- the proposed footbridge column for supporting a link between Building II (i.e. Entertainment Building) and the southeast corner of Building I (i.e. Aon China Building) would affect the proposed station entrances of the Shatin to Central Link (SCL) of the Kowloon-Canton Railway Corporation (KCRC). The KCRC had thus raised objection to the footbridge proposal when consulted. Before the proposal for the SCL project was finalised, it would not be appropriate to proceed further with the footbridge proposal; and

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- the KCRC and the MTR Corporation Limited submitted a joint report on the proposed merger to the Government on 16 September 2004. The report also covered a review of the SCL scheme. The Administration would keep in view the review of the SCL project and would assess its impact on the footbridge connection requirement.

12. The Committee wishes to be kept informed of the Administration's assessment on the impact of the SCL project on the footbridge connection requirement.

13. **The use of energy-efficient air-conditioning systems in Hong Kong** (paragraphs 23 to 24 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

- the consultancy study for the implementation of water-cooled air-conditioning system (WACS) in Wanchai and Causeway Bay was substantially completed and the final report was expected to be due within 2004. A District Cooling System (DCS) in Wanchai North Waterfront by adopting a Build, Operate and Transfer form of contract was considered commercially viable and was recommended for implementation. The Electrical and Mechanical Services Department (EMSD) conducted a forum on 26 July 2004 to introduce and promote the DCS in Wanchai North Waterfront to the relevant building owners and their management agents;
- the South East Kowloon Development (SEKD) was still undergoing a comprehensive planning and engineering review. As the eventual reclamation plan for the SEKD would affect the siting of the DCS facilities and the commercial viability of the DCS project, the EMSD would need to review the feasibility of the DCS project having regard to the ultimate revision of reclamation plan for the SEKD;
- follow-up action on the salient points recommended by the study for the territory-wide implementation of WACS in Hong Kong had been taken, including lifting the restriction of using fresh water cooling towers in more areas where the fresh supply was adequate. The EMSD would publish a code of practice for WACS in 2005. The drafting of the code of practice had just commenced in September 2004 for planned publication in November 2005;

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- the EMSD had introduced a pilot scheme in 2000 to allow the use of fresh water in evaporative cooling to improve the energy efficiency of the air-conditioning systems of non-domestic buildings. The Administration had further expanded the scheme to cover 57 areas in May 2004. The Administration had received 107 applications and 62 of them had been approved in principle, covering about 2.1 million square metres of floor area. The estimated annual savings in electricity would be about 25 million kilowatt-hours. Eleven installations had been completed and commissioned;
- the EMSD had commenced the last phase of inspection programme of cooling towers with 450 towers inspected up to end September 2004. It was anticipated that about 1,000 cooling towers would be inspected by March 2005; and
- the Buildings Department (BD) had continued with the large-scale clearance exercise to remove potentially dangerous external unauthorised building works, including cooling tower supporting structures. It was estimated that more than 400 problematic cooling tower supporting structures were to be removed from commercial and industrial buildings in 2004. This included the 200 unauthorised structures supporting cooling towers in an unhygienic condition additionally removed in 2004 after the outbreak of the Severe Acute Respiratory Syndrome in 2003. The BD was pursuing prosecution action against defaulters for non-compliance of removal orders.

14. The Committee wishes to be kept informed of further development on the subject.

15. **Administration of allowances in the civil service** (paragraphs 25 to 26 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Job-related allowances for civilian grades

- the Administration had completed two phases of the review of Job-related allowances (JRAs) for civilian grades. Payment of the allowances had been rationalised, resulting in estimated annual savings of around \$20.5 million (or 33% of the estimated annual expenditure of around \$62 million on the concerned allowances). The third phase review would take into account the implementation of various initiatives in improving public health and hygiene since the outbreak of the Severe Acute Respiratory Syndrome;

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- the Administration would continue to have regard to all relevant factors, including the governing principles of JRAs, the original justifications for the allowances in question, present-day circumstances, prudence in the use of public expenditure, departmental management's review recommendations and feedback obtained from the staff consultation conducted by departmental management, in reviewing the allowances; and

Job-related allowances for disciplined services grades

- the Administration had introduced a review and monitoring mechanism for the payment of JRAs in the disciplined services similar to that applicable to the civilian grades. In other words, all Heads of Department of disciplined services were required to review each individual JRA under their purview and submit their review recommendations to the Civil Service Bureau for approval on a time-limited basis, subject to further review and re-approval by the end of the specified validity period. The first review under this new review mechanism was under way. The Administration aimed to complete the review within 2004.

16. The Committee wishes to be kept informed of further development on the subject.

17. **Water purchased from Guangdong Province** (paragraphs 27 to 28 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Further efforts to incorporate more favourable terms in future water supply agreements, including more flexibility in the supply arrangements

- the Guangdong Authority had continued with the flexible water supply arrangements. During the first half of 2004, the Administration had achieved some savings of pumping costs through reduced delivery of Dongjiang water to impounding reservoirs. However, having regard to the drought yield condition, as evidenced by the fact that the actual amount of rainwater collected by Hong Kong's reservoirs from 1 January to 16 August 2004 was only about 30.6% of the long-term average for that period, the Administration had started to recoup part of the unsupplied quantities; and
- the Administration would continue to negotiate with the Guangdong Authority for more favourable terms in future water supply agreements, including more flexibility in the supply arrangements to suit Hong Kong's needs.

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18. The Committee notes that under the current water supply agreements, the annual supply quantities are fixed up to end of 2004. The supply quantities beyond 2004 are subject to further negotiation. The Committee wishes to be kept informed of the Administration's further efforts to incorporate more favourable terms in future water supply agreements, including more flexibility in the supply arrangements.

19. **Interdiction of government officers** (paragraphs 29 to 30 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Review of the disciplinary procedures practised in the Hong Kong Police Force

- the working group to review the discipline system of the Hong Kong Police Force (Police Force) had examined the short, medium and long-term improvements to the system and the Police Force management was considering these recommendations. The short-term recommendations that involved changes in administrative procedures would most likely be implemented in 2005 while the medium and long-term recommendations, which would require legislative amendments, were being examined in more detail; and

Stoppage of salary on the date of conviction

- the Administration was reviewing the issue of amending section 37(4) of the Police Force Ordinance to stop payment of the salary of an interdicted officer with effect from the date of conviction (as opposed to the following day).

20. The Committee wishes to be kept informed of further development on the subject.

21. **Provision of legal aid services** (paragraphs 37 to 38 of Part IV of P.A.C. Report No. 41). The Committee was informed that the Administration was considering the feasibility and effectiveness of launching a pilot scheme on mediation for legally aided cases, and would examine the parameters, time frame, and resource requirements for such a pilot scheme.

22. The Committee wishes to be kept informed of the viability of launching the above pilot scheme.

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23. **Residential services for the elderly** (paragraphs 39 to 40 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Developing an accreditation system for residential care services for elders

- in June 2004, the Hong Kong Association of Gerontology (HKAG) submitted to the Social Welfare Department (SWD) a report on the pilot project on the development and establishment of an accreditation system for residential care services for elders in Hong Kong. The report recommended the setting up of a voluntary accreditation system to be operated by a non-statutory independent body based on the principles of peer review and continuous service improvement. The recommendations were presented to the Elderly Commission (EC) and the Legislative Council Panel on Welfare Services in June and July 2004 respectively. Both the EC and the Panel supported the HKAG's proposals in general. The Health, Welfare and Food Bureau and the SWD were considering the HKAG's recommendations, taking into account comments from the EC, the Panel and other relevant parties; and

Implementing work plan on provision of subsidised long-term care services and actions taken to address the problem of allocation of resources between the Hospital Authority and the Social Welfare Department regarding the provision of infirmary care

- the SWD expected that about 200 subsidised infirmary places would be provided under the scheme of providing infirmary places for medically stable elders in a non-hospital setting in the initial stage.

24. The Committee wishes to be kept informed of further development on the subject.

25. **The Customs and Excise Department's efforts to protect government revenue from dutiable commodities** (paragraphs 41 to 42 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Implementation of the Open Bond System

- in September 2004, the Customs and Excise Department (C&ED) completed the second post-implementation review on the Open Bond System (OBS). So far, no fraud or major deficiency under the OBS had been detected;

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Customs audits of oil companies

- in April 2004, the C&ED started a pilot scheme with an oil company to develop a prototype audit programme using the system-based approach (SBA) model. Upon completion of the scheme in October 2004, the C&ED would review its effectiveness and the practicability of applying the SBA model to other oil companies; and

Trial Scheme of “Red and Green Channels”

- the C&ED would conduct a trial scheme of “Red and Green Channels” in the first quarter of 2005 at all control points including the Airport. This should help the C&ED further strengthen its capability to prevent and detect abuses of duty-free concessions by incoming travellers.

26. The Committee wishes to be kept informed of the progress made by the C&ED in adopting the SBA in customs audits of oil companies and conducting the trial scheme of “Red and Green Channels”.

27. **Special Finance Scheme for small and medium enterprises** (paragraphs 43 to 44 of Part IV of P.A.C. Report No. 41). The Committee was informed that the Treasury was processing claims for compensation with the assistance of the Department of Justice and the Hong Kong Monetary Authority as necessary. So far, 1,159 claims involving a total of \$322 million had been settled. Another 255 claims involving a total of \$25 million had been suspended for processing as requested by the participating lending institutions in view of active repayment by the borrowers. The remaining 241 cases, involving a total of \$43 million and quite a lot of supporting documents or clarifications being outstanding, were still being processed.

28. The Committee wishes to be kept informed of further progress on the subject.

29. **Small house grants in the New Territories** (paragraphs 45 to 47 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Implementation of the Small House Policy

- deliberations had continued on the various issues relating to the Small House Policy. The Administration was working towards the target of identifying options for further consultation with stakeholders;

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- regarding the discussion with the Heung Yee Kuk (HYK) on the proposed across-the-board three-year moratorium on assignment of small houses, the HYK's stance of opposing any moratorium remained unchanged. The Administration would continue the discussion with the HYK on the way forward;

Checking of Indigenous Villager Status

- following the suspension at the end of April 2004 of the new procedures for checking an applicant's indigenous villager status, the Lands Department (Lands D) had engaged the HYK in further discussion on the matter. The HYK had disputed the need for any revised procedures for checking an applicant's indigenous villager status. It considered that certification of a person's indigenous villager status was a function of Indigenous Inhabitant Representatives elected under the Village Representative Election Ordinance (Cap. 576). The Lands D would continue to discuss with the HYK with a view to implementing the revised procedures at the earliest opportunity; and

Processing of small house grant applications

- along with the above checking procedures, implementation of the new and streamlined processing procedures for new applications for small house grants had also been suspended. Accordingly, the revised performance pledge for 2004 had not been publicised. It remained the Lands D's intention that once the discussion with the HYK on the revised procedures for verifying the indigenous villager status of small house applicants had been concluded, the revised processing procedures would be put into practice without further delay.

30. The Committee wishes to be kept informed of the progress of the various courses of action taken by the Administration.

31. **Primary education — Planning and provision of primary school places** (paragraphs 48 to 49 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Progress of the study on small class teaching

- in May 2004, the Education and Manpower Bureau (EMB) invited all public-sector primary schools to apply for participation in the Study on Small

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Class Teaching starting from the 2004-05 school year. The applications were considered by the Steering Committee for this Study, comprising academics, front-line educators and EMB representatives. Schools were informed of the selection result in mid-July 2004. The Study had commenced since September 2004, and was expected to be completed by 2007; and

Progress made by the Education and Manpower Bureau in phasing out rural schools

- a parent of a rural school had lodged an application for judicial review to the High Court regarding the EMB's decision to cease providing grants to the school with effect from 1 September 2004. The application had been dismissed by the Court. In the 2004-05 school year, there were 66 rural schools in operation. Of these rural schools, 40 did not have any Primary One class. Schools without Primary One class were expected to be phased out gradually.

32. The Committee wishes to be kept informed of:

- the progress of the study on small class teaching; and
- the progress made by the EMB in phasing out rural schools.

33. **Primary education — The administration of primary schools** (paragraphs 50 to 51 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Strategic planning and financial management

Fundamental review of grants to schools (including review of the level of surplus funds of the Operating Expenses Block Grant for aided schools and the Subject and Curriculum Block Grant for government schools and measures taken to help schools plan the optimum use of the surplus funds)

- to ensure more effective use of public funds, the Education and Manpower Bureau (EMB) was conducting a review on the existing recurrent non-salary grants provided to government and aided schools (including the Operating Expenses Block Grant (OEBG)/Subject and Curriculum Block Grant (SCBG) constituent grants and the policy of allowing schools to retain a surplus of up to 12 months' provision of the OEBG/SCBG) with a view to streamlining the

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deployment of grants and devolving greater funding flexibility to schools. The EMB would come up with proposals for consultation with the school sector as well as the Legislative Council (LegCo) in the 2004-05 school year;

Strategic planning and self-evaluation of schools

- the four-year cycle of the phase-in approach of external school review (ESR) for validating school self-evaluation and supporting schools' strategic development planning had commenced in February 2004. The EMB had successfully achieved the target by conducting ESR on 106 primary, secondary and special schools in the 2003-04 school year. The target for the 2004-05 school year was 150 primary, secondary and special schools. The first four-year cycle would be completed in the 2006-07 school year;

Use of information technology equipment in schools

- following a two-month public consultation, the EMB issued a policy document entitled "Empowering Learning and Teaching with Information Technology" on 29 July 2004. The document set out the next information technology (IT) in education strategy which sought further integration of IT into the learning and teaching process. The new strategy had the following seven specific goals and would be implemented starting from the 2004-05 school year:
 - (a) empowering learners with IT;
 - (b) empowering teachers with IT;
 - (c) enhancing school leadership for the knowledge age;
 - (d) enriching digital resources for learning;
 - (e) improving IT infrastructure and pioneering pedagogy using IT;
 - (f) providing continuous research and development; and
 - (g) promoting community-wide support and community building;

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Human resource management

Procedures for the appointment and dismissal of teaching staff in schools

- the Education (Amendment) Bill 2002 was passed by the LegCo on 8 July 2004 and was known as the Education (Amendment) Ordinance 2004 (the Amendment Ordinance). The Amendment Ordinance came into effect on 1 January 2005. All aided schools were required to make a submission for the establishment of an incorporated management committee (IMC) by 1 July 2009;
- under the Amendment Ordinance, Regulation 76 of the Education Regulations provided that the appointment of teachers within the establishment or for a term not less than six months should be approved by the majority of the managers of the school, and the dismissal of teachers within the establishment or employed for a term not less than six months should be approved by the majority of the managers of the school at a meeting of the management committee or IMC;
- the Amendment Ordinance provided that the IMC should appoint a principal selection committee before recommending any person to be the principal. It also provided for the composition of the principal selection committee which should select in an open, fair and transparent manner a suitable person to be the principal;
- the EMB would continue to require aided schools to adopt an open, fair and competitive appointment system and to comply with relevant provisions in the Education Ordinance and its subsidiary legislation in the recruitment of teachers;

Review of the distribution of school holidays throughout the school year

- the EMB completed in May 2004 the review of school holidays in the 2003-04 school year. A total of 447 calendars of public sector schools (including 250 primary and 197 secondary schools) were selected by stratified random sampling for analysis. The results showed that the number of days in the 2003-04 summer holidays was 47, showing a notable reduction when compared to the 53 days in the 2002-03 school year. This indicated that schools had responded positively to the recommendation on rescheduling of school holidays in the 2003-04 school year put forward in the EMB Circular Memorandum No. 136/2003 issued in June 2003; and

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- the EMB issued Circular Memorandum No. 150/2004 in June 2004 to advise schools on holiday arrangements and the setting of school calendars for the 2004-05 school year with a view to maximising student learning time.

34. The Committee wishes to be kept informed of the results of the fundamental review of grants to aided and government schools.

35. **Primary education — Delivery of effective primary education** (paragraphs 52 to 53 of Part IV of P.A.C. Report No. 41). The Committee was informed that:

Actions to promote extra-curricular activities and school-based curriculum development

- in the 2004-05 school year, a total of 1,100 schools joined the Jockey Club Life-wide Learning Fund and it was anticipated that 118,000 students would be eligible for support from the Fund;
- up to 31 August 2004, about 900 primary school heads and teachers had participated in seminars and workshops to promote quality practices in Life-wide Learning and extra-curricular activities related topics. On-going Life-wide Learning professional development programmes would be augmented in the 2004-05 school year. Besides, the number of schools joining the network school scheme had expanded from 32 in the 2003-04 school year to about 50 in the 2004-05 school year;
- for the 2004-05 school year, the Education and Manpower Bureau (EMB) had so far allocated additional teacher posts for leading school curriculum development to another batch of 154 public-sector primary schools with six or more operating classes. In addition, a Curriculum Leadership Grant of \$94,340 was provided to each of the 58 public-sector primary schools with one to five operating classes. The provision for each school was time-limited for five years;

Surveys on students' physical fitness status and participation in sports activities

- a total of 45 primary schools with over 7,000 students were sampled and had taken part in the survey conducted by The Chinese University of Hong Kong. Data collection had been completed in June 2004 and data analysis was in progress;

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Performance indicators for schools to assess and report their performance

- the EMB had posted the “Catering for Student Differences — Indicators for Inclusion” on its web page in June 2004. The EMB had organised three experience-sharing workshops in January 2004 and two seminars in May 2004 to illustrate to the 117 schools in the Integrated Education Programme the uses of such indicators in designing school self-evaluation and preparing school development plans;

Whole-school approach to support students with diverse needs

- the EMB had requested all primary schools to adopt the whole-school approach to support students with special educational needs. Starting from the 2004-05 school year, 232 primary schools had been adopting a whole-school approach, of which 168 were participating in the pilot of the new funding model and 64 would implement integrated education programmes;

Enhancing the effectiveness of the assessment mechanism in facilitating learning and teaching

- the EMB administered the System Assessment at Primary 3 in mid-2004 and would be reporting results to schools by the end of 2004. With the introduction of the System Assessment, the Secured Hong Kong Attainment Test at Primary 3 and Primary 5 had been discontinued;

Promoting Teachers’ Professional Development

- in the 2003-04 school year, the EMB conducted over 110 professional development programmes on curriculum development for primary school heads and teachers. In addition, the EMB was planning to conduct about 160 related professional development programmes in the 2004-05 school year;

Promotion campaigns to convey to parents the importance of participation in their children’s school activities

- up to October 2004, 130 schools had registered with the “Good Practices Sharing on Web” of the Committee on Home-School Co-operation. Among them, 38 schools had already uploaded their projects on the web;

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- the Committee on Home-School Co-operation organised a symposium on 12 June 2004 on “Home-school co-operation: how to foster a better learning environment”. About 600 parents attended;
- over 1,000 teachers received their Certificate of Appreciation in the “Parent-Also-Appreciate-Teachers” Drive in 2004. The Recognition Ceremony was held on 7 July 2004 to conclude the Drive; and

Introducing self-evaluation arrangements for schools

- the EMB successfully achieved its target by conducting External School Review on 106 primary, secondary and special schools in the 2003-04 school year. The target for the 2004-05 school year was 150 primary, secondary and special schools. The four-year cycle would be completed by the 2006-07 school year.

36. The Committee wishes to be kept informed of further development on the subject.

37. **Public markets managed by the Food and Environmental Hygiene Department** (Chapter 1 of Part VII of P.A.C. Report No. 41). The Committee was informed that:

Comprehensive review of the market stall vacancy rate of public markets

- to invite more trade operators to consider conducting business in the markets, the Food and Environmental Hygiene Department (FEHD) had written to more than 40 trade associations in July 2004 to publicise its markets and invite members of the associations to lease the FEHD’s market stalls. The FEHD had also published information booklets containing useful information of its markets for distribution to interested parties and the public. The FEHD would continue to explore different ways to attract potential stall tenants from a greater variety of trades so as to expand the range of products sold in the markets;
- to enhance attractiveness to potential bidders, the FEHD had identified a number of long-standing vacant small stalls for merging into larger stalls before letting them out through open auction. Where technically feasible and economically viable, the FEHD would request the Architectural Services Department (Arch SD) to carry out the conversion works;

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- to enhance communication with market-goers and tenants, the FEHD had launched a quarterly newsletter since August 2004 for distribution in all public markets. Promotion and improvement initiatives, such as festive decorations and the provision of rest area, would be launched in a few selected markets with a view to attracting more customers and creating a more favourable shopping environment. The FEHD would consult the relevant Market Management Consultative Committees on these proposed initiatives before implementing them;
- the FEHD was studying the feasibility of setting a target market stall vacancy rate (MSVR) for each individual market by making reference to the overall MSVR in the past years, circumstances in the district and competition in the vicinity;
- the FEHD had reviewed the reasons for the high MSVRs in the few markets commissioned after 1998. In general, the reasons included increasing competition from supermarkets, the presence of a number of fresh provision shops and other retail outlets in the vicinity of these markets, changing shopping habits of the public, over-provision of market stalls, etc. The FEHD would study in greater depth the causes for the high MSVRs in the concerned markets, namely Lei Yue Mun, Luen Wo Hui, Peng Chau and Yee On Street markets where the MSVRs were 20% or over;

Review of ways to express the market stall vacancy rate

- the FEHD had completed the review and would present two overall MSVRs, namely a gross MSVR which covers all vacant stalls including those set aside for designated purposes, and a net MSVR which excluded all stalls frozen for such purposes, when next publishing the relevant documents;

Review of the justifications for the maximum number of non-trading days allowed in a year

- the FEHD was drawing up a new aligned tenancy clause governing the maximum number of non-trading days allowed in a year with a view to standardising the different provisions in the tenancy agreements relating to non-trading days in markets in the urban areas and the New Territories. The FEHD planned to introduce the aligned tenancy clause when it entered into new tenancy agreements with the stall tenants;

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Review of the demand for public market facilities

- the Health, Welfare and Food Bureau (HWFB) was discussing with the Planning Department the need to review the current planning standards for the provision of market facilities as set down in the Hong Kong Planning Standards and Guidelines;

Study to identify markets that might merit closure and details of the Health, Welfare and Food Bureau's rationalisation plan to be drawn

- the FEHD was conducting a study to identify markets with serious and insurmountable viability problems that might merit closure/consolidation. Based on the results of the study and the views of the stakeholders including the affected stall tenants and the relevant District Councils (DCs), the HWFB and the FEHD would draw up rationalisation plans;

Reassessment of the need to retrofit air-conditioning systems in public markets, including the Yue Wan Market, the San Hui Market and the Fa Yuen Street Market

- the FEHD completed a review of the need to retrofit air-conditioning (A/C) systems to public markets and cooked food centres including the Yue Wan Market, the San Hui Market and the Fa Yuen Street Market and advised the Legislative Council Panel on Food Safety and Environmental Hygiene on 3 March 2004 that there was no clear evidence to suggest that retrofitting of A/C systems would help improve viability of these markets. The Panel took a strong view that the FEHD should carry out the retrofitting works. The FEHD subsequently informed the Committee that the FEHD would proceed with the above projects. The Finance Committee had approved funding for the works in the Yue Wan Market. Subject to the outcome of consultation with the relevant DCs or concerned stall tenants, the FEHD planned to submit funding bids for the relevant works in the San Hui Market and Fa Yuen Street Market in the 2004-05 legislative session;

Identification of beneficial permanent use of vacant market floor space in the Fa Yuen Street Market and the To Kwa Wan Market

- the Arch SD had confirmed the technical feasibility of the proposed conversion of the vacant floor space on the second floor of Fa Yuen Street Market into office accommodation for government use. The FEHD, the Government Property Agency and the Financial Services and Treasury Bureau were exploring the feasibility and cost-benefits of internal relocation and reallocation of vacated offices to other government users; and

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- the FEHD was exploring the possibility of turning the vacant basement floor in the To Kwa Wan Market into one of the FEHD's seized goods compounds. The FEHD and the Arch SD were now studying the technical feasibility of this proposal.

38. The Committee wishes to be kept informed of further development on the subject.

39. **Provision of noise barriers for mitigating road traffic noise** (Chapter 2 of Part VII of P.A.C. Report No. 41). The Committee was informed that:

Sufficient time in works contracts and incremental approach

- the Administration was consulting relevant departments on proposed amendments to two circulars promulgated by the Environment, Transport and Works Bureau with a view to formally reminding the works departments to:
 - (a) allow sufficient time in their works contract implementation plans for complying with the relevant statutory requirements; and
 - (b) adopt an incremental approach in putting up noise barriers to tie in with the timing of completion of the planned environmentally sensitive uses;

Recover costs from private developers

- the Administration was checking whether there were cases of noise mitigating works similar to the private residential development concerned in Ma On Shan. Subject to the outcome of this research, the Administration would explore the feasibility of recovering from the developer concerned the cost of constructing the noise barriers as appropriate; and

Other audit findings

Post-implementation monitoring

- regarding the recommendation to conduct post-implementation monitoring of the effectiveness of the noise barriers for Tolo Highway Widening Project and Hiram's Highway Improvement Phase 3, the Highways Department had undertaken to complete the monitoring as recommended by end 2004.

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40. The Committee wishes to be kept informed of the progress of the various measures being taken by the Administration.

41. **Buildings Department's efforts to tackle the unauthorised building works problem** (Chapter 3 of Part VII of P.A.C. Report No.41). The Committee was informed that:

Extent of compliance with section 24 orders and complaint cases

- the Buildings Department (BD) had enhanced its monitoring system on complaint cases and provided additional staff training. It had also deployed additional resources and set performance targets to speed up the clearance of long outstanding removal orders in respect of unauthorised building works (UBW). Progress in clearing these outstanding removal orders was satisfactory. The BD still aimed to clear by March 2005 100%, 75%, 50% and 35% of the outstanding removal orders issued before 1991, between 1991 and 1995, between 1996 and 1998 and in 1999 respectively. The targets to clear 80%, 75%, 52% and 40% of the orders issued in 2000, 2001, 2002 and 2003 respectively by March 2005 had already been achieved by July 2004;
- the BD had deployed additional resources to speed up follow-up actions on complaint cases. For those complaint cases in the Buildings Condition Information System (BCIS) without the "initial action date", the BD had deployed additional resources to enter all relevant data into the BCIS and had completed all outstanding "initial actions" by June 2004. "Initial actions", once completed, were duly recorded into the BCIS. These improvement measures had been fully adopted;

Buildings Department's prosecution policy and practice

- the BD had stepped up prosecution against owners who failed to comply with removal orders. The current target was to instigate 1,000 prosecutions in 2004 and 2,000 prosecutions in 2005. The BD had already initiated 1,076 prosecutions by 15 September 2004;

Blitz operations

- the BD had since 2003 put in place measures to improve the effectiveness of the Blitz operations, such as reinforcing contract provisions to ensure that outsourced contractors employed staff with the required competence to

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provide quality services, thereby reducing the department's cost in supervising the contractors. The BD had also set more reasonable target completion time for the 2004 Blitz operations and ensured that the target completion time was met;

The Coordinated Maintenance of Buildings Scheme

- the BD had reviewed the effectiveness of the Coordinated Maintenance of Buildings Scheme (CMBS) and was preparing a report on the outcome;

Illegal rooftop structures

- the BD had completed a survey and identified an additional 1,060 single staircase buildings with illegal rooftop structures for clearance action. The BD was preparing an action plan to clear these additional illegal rooftop structures, taking into consideration the resources required and the means to redeploy resources;

Control of signboards

- as regards the removal of dangerous signboards, the BD had devised a work plan to clear those long outstanding Dangerous Structure Removal Notices by December 2004. Progress was in accordance with the work plan. Furthermore, the BD proposed to include the control for the erection of signboards in the minor works control regime to be established under the Buildings Ordinance. The minor works control regime aimed at providing a legal, safe and cost-efficient means for the carrying out of minor works, including signboards. The Administration intended to introduce the Buildings (Amendment) Bill in 2005 to take forward the proposed regime. The Administration would carry out a post-implementation review of the regime to ascertain its effectiveness; and

Removal action by government term contractor

- for those outstanding removal orders involving UBW in common areas of buildings, and where building owners had difficulties in coordinating the necessary removal works, the BD had been stepping up the enforcement actions by mobilising the government contractor to carry out the works and thereafter recovering the costs from the liable owners.

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42. The Committee wishes to be kept informed of further development on the clearance of outstanding removal orders of UBW, the BD's prosecution practice, the CMBS, illegal rooftop structures and control of signboards.

43. **Planning and provision of public secondary school places** (Chapter 4 of Part VII of P.A.C. Report No. 41). The Committee was informed that:

Classroom utilisation

- the Education and Manpower Bureau (EMB) continued to monitor closely the utilisation of classrooms by schools to ensure the optimal use of resources for promoting learning and teaching effectiveness;

Unfilled places in public secondary schools

The problem of unfilled places at Secondary Seven

- the EMB would continue with the existing practice of allowing schools to admit more Secondary Six students on a voluntary basis while respecting schools' professional decision;

Under-utilisation of ex-prevocational/technical schools

- to address the problem of under-utilisation in ex-prevocational/technical schools, the EMB continued to take appropriate action such as combining under-enrolled classes. In the 2004-05 school year, a total of 80 under-enrolled classes in these schools had been combined and packed into 65 classes, and eight of these schools had been approved to operate Project Yi Jin courses as an additional progression path for students who did not wish to pursue the traditional senior secondary curriculum;

Need for buying schools places from caput schools

- the EMB was carrying on the discussion with the Caput Schools Council and the nine caput schools on the way forward. Among them, six seemed receptive to the idea of joining the Direct Subsidy Scheme (DSS), one proposes to close down by the 2006-07 school year and the remaining two had yet to decide on the way forward should the Government cease the provision of subvention as the overall student population declined further. The EMB would continue the dialogue with the caput schools and monitor the demand and supply of school places in the respective districts;

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Government secondary schools

Application of the broad guideline that each district should have one government school

- the EMB would follow the broad guideline as and when opportunities arose to relocate, merge or phase out government schools. This was subject to the availability of school sites. Reference would also be made to supply and demand of school places at the district level;

Objectives of providing government secondary schools

- following a critical review, the EMB considered that government schools should continue to play a special role in the school system, for example, in pioneering new initiatives and serving as community resource centres in education. The EMB would continue to adjust the class structure and number of classes in government schools having regard to changes in demands;

Under-utilisation in some government secondary schools

- the EMB continued to monitor the utilisation of government secondary schools and to combine under-enrolled classes. In the 2004-05 school year, seven government secondary schools would see a reduction of a total of 11 classes;

Higher operating cost of government secondary schools

- in the 2004-05 school year, the EMB would continue with the recruitment freeze for all government school teaching posts and the employment of temporary teachers on non-civil service contract terms to fill teaching vacancies. Where possible, government schools would contract out janitor and clerical services;

Model for projecting future supply and demand for public secondary school places

Vacant classrooms

- the EMB continued to monitor the utilisation of classrooms to ensure the optimal use of resources, and would factor this in the regular updates of the projected supply and demand of school places;

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School places reserved for repeaters

- in June 2004 the EMB completed a survey on the utilisation of repeater places in public-sector secondary schools. The survey results indicated that the utilisation rate on a school basis corresponded closely with the overall utilisation rate of 5% of enrolment for all public sector secondary schools. Although there was a lower demand for repeater places at the junior secondary levels, there was a higher demand at the senior secondary levels. In overall terms, schools agreed that an overall 5% provision of school places for repeaters was appropriate. The EMB endorsed this view;

School places provided by Direct Subsidy Scheme schools

- less than five years had elapsed since the last major modification of the DSS policy. Since the proportion of DSS school places was still low (less than 5%) as at present, the EMB considered it necessary to continue to build DSS schools and/or approve the transfer of aided schools to the DSS in order to realise the policy objective of increasing diversity and choice of education opportunities for students. The EMB would continue to monitor the development of DSS schools, with particular attention on their trend and pattern of enrolment; and

New schools under planning

- in accordance with the established practice, the latest annual update of the supply projection in the last quarter of 2003 had reflected all the projects added to the School Building Programme in the year. As always, the EMB continued to ensure that all new school projects added to the School Building Programme after one annual updating exercise in projection would be taken into account automatically in the next one.

44. The Committee wishes to be kept informed of:

- the outcome of the discussion between the EMB and the Caput Schools Council of the need for buying schools places from caput schools; and
- the progress of the development of DSS schools.

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45. **The acquisition and clearance of shipyard sites** (Chapter 5 of Part VII of P.A.C. Report No. 41). The Committee was informed that:

Resumption and clearance of the North Tsing Yi shipyard site

- the recommendations in paragraph 2.14 of the Audit Report mainly related to the need to hold tenants under short term tenancies (STTs) to their contractual obligation of clearing structures when the STTs were terminated. The Director of Audit (D of A) had recommended that where a waiver of this obligation was considered necessary, the prior approval of the Secretary for Financial Services and the Treasury had to be sought. Also, the Director of Lands should state clearly in the Lands Administration Office Instructions (LAOI) the specific justifications under which an STT tenant might be exempted from clearing the site upon termination of the tenancy;
- the Administration was considering how best to implement these recommendations. Experience from past clearance exercises indicated that some STT tenants might have genuine financial difficulties in arranging for the demolition of their structures. In the light of this experience, the Lands Department (Lands D) was examining in conjunction with relevant bureaux and departments the possibility of exempting certain clearerees from complying with the self-demolition requirement on compassionate grounds and possibility of providing measures to better enforce the self-demolition requirement. Subject to the outcome of the forgoing exercise, the LAOI would be amended as recommended by the D of A;
- as regards the issue of the recovery of the decontamination costs of the North Tsing Yi shipyard sites, the Government had issued protective writs to maintain its ability to recover costs from the ex-tenants and owners and was gathering evidence in this regard;

Assessment of contamination at the Penny's Bay shipyard site

- the Civil Engineering and Development Department had implemented the recommendations in paragraph 3.25 of the Audit Report in relation to the planning of site investigations for potentially contaminated leased sites before they were surrendered to or resumed by the Government;
- the Lands D had implemented the recommendations in paragraph 3.26 of the Audit Report in relation to the stipulation in the lease conditions that the Government had the right to carry out site investigation prior to resumption or surrender of sites to the Government. The LAOI had also been updated

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to specify the need of sharing information among departments prior to resumption or surrender of land to the Government;

- pursuant to the recommendation in paragraph 3.27 of the Audit Report, the Environment, Transport and Works Bureau had issued a circular memorandum to all works departments promulgating Audit's recommendations for improving the pre-acquisition site investigations and liaison with other concerned departments for potentially contaminated sites;

Surrender of the Penny's Bay shipyard site to the Government

- the Lands D had implemented the recommendations in paragraph 4.29 of the Audit Report in relation to the incorporation of environmental protection and indemnity clauses in land lease conditions; and
- as regards the recovery of the decontamination cost from the ex-lessee of the Penny's Bay shipyard site or the shipyard operator, the Government was still reviewing the legal and technical issues with outside leading counsel and experts. According to the advice of the Department of Justice, details on those issues should not be disclosed at this stage in order not to prejudice the Government's interests.

46. The Committee wishes to be kept informed of the progress of the various courses of action taken by the Administration.

47. **Funding of tertiary education** (Chapter 6 of Part VII of P.A.C. Report No. 41). The Committee was informed that:

University Grants Committee's endeavours in benchmarking the cost of tertiary education

- as a first step to review the costing and funding methodology of the sector funded by the University Grants Committee (UGC), the UGC had appointed a consultant to carry out a scoping study. Subject to the results of the scoping study, the UGC would draw up a work plan within the 2004-05 academic year, and conduct the review during the 2005-06 to 2007-08 triennium when the funding situation became more stable;

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Funding and resource allocation

- the UGC would adopt a new funding methodology in the allocation of funds to UGC-funded institutions for the 2005-06 to 2007-08 triennium. To enhance the transparency of the funding methodology and the institutions' understanding of how funds were distributed, the UGC would disclose the details of the Academic Programme Categories, together with their relative cost weightings, upon completion of the funding exercise in early 2005;

Research assessment exercise and implementation of research projects

Transparency of the research assessment exercise results and widening the membership of the research assessment exercise assessment panels

- the UGC would bear in mind the need to implement measures to enhance the transparency of the research assessment exercise (RAE) results, as well as to widen the membership of the RAE assessment panels when planning for the next RAE to be conducted for the 2005-06 academic year;

Terminated research projects

- the Research Grants Council (RGC) had formed a Working Group to examine various issues relating to the change of Principal Investigators (PIs), assessments of terminated projects, and the extension of time of research projects. The Working Group had completed its deliberations and the recommendations were considered by the RGC at its meeting in June 2004. The RGC's decisions were as follows:
 - (a) the RGC recognised the need to build into the system some flexibility for the change of PIs, in particular in the current financial climate when there was a practical need for institutions to retain maximum freedom in managing their staff resources. On the other hand, the RGC was also mindful of the need to uphold the quality of project management. The RGC had therefore decided to adopt a prudent approach and to allow change of PIs during the 7th to the 12th month of the project period in exceptional cases and where there were genuine and justifiable reasons; and
 - (b) in order to assess terminated projects in a more effective and reasonable manner, the RGC had adopted a new template for end-point assessment. When assessing projects that were terminated before the original expected completion date, the RGC would take into account the reason(s)

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for termination, and assess the performance of the project in the light of time and money spent on the project;

Extension of time of research projects

- having regard to the lead time required for projects to start, the RGC had decided that the official commencement date for all projects should be the first day of January of the year following the award of research grant, unless the PI set an earlier date. The maximum allowable extension would be 12 months. The first six-month extension would be scrutinised and approved by institutions, and any further extension requests would only be considered by the RGC where strong justification existed. Requests for extension exceeding 12 months would not be considered unless under extraordinary circumstances. As in the past, the RGC would continue to consider requests for extension on a case-by-case basis, and institutions should exercise their judgement before forwarding recommendations to the RGC for consideration. The new rules would apply to projects funded in the 2004-05 academic year and thereafter;

- in view of the development of the local research community over the years, the RGC considered that it was timely to review the requirements regarding the completion of research reports. Taking into account the standards and practices of other international funding bodies, the RGC had decided to shorten the timeline for submission of completion reports from 18 to 9 months after the approved completion date of the project. This new rule would apply to projects funded in the 2004-05 academic year and thereafter;

Funding of self-financing activities

- the Working Group on Review of Overhead Recovery Practices on Self-financing Activities of UGC-funded Institutions had analysed relevant data collected on the existing practices of individual institutions in recovering the overheads of self-financing academic programmes and continuous and professional education programmes. A final draft report and a set of proposed guidelines had been produced and were being circulated to the Working Group for comments;

- as regards non-UGC-funded research contracts and grants, the Working Group had also analysed relevant data collected on the existing practices of individual institutions, and a set of proposed guidelines was being drafted. After deliberations among the institutions, the Working Group would, in

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consultation with the UGC, prepare a consolidated recommendation for consideration by the Heads of Universities Committee;

- as part of the review of overhead charging, the UGC would also consider whether student hostels should be subject to overhead charging and, if necessary, revise the UGC Notes on Procedures accordingly;

Refund of government rents and rates

- the Education and Manpower Bureau was taking action to promulgate its policy on refund of government rents and rates to eligible educational institutions in Hong Kong through its established channels; and
- the UGC had submitted a set of draft guidelines on the eligibility criteria for refund of government rents and rates to the Administration for consideration. Subject to the views of the Administration, the UGC would consult institutions on the draft guidelines and would update the UGC Notes on Procedures accordingly in due course.

48. The Committee wishes to be kept informed of further development on the subject.

VI. Committee Proceedings

Consideration of the Director of Audit's Report tabled in the Legislative Council on 24 November 2004 As in previous years, the Committee did not consider it necessary to investigate in detail every observation contained in the Director of Audit's Report. The Committee had therefore only selected those chapters in the Director of Audit's Report No. 43 which, in its view, referred to more serious irregularities or shortcomings. It is the investigation of those chapters which constitutes the bulk of this Report.

2. **Meetings** The Committee held a total of 21 meetings and 10 public hearings in respect of the subjects covered in this Report. During the public hearings, the Committee heard evidence from a total of 23 witnesses, including 3 Directors of Bureau and 3 Heads of Department. The names of the witnesses are listed in *Appendix 4* to this Report. A copy of the Chairman's Introductory Remarks at the first public hearing on 8 December 2004 is in *Appendix 5*.

3. **Arrangement of the Report** The evidence of the witnesses who appeared before the Committee, and the Committee's specific conclusions and recommendations, based on the evidence and on its deliberations on the relevant chapters of the Director of Audit's Reports, are set out in Chapters 1 to 5 below.

4. The audio record of the proceedings of the Committee's public hearings is available in the Library of the Legislative Council for the public to listen to.

5. **Acknowledgements** The Committee wishes to record its appreciation of the co-operative approach adopted by all the persons who were invited to give evidence. In addition, the Committee is grateful for the assistance and constructive advice given by the Secretary for Financial Services and the Treasury, the Legal Adviser and the Clerk. The Committee also wishes to thank the Director of Audit for the objective and professional manner in which he completed his Reports, and for the many services which he and his staff have rendered to the Committee throughout its deliberations.

**VII. Observations of the Public Accounts Committee on the Report
of the Director of Audit on the Accounts of the Government of the
Hong Kong Special Administrative Region for the year ended 31 March 2004**

The Committee noted the Report of the Director of Audit on the Accounts of the Government of the Hong Kong Special Administrative Region for the year ended 31 March 2004.

Chapter 1

Control and monitoring of District Council expenses and related activities

The Audit Commission (Audit) conducted a review on the control and monitoring of District Council (DC) expenses and related activities.

Tax deduction on 50% of the honorarium for District Council Members

2. The Committee noted from paragraphs 2.14 and 2.15 of the Director of Audit's Report (the Audit Report) that the Commissioner of Inland Revenue had, since 1982, adopted an administrative measure which allowed, without query, a deduction of 50% of the honorarium for a DC Member as tax deductible expenses. Since April 1996, the DC Members' remuneration package had been expanded to include allowance and grant for various office expenses incurred by DC Members for discharging their duties. The current rates of the allowance and grant for reimbursable expenses amounted to almost 50% of the total remuneration package for DC Members. The tax treatment for DC Members' honorarium was different from those for Executive Council (ExCo) Members' and Legislative Council (LegCo) Members' honorariums which were all taxable.

3. The Committee asked whether the Director of Home Affairs had consulted the Commissioner of Inland Revenue on the taxation matters relating to the inclusion of the Office Rental Allowance (ORA) in DC Members' remuneration package in 1996.

4. **Mrs Pamela TAN KAM Mi-wah, Director of Home affairs**, responded that:

- the Home Affairs Department (HAD) had consulted the Commissioner of Inland Revenue in 1995 on whether the ORA was taxable and the Commissioner had given a negative reply; and
- before expanding the scope of the ORA to allow the employment of DC Members' assistants in 2000, the HAD had also consulted the Commissioner in 1999 and the Commissioner had responded that the ORA after the expansion was not taxable.

5. **Mrs Alice LAU MAK Yee-ming, Commissioner of Inland Revenue**, pointed out that the HAD had consulted the Inland Revenue Department (IRD) before adjusting DC Members' honorarium and before starting to provide them with accountable allowance.

6. The Committee asked whether the different tax treatments for the honorariums of LegCo Members and DC Members were fair.

Control and monitoring of District Council expenses and related activities

7. The **Commissioner of Inland Revenue** responded that:

- both LegCo Members and DC Members had the right to claim tax deduction on expenses incurred in discharging their official duties. The administrative measure regarding tax deduction on DC Members' honorarium was an arrangement to deal with their expenses of this nature;
- the IRD did not adopt such measure on its own initiative. Rather, it would only act on individual employer's or organisation's request for such tax treatment. In considering these proposals, the IRD adopted the same criteria, i.e. whether the amount claimed was small, whether it would be too complicated to keep the receipts and whether the characteristics of the trade concerned warranted such tax deduction. For instance, the IRD had agreed to the Judiciary's proposal of adopting an administrative measure which allowed tax deduction on the expenses for dry-cleaning the wigs and robes of judges, on the grounds that the amount of such expenses was small and the attire was required for the work of judges; and
- the administrative measure for DC Members' honorarium was proposed to the IRD by the HAD. She was not aware that the LegCo had discussed with the IRD whether LegCo Members required such an administrative measure on tax deduction. If LegCo Members had, in addition to those reimbursable under the operating expenses package, incurred expenses which were wholly, exclusively and necessarily on LegCo business, they could apply to the IRD for tax deduction on such expenses.

8. The Committee enquired about the rationale for adopting the above administrative measure for DC Members' honorarium in 1982 and retaining it despite the expansion of DC Members' remuneration package.

9. The **Commissioner of Inland Revenue** explained that:

- in 1982, DC Members' remuneration package was an all-inclusive non-accountable honorarium to meet earnings forgone due to time spent on DC matters and expenses incurred in connection with DC business. The package did not include an accountable allowance for office expenses incurred by DC Members. The honorarium was, for tax purposes, regarded as an income from office held and as such it would attract Salaries Tax under the Inland Revenue Ordinance (IRO). However, expenses wholly, exclusively and necessarily incurred in the production of income chargeable

Control and monitoring of District Council expenses and related activities

to tax could be claimed for tax deduction under the IRO. The claim, however, had to be substantiated to the IRD. At that time the IRD considered that 50% of the honorarium was a small and reasonable amount of money for expenses wholly, exclusively and necessarily incurred in the production of income and was therefore tax deductible. By allowing such deduction, the IRD could also obviate the need for DC Members to substantiate the deduction claim for such an amount and to keep the relevant documentary evidence of expenses. The IRD therefore adopted the administrative measure;

- after 1982, the honorarium had been increased due to inflation and the strengthening of DC Members' role. In 1996, the remuneration package had been expanded to include the ORA which was replaced by the Accountable Allowance (AA) afterwards. The AA was not taxable because it was used for expenses incurred by DC Members in the strengthening of their role and payable on a reimbursable basis on production of certified receipts for such expenses. The IRD noted the substantial increase in the rate of the AA from \$10,000 to \$17,000 since December 2001. As the administrative measure had already been adopted for a number of years by that time, the IRD decided to retain the measure for the time being;
- according to the table on the percentages of non-taxable income in the total income of DC Members and LegCo Members, in **Appendix 6**, the percentages in respect of DC Members and LegCo Members in 1996 were 61% and 65% respectively. The former percentage rose to 68% following the increase of DC Members' honorarium in 2000, while the latter remained unchanged. After adjustments to the remuneration packages of DC Members and LegCo Members in 2001, the percentages stood at 75% and 69% respectively. The latest percentages in 2004 were 75% and 70% respectively. She considered that as the percentages in respect of DC Members and LegCo Members were comparable, the tax deduction on 50% of DC Members' honorarium, which was used in computing their non-taxable income, was not unreasonable; and
- nevertheless, as the measure had been in force for a number of years, the IRD agreed to Audit's observation that there was a need to review the justifications for continuing the measure. The IRD had discussed with the HAD and come to a preliminary view that the administrative measure should be removed. As a large portion of the current (2004-05) year of assessment had passed and the administrative measure was still in force at present, DC Members might not have kept the receipts for the expenses which would be required for claiming tax deduction. As such, the IRD considered it reasonable for the removal to be implemented for the 2005-06 final and subsequent years of

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assessment. By then DC Members, like other taxpayers, would have to apply for tax deduction on any amount of expenses incurred and keep documentary evidence of such expenses.

10. The Committee asked about the percentage of DC Members who claimed tax deduction on 50% of their honorarium.

11. The **Director of Home Affairs** replied that, in the past four years, about 65% of DC Members claimed tax deduction on 50% of their honorarium and the remaining 35% claimed more than that. Of this 35%, some successfully claimed tax deduction on 100% of their honorarium while the deduction for the others was slightly higher than 50% of their honorarium.

12. The Committee further asked whether DC Members had to submit supporting documentary evidence in making claims for tax deduction on their honorarium.

13. In response, the **Commissioner of Inland Revenue** informed the Committee that:

- DC Members were required to return to the HAD duly completed forms regarding whether or not they would provide a monthly breakdown of expenses for claiming tax deduction;
- for those claiming tax deduction on 50% of their honorarium, they could opt not to provide such breakdown. As the arrangement for tax deduction on 50% of DC Members' honorarium was operated under an honour system, the DC Members concerned did not need to keep or submit supporting documentary evidence; and
- for those claiming tax deduction on more than 50% of their honorarium, they should opt to provide a monthly breakdown of expenses and keep the documentary evidence for verification by the IRD if necessary.

Control and monitoring of District Council expenses and related activities

14. In view of the Commissioner of Inland Revenue's reply that the IRD and the HAD planned to remove the administrative measure starting from the 2005-06 year of assessment, the Committee asked:

- whether the removal of the administrative measure would affect DC Members' services to local residents; and
- whether the Administration had consulted DC Members on the above plan and, if not, whether it would do so.

15. The **Director of Home Affairs** clarified that the plan only gave a direction on the matter. The detailed arrangements for implementing the plan had yet to be worked out. The HAD would proactively communicate with DC Members concerning the impact of the plan on their services to the public, with a view to making reasonable arrangements for the continuation of their services to the local community.

16. The **Commissioner of Inland Revenue** added that the IRD respected the views of LegCo Members and would take into account the Public Accounts Committee's views in its Report before deciding on the plan.

17. In response to the Committee's enquiry about the work plan for implementing the removal, the **Commissioner of Inland Revenue**, in her letter dated 28 December 2004 in *Appendix 7*, informed the Committee that:

- the IRD had contacted the HAD regarding whether there would be any change to the remuneration package of DC Chairmen and Members as well as the control and monitoring measures to be exercised over the reimbursable and non-reimbursable expenses; and
- subject to the HAD's response and the Committee's comments, the IRD would proceed to implement the removal. In any event, the IRD would, through the HAD, advise the DC Chairmen and Members to keep documentary evidence of expenses incurred from 1 April 2005 in support of their tax deduction claims for the 2005-06 final and subsequent years of assessment.

Control and monitoring of District Council expenses and related activities

18. Regarding the IRD's comparison of the non-taxable incomes of DC Members and LegCo Members, the Committee pointed out that the two incomes were very different because, unlike DC Members, LegCo Members could not claim tax deduction on 50% of their honorarium. In fact, LegCo Members' honorarium was all taxable. If 50% of DC Members' honorarium was regarded by the Administration as tax-deductible expenses incurred on DC business, the Administration might consider converting that amount into DC Members' Operating Expenses Allowance (OEA) which was non-taxable. As such, DC Members' honorarium, similar to those of ExCo Members and LegCo Members, would all be taxable.

19. The **Commissioner of Inland Revenue** responded that:

- the above conversion proposal could be an option for consideration by the Administration in its review of the matter. However, if the review concluded that DC Members' honorarium should be kept at the present level, the more reasonable way to deal with the matter was to remove the administrative measure regarding tax deduction on the honorarium; and
- the Administration would closely communicate with DC Members before implementing the removal arrangements. After the removal, DC Members, similar to LegCo Members, could claim tax deduction on the expenses which were wholly, exclusively and necessarily incurred on DC business and which exceeded the amount of the OEA.

Allowance and grant for District Council Members

20. As revealed in paragraph 3.7 of the Audit Report, Audit found 354 cases of non-compliance with the HAD Guidelines on the reimbursement of the OEA and the Information Technology and Other Support Grant (ITOSG) to DC Members during its random sample check on the reimbursement records of the OEA and the ITOSG in respect of DC Members in nine selected District Offices (DOs) for the period January 2002 to March 2004. As these records only concerned some one-third of DC Members in these nine DOs and there were altogether 18 DCs in Hong Kong, the number of non-compliance cases in respect of all DC Members in the territory might probably be much larger than 354. The Committee asked whether the HAD would take immediate action to ensure full compliance with its guidelines.

Control and monitoring of District Council expenses and related activities

21. In response, the **Director of Home Affairs** informed the Committee that:
- the HAD accepted Audit's recommendation that improvements should be made regarding the processing of claims for reimbursement of the OEA. The HAD had started to make such improvements and would review the existing guidelines to provide clearer guidance to its staff at district level;
 - the HAD had asked its staff at district level to strictly follow the HAD Guidelines and exercise meticulous care in processing the claims. The co-operation of DC Members was also necessary, e.g. early submission by DC Members of receipts which were missing in their claims; and
 - some of the 354 cases of non-compliance arose from Audit's interpretation of what constituted non-compliance, which was different from that of the HAD. For instance, name cards containing photographs were, in Audit's view, publicity items containing information other than those allowed in the HAD Guidelines. However, such name cards were regarded by the HAD as printed items and thus photographs were allowed. These different interpretations gave rise to such a large number of cases of non-compliance.
22. The Committee asked about the details of the follow-up actions taken on the 354 cases of non-compliance.
23. In her letter of 31 December 2004 in *Appendix 8*, the **Director of Home Affairs** informed the Committee that the HAD had examined the 354 cases. The HAD would request the DC Members concerned to provide supplementary information in support of their claims and would recover the overpayment of allowance and grant, etc, as soon as possible. It aimed to complete all follow-up actions by March 2005. Details of the follow-up/remedial actions were also provided in the letter.
24. According to paragraphs 3.18 and 3.19 of the Audit Report, the Director of Home Affairs generally agreed with Audit's recommendations regarding non-compliance with and revision of the HAD Guidelines. The Committee asked about the progress in implementing these recommendations.

Control and monitoring of District Council expenses and related activities

25. In her letter of 31 December 2004, the **Director of Home Affairs** pointed out that the HAD:

- had appealed to all DC Members in early December 2004 for full compliance with the HAD Guidelines in claiming reimbursement of the OEA and the ITOSG. It had also held a special briefing with all DC Chairmen and Vice-Chairmen to explain to them the major areas of non-compliance and the imminent introduction of additional control measures to step up the monitoring system;
- had reminded all staff at the district level to process the reimbursement of the OEA and the ITOSG with meticulous care and ensure strict adherence to the HAD Guidelines; and
- was reviewing the HAD Guidelines based on Audit's recommendations and would consult DC Members in January 2005 to seek their comments on the proposed revision.

Use of District Council funds for the Minor Environmental Improvement projects

26. The Committee noted that, in its random sample check of the Minor Environmental Improvement (MEI) projects in nine selected DOs, Audit had found cases of non-compliance with the District Council Funds Guidelines (DCF Guidelines) on the use of DC funds. The MEI projects for grass-cutting jobs were outside the HAD's responsibilities. In addition, some MEI projects for grass-cutting jobs were not cost-effective.

27. The Committee further noted that Audit had recommended that the Director of Home Affairs should, in implementing the MEI projects, ensure that the DOs comply with the requirements and observe the conditions laid down in the relevant circulars and guidelines; evaluate the cost-effectiveness of the projects; and ensure that the Government was protected against claims for accidents arising from the projects. The Committee asked about the progress in implementing Audit's recommendations.

Control and monitoring of District Council expenses and related activities

28. In her letter of 31 December 2004, the **Director of Home Affairs** informed the Committee that the HAD:

- had requested/reminded all DOs to:
 - (a) draw up/update the list of MEI projects for which they had maintenance responsibility; and
 - (b) comply with the DCF Guidelines and government circulars in implementing MEI projects;
- had awarded term contracts for, amongst others, grass cutting in three districts in the New Territories. It planned to expand the term contract system to cover the remaining districts in April 2005; and
- was reviewing the following arrangements and would revise the relevant guidelines where necessary:
 - (a) the need to conduct annual checks for projects requiring maintenance to a high standard; and
 - (b) the granting of cash assistance to rural committees to undertake grass-cutting jobs.

Submission of annual district plans

29. According to paragraphs 5.14 and 5.15 of the Audit Report, the Director of Home Affairs generally agreed with Audit's recommendations regarding monitoring of the submission of the annual district plans (ADPs) by the core departments. The Committee asked about the progress in implementing Audit's recommendations.

30. In her letter of 31 December 2004, the **Director of Home Affairs** informed the Committee that the HAD had drawn up a set of standard procedures for monitoring the submission of the ADPs by the core departments. All DOs had been requested to adhere to the standard procedures with effect from 1 January 2005.

Control and monitoring of District Council expenses and related activities

District Council Homepages

31. The Committee noted that Audit had reviewed the Homepages of all the 18 DCs and found cases of non-compliance with the Guidelines on Dissemination of Information through Government Homepages (Government Homepage Guidelines) and improper use of DC funds for developing additional homepages.

32. The Committee further noted that Audit had recommended that the Director of Home Affairs should encourage the DC Secretariats to follow the Government Homepage Guidelines and improve the contents of DC Homepages, and review the use of DC funds for the development and maintenance of separate homepages for the DCs. The Committee asked about the progress of implementing Audit's recommendations.

33. In her letter of 31 December 2004, the **Director of Home Affairs** informed the Committee that the HAD:

- had advised the DCs to follow the Government Homepage Guidelines;
- would assist DCs in drawing up short-term and long-term improvement plans for their respective DC Homepages, having regard to the current level of compliance with the relevant Audit's recommendations, individual district needs and characteristics; and
- had reviewed the use of DC funds for developing additional DC Homepages and revised the existing arrangement so that DC funds could be used for one-off development and/or annual enhancement/maintenance of these homepages on a project-by-project basis.

34. **Conclusions and recommendations** The Committee:

Tax deduction on 50% of the honorarium for District Council Members

- expresses serious concern that the Commissioner of Inland Revenue continued to adopt the administrative measure which allows, without query, a deduction of 50% of the honorarium for a District Council (DC) Member as tax deductible expenses despite the fact that, since April 1996, the DC Members' remuneration package has been expanded to include allowance and grant for various office expenses incurred by DC Members for discharging their duties;

Control and monitoring of District Council expenses and related activities

- expresses concern that the tax treatments for the honorarium of DC Members and those of Executive Council (ExCo) Members and Legislative Council (LegCo) Members are not the same. The honorariums of ExCo Members and LegCo Members are all taxable whereas a tax deduction on 50% of a DC Member's honorarium is allowed;
- notes that the Commissioner of Inland Revenue plans to remove the above administrative measure for the 2005-06 final and subsequent years of assessment;
- recommends that the Director of Home Affairs should consider revising the existing remuneration package of DC Members by converting 50% of a DC Member's honorarium to the Operating Expenses Allowance (OEA) which is non-taxable, so that DC Members' honorarium, similar to those of ExCo Members and LegCo Members, is all taxable;

Allowance and grant for District Council Members

- expresses alarm and strong resentment that:
 - (a) 354 cases of non-compliance with the Home Affairs Department (HAD) Guidelines on the reimbursement of the OEA and the Information Technology and Other Support Grant (ITOSG) to DC Members were found by the Audit Commission during its random sample check on the reimbursement records of the OEA and the ITOSG in respect of only about one-third of the DC Members of nine selected District Offices (DOs); and
 - (b) despite complaints from time to time against DC Members for misusing the OEA subsidised ward offices for non-DC activities, the HAD Guidelines still do not provide adequate guidance for the DOs to deal with issues relating to such misuse;
- expresses serious concern that the supporting documents to substantiate the OEA claims for the employment of assistants by DC Members are inadequate;
- expresses concern that:
 - (a) the HAD Guidelines do not specify the detailed requirements of a site visit to DC Members' ward offices; and

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- (b) there is no procedure for handling the return of capitalised items partly paid for by DC Members;
- notes that the HAD:
 - (a) has examined the 354 cases of non-compliance and will request the DC Members concerned to provide supplementary information in support of their claims and will recover the overpayment of allowance and grant, etc, as soon as possible. It aims to complete all follow-up actions by March 2005;
 - (b) has appealed to all DC Members in early December 2004 for full compliance with the HAD Guidelines in claiming reimbursement of the OEA and the ITOSG. It has also held a special briefing with all DC Chairmen and Vice-Chairmen to explain to them the major areas of non-compliance and the imminent introduction of additional control measures to step up the monitoring system;
 - (c) has reminded all staff at the district level to process the reimbursement of the OEA and the ITOSG with meticulous care and ensure strict adherence to the HAD Guidelines; and
 - (d) is reviewing its Guidelines based on audit recommendations in paragraph 3.18(b) of the Director of Audit's Report and will hold consultation with DC Members in January 2005 to seek their comments on proposed revision of the Guidelines;

Use of District Council funds for the Minor Environmental Improvement projects

- expresses grave concern and finds it unacceptable that:
 - (a) contrary to the District Council Funds Guidelines (DCF Guidelines), seven out of nine selected DOs did not maintain an up-to-date list of all the Minor Environmental Improvement (MEI) projects for which they had maintenance responsibility;
 - (b) approvals for some MEI projects given by the approving officers were not in line with the approving authority stated in the DCF Guidelines;
 - (c) extra works not covered by the DC's original approval were included in an MEI project;

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- (d) payments for some MEI projects were not in accordance with the relevant circulars or guidelines;
 - (e) some MEI projects for grass-cutting jobs were outside the ambit of the HAD's responsibilities;
 - (f) the arrangement of some MEI projects for grass-cutting jobs under separate contracts was not cost-effective; and
 - (g) some MEI projects for grass-cutting jobs undertaken by a rural committee were not cost-effective and the Government is exposed to claims for accidents arising from the projects;
- notes that the HAD:
- (a) has requested/reminded all DOs to:
 - (i) draw up/update the list of MEI projects for which they have maintenance responsibility; and
 - (ii) comply with the DCF Guidelines and government circulars in implementing MEI projects;
 - (b) has awarded term contracts for, amongst others, grass cutting in three districts in the New Territories. It plans to expand the term contract system to cover the remaining districts in April 2005; and
 - (c) is reviewing the following arrangements and will revise the relevant guidelines where necessary:
 - (i) the need to conduct annual checks for projects requiring maintenance to a high standard; and
 - (ii) the granting of cash assistance to rural committees to undertake grass-cutting jobs;

Control and monitoring of District Council expenses and related activities

Submission of annual district plans

- expresses concern that:
 - (a) the overall average submission rate of 55% of the annual district plans (ADPs) by the core departments, for the period from January 2002 to June 2004, was not satisfactory;
 - (b) the non-submission of the ADPs by the core departments might affect the effectiveness of the DCs in reflecting the community views on their work plans; and
 - (c) the HAD had not issued guidelines on the standard procedures to be followed by all the DOs for monitoring and following up the submission of the ADPs by the core departments;
- notes that the HAD has drawn up a set of standard procedures for monitoring the submission of ADPs by core departments. All DOs have been requested to adhere to the standard procedures with effect from 1 January 2005;

District Council Homepages

- expresses concern that there were cases of non-compliance with the Guidelines on Dissemination of Information through Government Homepages (Government Homepage Guidelines) in the set-up and maintenance of the 18 DC Homepages;
- expresses dismay that two DCs used DC funds to set up their own separate homepages showing their DC activities, which were not appropriate under the guidelines on the use of DC funds;
- notes that the HAD:
 - (a) has advised the DCs to follow the Government Homepage Guidelines;
 - (b) would assist DCs in drawing up short-term and long-term improvement plans for their respective DC Homepages, having regard to the current level of compliance with the relevant audit recommendations, individual district needs and characteristics; and

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- (c) has reviewed the use of DC funds for developing additional DC Homepages and revised the existing arrangement so that DC funds can be used for one-off development and/or annual enhancement/maintenance of these homepages on a project-by-project basis; and

Follow-up actions

- wishes to be kept informed of:
 - (a) the progress of implementing the removal of the administrative measure regarding tax deduction;
 - (b) the decision made by the Director of Home affairs on the Committee's recommendation that 50% of a DC Member's honorarium be converted to the OEA and any progress made;
 - (c) the progress and results of the follow-up actions taken on the 354 cases of non-compliance;
 - (d) the progress of reviewing the HAD's Guidelines on the reimbursement of the OEA and the ITOSG;
 - (e) the progress of reviewing the need to conduct annual checks for the MEI projects requiring maintenance to a high standard and the granting of cash assistance to rural committees to undertake grass-cutting jobs; and
 - (f) the progress of assisting DCs in drawing up short-term and long-term improvement plans for their respective DC Homepages.

Chapter 2

Government subsidies to the English Schools Foundation

The objectives of this audit review were to examine the evolution of government subsidies to English Schools Foundation (ESF) schools vis-à-vis international schools, and the Education and Manpower Bureau (EMB)'s reviews of the subsidies to the ESF in recent years.

2. **Prof Hon Arthur LI Kwok-cheung, Secretary for Education and Manpower,** and **Prof Felice Lih MAK, Chairman, ESF,** respectively made an opening statement at the Committee's public hearing. Their statements are in *Appendices 9 and 10* respectively.

Reviews of government subsidies to English Schools Foundation schools and international schools

3. The Committee noted that government subvention to the ESF on the parity of subsidy principle was premised on the 1965 Education Policy White Paper in recognition of the need for English schools for English-speaking children, which led to the establishment of the ESF in 1967 through the enactment of The English Schools Foundation Ordinance. Since the establishment of the ESF, the EMB had carried out three major reviews of government subsidies to ESF schools in 1979, 1995 and 1999.

4. The Committee also noted that, in response to the request from expatriate communities for the provision of more international school places, the EMB formed a Working Group on the Provision of International School Places to review the government subsidies to international schools. The Working Group's recommendations were approved by the Executive Council in 1995.

5. In response to the Committee's enquiry as to why ESF schools were not included in the review of government subsidies to international schools in 1995, the **Secretary for Education and Manpower** said that because of the unique status of the ESF, which was established under its own Ordinance, the EMB considered it more appropriate to conduct separate reviews for ESF schools and international schools. This arrangement had no implication on whether ESF schools were international schools.

6. According to paragraph 2.7(a) of the Director of Audit's Report (the Audit Report), in January 2000, in its report to the Social Service Policy Group chaired by the Chief Secretary for Administration, the EMB stated that ESF schools were not different in nature from other international schools in terms of curriculum offered and student mix.

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However, government subsidies provided for ESF schools were much more favourable than those for other international schools. As revealed in Appendix B to the Audit Report, on 22 February 2000, the EMB expressed a different view that ESF schools were in a category entirely different from international schools and played an important role in providing parents with choice and diversity. In this connection, the Committee asked:

- about the reasons for the EMB changing its view; and
- whether such a change implied that the EMB had in the past recognised that ESF schools were different from international schools.

7. The **Secretary for Education and Manpower** and **Mrs Fanny LAW, Permanent Secretary for Education and Manpower**, responded that:

- as the level of government subsidies provided to ESF schools was different from that of international schools, seen in this perspective, it was true that ESF schools were in a category different from international schools;
- as defined by the Working Group on the Provision of International School Places, international schools were schools which followed a non-local curriculum and their students did not sit for local examinations. From this perspective, ESF schools were not different from international schools in nature, as ESF schools also followed a non-local curriculum and their students also did not sit for local examinations;
- unlike local aided schools, the graduates of which mostly pursued their studies in local universities, the majority of the graduates of ESF schools, similar to those of international schools, pursued their studies overseas; and
- local schools must provide their students with a choice to sit for local examinations, even if they offered the International Baccalaureate curriculum.

8. In response to the Committee's enquiry about the ESF's position within the education sector, **Mr John Bohan, Acting Secretary and Chief Executive, ESF**, stated in his letter of 28 December 2004, in *Appendix 11*, that:

- among those living and working in Hong Kong were people from around the world, including ethnic Chinese who held passports of other countries, people of other Asian ethnicities, Eurasians, as well as those who would traditionally have been categorised as "expatriates". These groups had permanent

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residence rights in Hong Kong. They contributed to the local economy, paid taxes and considered themselves as Hong Kong people. The ESF served people in those categories as well as an increasing number of local Chinese families;

- with regard to its student population, the ESF did not regard a distinction between “local” and “international” as a meaningful one. In ESF schools, nowadays 81% of students were permanent residents in Hong Kong; and
- the ESF regarded itself as an integral part of the local education system. Underpinned by its Ordinance, the ESF provided the system with an international dimension, as befit an international city. ESF schools were partners of the EMB, working together on a number of initiatives including the opening of private independent schools.

9. As stated in paragraph 2.10(a) of the Audit Report, during the EMB’s consultations on the possible withdrawal of government subsidies to the ESF, the Chairman of the Foundation, the supreme governing body of the ESF, and the Chief Executive of the ESF had indicated their willingness to work with the Government for a smooth transition. However, in her opening statement made at the hearing, the Chairman of the ESF stated that no proposal on changing the basis of ESF funding was ever put before the Foundation. The Committee asked:

- about the basis of her statement; and
- whether the Foundation knew about the proposed withdrawal of government subsidies to the ESF at that time.

10. The **Chairman, ESF** said that:

- as provided in The English Schools Foundation Ordinance, the Foundation was the supreme governing body over the Executive Committee (ExCom) which was the executive body of the Foundation. This provision clearly stipulated that decision-making powers vested in the Foundation rather than the ExCom;
- the ExCom had not provided sufficient information to the Foundation as far as the proposed reduction or withdrawal of recurrent government subsidies was concerned, which she considered to be serious negligence of the ExCom; and

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- according to the minutes of the Foundation's annual general meetings, the proposed reduction or withdrawal of government subsidies to the ESF had not been discussed nor endorsed by the Foundation.

11. **Mrs Cherry TSE, Deputy Secretary for Education and Manpower**, stated that the Secretary of the ESF had made a report on "ESF subvention", among other issues, to the Foundation at its annual general meeting on 14 December 2000. An extract from the minutes of the meeting is in *Appendix 12*. The Secretary's Report on the "ESF subvention" issue read as follows:

"Last year I spoke of the issue of the ESF grant which has supported ESF since 1967 and in the case of the Government's English schools long before that.

As a result of lengthy negotiation, the grant has been capped at its current level apart from growth in student numbers. So effectively, the principle of parity has been conceded. It was unrealistic with the Government spending so much on its own programme of reform that we should also benefit thereby depriving the local sector of much-needed resources. However, we shall reserve the right to go back to Government should inflation bite and threaten our viability."

12. The **Deputy Secretary for Education and Manpower** added that:

- it was ESF practice that the Secretary would report to the Foundation at its annual general meetings on any important issues that had come up in the past year;
- judging from the contents of the Secretary's Report, the Foundation should have been aware that:
 - (a) there was ongoing discussion between the ESF and the Government over the proposed reduction or withdrawal of recurrent government subsidies to the ESF; and
 - (b) the parity of subsidy principle had been conceded;
- given that the Foundation meeting on 14 December 2000 was attended by various stakeholders including school principals as well as representatives of teachers and parents, they should have been aware of the concession on the parity of subsidy principle and the possible withdrawal of government subsidies to the ESF; and

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- the minutes of the Foundation meeting should have recorded more details if there was any dissenting view on the “ESF subvention” issue reported by the Secretary.

13. **Dr Sarah Rigby, Chairwoman of Joint Council of Parent Teacher Associations, ESF**, said that:

- as the “ESF subvention” issue was subsumed in the Secretary’s Report instead of being put as a separate agenda item for that Foundation meeting, the issue was not widely communicated to the ESF parents at large. If the issue was included under a separate agenda item, there should have been much more inputs from parents;
- when reading the Secretary’s Report in context, the concession on the parity of subsidy principle was made under a difficult economic climate. It was therefore logical to believe that this was only a temporary arrangement to help tide over the difficulties at that time; and
- as the proposed reduction or withdrawal of subsidies to the ESF involved a substantial change to the subvention policy and would have implications on many parties, it should only be proceeded with after extensive consultation with stakeholders. However, the ESF parents had not been consulted throughout the process.

14. **Mr Alex CHIU, Parents Representative, ESF**, shared Dr Rigby’s view that ESF parents should be consulted as the proposed withdrawal of subsidies had far-reaching implications on ESF parents.

15. The **Deputy Secretary for Education and Manpower** pointed out that if the parents were not satisfied with the ESF’s approach for handling the proposed withdrawal of government subsidies, they could have requested a review of the issue by the Foundation at its subsequent meetings. However, the issue had not been further raised at any of the subsequent meetings of the Foundation.

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16. The **Chairman, ESF** said that:

- as the “ESF subvention” issue had not been placed on the agenda of the Foundation meeting on 14 December 2000 as an item for discussion, it should not be taken to mean that the proposed reduction or withdrawal of recurrent government subsidies to the ESF had been deliberated and endorsed by the Foundation;
- since the Government’s proposal to reduce or withdraw its subsidies to the ESF was a very important issue, it should not have been buried in the Secretary’s Report. It should have been put up separately for open discussion by all stakeholders; and
- although the 6% pay cut proposal was very moderate, it had triggered a strong reaction when it was considered at a Foundation meeting. Hence, she did not believe that the proposed withdrawal of government subsidies to the ESF, if discussed at the Foundation meeting on 14 December 2000, could have been passed so smoothly.

17. In response to the Committee’s enquiry, the **Acting Secretary and Chief Executive, ESF** informed the Committee that:

- although the Foundation had not discussed the parity of subsidy principle and the possible withdrawal of government subsidies, the issues had been discussed by the ExCom at two of its meetings on 7 March 2000 and 5 April 2000; and
- apart from the ExCom meetings, there was ongoing discussion of the issue among the Chairman, the Vice-Chairman, the Treasurer and the Chief Executive of the ESF.

18. The **Acting Secretary and Chief Executive, ESF** then referred the Committee to Appendix B to the Audit Report, which provided a summary of the exchange of views between the EMB and the ESF on the Government’s proposed withdrawal of recurrent subsidies to the ESF. He stated that:

- in late 1999, the ESF suggested that the Government should allow the ESF to modify its land lease conditions so that it could redevelop its school sites and expand its services. This would facilitate the ESF in generating income to compensate for the withdrawal of government subsidies;

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- on 22 February 2000, the EMB stated that some commercial developments were necessary within the framework of any changes in the usage of ESF sites. A summary of the relevant discussion on 22 February 2000 between the EMB and the ESF was provided in the ESF Chief Executive's letter of 16 March 2000, in *Appendix 13*;
- in his letter of 13 April 2000, in *Appendix 14*, the Secretary for Education and Manpower informed the ESF that the Government would have difficulties in agreeing to the ESF's proposed redevelopment of the Borret Road site if it was no longer required for educational purposes;
- based on the above, it was clear that the understanding reached between the EMB and the ESF about the proposed withdrawal of subsidies involved reciprocal undertakings by the Government to review the ESF's ability to use its properties to generate additional income. The EMB's inability to support its undertaking in this regard had made it more difficult for the ESF to cope with the proposed withdrawal of subsidies;
- as a result, the Chief Executive of the ESF informed the EMB, via her letter of 15 January 2001 in *Appendix 15*, that:
 - (a) unless a radical scheme was envisaged to involve commercial use of ESF leading school sites, it was highly unlikely that sufficient revenue could be raised to replace the one-third of the ESF's costs covered by government subsidies; and
 - (b) it was not the time to embark on the scheme on commercial use of ESF school sites in view of the political sensitivity and the property market condition at that time; and
- the discussion between the EMB and the ESF on the arrangement for phasing out government subsidies had virtually been brought to an end by the ESF Chief Executive's letter of 15 January 2001.

19. The **Chairman, ESF** added that the discussion between the EMB and the ESF over the years on the future of government subsidies to the ESF was never concluded and that the ESF was an integral part of the local education system. The ESF's position on the parity of subsidy principle remained unchanged and it should be entitled to government funding as other schools in the aided sector.

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20. The Committee noted from the ESF Chief Executive's letter of 16 March 2000 that the Chairman of the ESF had emphasised that the phasing-out programme should stretch over a period of 13 years. As this proposed arrangement was raised by the former Chairman of the ESF, the Committee invited him to provide in writing the reasons for and the circumstances leading to his agreement to this arrangement.

21. In his reply of 17 January 2005, in *Appendix 16*, **Mr Jal Shroff, former Chairman, ESF** advised that:

- to the best of his knowledge, there was no firm agreement with the Government that the parity of subsidy principle be forgone and that the withdrawal of subsidies be phased out over a period of 13 years. If there had been such an agreement, the matter would have been resolved;
- his understanding was that he had in discussion with a representative of the EMB who suggested that a way to resolve the issue was for the EMB to phase out the subsidies over a period of 13 years plus modification of all the ESF's land lease conditions so that it had the option to redevelop some of its school sites commercially to generate additional income to make up for the loss of revenue from the subsidies; and
- he believed that there was a reasonable chance for the Foundation and the ExCom to accept the above arrangement as a "fair" solution. However, as the EMB was not in a position to agree to the modification of land lease conditions, as far as he could remember, the discussion did not continue.

22. The **Permanent Secretary for Education and Manpower** stated at the hearing and the **Secretary for Education and Manpower** stated in the letter of 24 January 2005, in *Appendix 17*, that:

- as the full programme of ESF education lasted 13 years, the 13-year phasing out programme suggested by the ESF would ensure that existing parents would not be affected by the change and that notice could be given to new parents;
- the 13-year withdrawal programme was not dependent on the proposed land lease modification. As clearly illustrated by the exchange of views between the EMB and the ESF in 2000 and 2001, the Government shared the ESF's view that the withdrawal of subsidies should be properly managed with a reasonable transitional arrangement, which should comprise a basket of

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measures such as expansion of the ESF's services, reduction of its cost base and redevelopment of its school sites. Land lease modification was only one of the several possibilities mooted;

- the EMB was willing to allow time for the ESF to operate more kindergartens as this kind of education business had great potential for development. This would be conducive to the ESF generating more income to facilitate its operation under a self-financing mode;
- as a measure to reduce its overall unit cost, the ESF was also encouraged to operate private independent schools. Nevertheless, the Secretary for Education and Manpower had made clear to the ESF, in his letter of 13 April 2000, that the approval of the application for a private independent school was independent of the proposal to phase out government subsidies to the ESF;
- regardless of whether there had been proper consultation within the ESF about the proposed withdrawal of subsidies, the Chief Executive of the ESF had clearly acknowledged in her letter of 15 January 2001 that the parity of subsidy principle had been forgone following the freeze of the per-class subsidies with effect from the 2000-01 school year. The only trigger for revisiting the issue was when inflation threatened the ESF's viability. Logically, this trigger did not justify disowning the agreement to forgo the parity of subsidy principle especially when, after years of deflation, the prevailing price level remained significantly lower than that in 2000;
- the concession on the parity of subsidy principle took place after the Secretary for Education and Manpower had conveyed, via his letter of 13 April 2000, to the ESF the Government's reservation about land lease modification. In other words, the explicit agreement to forgo the parity of subsidy principle was made in the clear knowledge of the non-feasible nature of lease modification;
- the Government had been pursuing the subvention review with goodwill, taking into account the possible impact on the ESF and its stakeholders. That was why, despite its principled approach, the reduction in government subsidies to the ESF had been rather mild notwithstanding the fiscal deficit. The Government had been exercising utmost care in ensuring that the review and any changes arising from it must be consistent with students' best interest and must abide by the law; and

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- in the EMB's view, the focus of the discussion was not on "whether" recurrent government subsidies should be withdrawn, but rather "how" the withdrawal should be phased. The EMB had been conscientiously pursuing the subvention review through frequent discussions with the ESF over the past few years, and would expedite action to complete it.

23. The **Deputy Secretary for Education and Manpower** supplemented that:

- the ESF enjoyed preferential treatment not only vis-à-vis international schools but also private independent schools and direct subsidy schools. Under the existing arrangement, private independent schools were not provided with recurrent government subsidies whereas direct subsidy schools were subject to various regulatory monitoring by the EMB. However, in the case of the ESF, it was provided with recurrent government subsidies but was not subject to the EMB's regulatory monitoring;
- another example of preferential treatment was that, among the various types of schools, only ESF schools were allowed to convert up to 50% of the capital grant into a loan to enable them to meet the larger cash-flow requirements in their school building projects; and
- the EMB considered that the existing subvention arrangement for the ESF was an anomalous historical legacy, which should be revisited in the present-day context, having regard to the development of a vibrant international school sector outside the ESF system.

24. In paragraph 2.22(b) of the Audit Report, the ESF provided a number of reasons to justify that its schools were different from international schools and that it was an integral part of the local system. In view of the historical context of the provision of subvention to ESF schools, the Committee enquired whether the Government would consider continuing its recurrent subsidies to ESF schools.

25. The **Secretary for Education and Manpower** responded that:

- it was the Government's responsibility to ensure optimal and appropriate use of public money. In view of the many problems and deficiencies in the governance and management of the ESF, the ESF should undertake a rigorous reform expeditiously to achieve the level of transparency and accountability required of a leading education institution. The EMB considered this an overriding priority over the subvention issue; and

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- ESF schools received recurrent government subsidies as local aided schools but were not subject to the same monitoring by the EMB. This was not a reasonable arrangement. If the ESF continued to fail to adopt a high standard of governance and management, the Government would have no alternative but to reduce or withdraw the existing subsidies, in order to safeguard public money.

26. **Dr Sarah Rigby** said that:

- the overriding issue was whether English-speaking children of Hong Kong should be entitled to a subvented education as other local children under the parity of subsidy principle;
- the English-speaking children in Hong Kong nowadays were very different from those in the old colonial days, as a large proportion of the former were permanent residents of Hong Kong and considered themselves as “Hong Kongers”. The Government should consider how this group of English-speaking children were to be catered for in the local school system; and
- from a macro perspective, the Government might consider adopting a voucher system to enable parents to select a school of their choice for their children with the amount of subsidy provided under the system.

27. The **Permanent Secretary for Education and Manpower** and the **Deputy Secretary for Education and Manpower** said that:

- the Government provided equitable access to nine years’ free and universal primary and junior secondary education to all children in the relevant age groups. There were schools which used English as the medium of instruction to cater for the needs of English-speaking children who wished to follow the local curriculum;
- for some reasons, such as parents’ preference for the pedagogy of a school, some parents chose to leave the local system which offered free education and to enter the private school sector at their own cost; and
- in the case of ESF schools, a majority of their students were local people. They chose to leave the local school system to join the ESF. In fact, the Government had already reserved school places for this group of students in the local system.

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28. **Dr Sarah Rigby** said that:

- there were very few primary and secondary schools within the local school system which used English as the medium of instruction. These schools were incredibly competitive in view of the limited places they offered. Many children would not fit into the local school system because of their lack of competency in Chinese. For example, some parents found that, upon their return to Hong Kong after emigrating overseas for a number of years, it was difficult for their children to re-integrate into the local school system;
- the ESF offered an affordable high quality education in the medium of English with an international dimension, which perfectly met the needs of middle-class English-speaking families. Some students whose families were on a budget might be forced to leave the ESF should there be significant increase in the school fees after the removal of government subsidies; and
- at present, the ESF had a total of some 12,000 students. If the government subsidies to the ESF were to be removed and a great number of these students had to leave the ESF because of financial problems, it would be a considerable task for the Government to work out how such a large group of students were to be integrated into the local school system.

29. The **Deputy Secretary for Education and Manpower** responded that the EMB would discuss the needs of English-speaking children with the new ESF Chief Executive after she assumed office in February 2005. In fact, there were some encouraging cases in which foreign students had successfully adapted to the environment of local direct subsidy schools.

30. The Committee enquired whether the Government would consider providing subsidies to the ESF in other forms, e.g. subsidies under the Direct Subsidy Scheme, so that the Government might exercise regulatory monitoring over ESF schools.

31. The **Permanent Secretary for Education and Manpower** replied that:

- a school would be denied subsidies under the Direct Subsidy Scheme if its school fees were beyond two and one-third of the average unit cost of an aided-school place. It appeared that the ESF was not eligible for the Scheme as its current school fees were much higher than the permitted level of school fees under the Scheme; and

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- the Code of Aid as applied to aided schools governed, among other things, teacher-to-student ratio, appointment and dismissal of staff, implementation of school-based management structure, use of premises, and so on. She did not consider this a suitable mode for ESF schools.

32. The **Secretary for Education and Manpower** said that the EMB would adopt an open mind in discussing with the new ESF Chief Executive, once she assumed office in February 2005, the way forward in respect of the future subvention arrangement for the ESF. The review might lead to no change, a reduction or an increase in government subsidies to the ESF.

33. The **Chairman, ESF** said that the ESF welcomed monitoring by the Government. She stressed that the ESF had demonstrated its resolve to achieve greater transparency and accountability. This was evidenced by its putting forward a proposal of restructuring its governance and management, which had been approved by the Foundation in December 2004. A timetable for implementing the proposed restructuring had also been drawn up.

34. According to paragraph 2.23(g) of the Audit Report, the EMB believed that through enhancing cost-efficiency, ESF resources could be saved without erosion of education quality or increase in tuition fees. The Committee asked about the basis of the EMB's statement.

35. The **Secretary for Education and Manpower** explained that:

- the statement was made on the basis of the calculations made by the EMB. The EMB noticed that there were wide concerns on fee increase among ESF parents. Some ESF staff had been quoted to have repeatedly suggested that withdrawal of government subsidies would automatically mean a 40% increase in the current fee level. This was grossly misleading. Such a causal relationship between subvention and the fee level could only be made if all of the following happened:
 - (a) the ESF intended to charge parents for every dollar of subsidies forgone;
 - (b) the ESF considered that there was absolutely no room for efficiency savings despite economy of scale; and

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(c) the ESF did not intend to undertake any improvement measures pursuant to the observations of the Audit Commission (Audit); and

- the EMB hoped that none of the above was true. In the EMB's view, the cost-effectiveness of the ESF, rather than government subvention, had a greater impact on the level of its tuition fees.

36. The **Acting Secretary and Chief Executive, ESF** said that:

- in 1994, the ESF instituted a fee policy that aimed to minimise fee increases whilst maintaining high-quality education;
- over the last six years, ESF school fees had increased only once, by less than 5%. This track record had been achieved during a period when government subsidies had been frozen or reduced. By comparison, some international schools had raised their school fees by 30% over the same period;
- the ESF had produced two charts showing its fee increases compared with other fee-paying institutions over the last six years. The charts were included in the ESF's submission of 10 December 2004, in *Appendix 18*; and
- as a subvented organisation, the ESF had been mindful of the need to provide affordable education in line with its mission of serving Hong Kong people.

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37. **Hon Frederick MA Si-hang, Secretary for Financial Services and the Treasury**, declared that his two daughters had attended an ESF school.

38. The Committee noted from paragraph 3.7(c) of the Audit Report that in February 2000, the Financial Services and the Treasury Bureau (FSTB) had expressed reservations about the Government exercising discretion to freeze the number of subsidised ESF classes, without reverting to the Finance Committee (FC) of the Legislative Council.

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39. Paragraph 3.8(a) of the Audit Report further revealed that subsequently, the FSTB advised the EMB in July 2004 that, on balance, it was not necessary for the EMB to seek the FC's approval in respect of the proposed arrangement to freeze the number of ESF classes eligible for recurrent government subsidies as from the 2004-05 school year. In this connection, the Committee asked about the reasons for the FSTB's change of view.

40. **Ms Bernadette LINN, Principal Assistant Secretary for Financial Services and the Treasury (Treasury)**, replied that:

- the FSTB's view in paragraph 3.7(c) of the Audit Report aimed to alert the EMB that the FSTB would have reservations if the Government unilaterally froze the number of subsidised ESF classes in future without reverting to the FC;
- the FSTB's advice stated in paragraph 3.8(a) of the Audit Report was made on the basis that:
 - (a) the EMB's proposed arrangement to freeze the number of ESF classes eligible for recurrent government subsidies as from the 2004-05 school year had been agreed with the ESF; and
 - (b) the proposed arrangement did not pose any conflicts to the funding approval given by the FC on 17 December 1980; and
- since the proposed arrangement was only a transitional measure pending the finalisation of permanent changes to the subsidy arrangement in the near future, the FSTB considered that it was not necessary for the EMB to seek the FC's explicit approval for such arrangement.

41. According to paragraph 3.10 of the Audit Report, Audit considered that if the EMB did not envisage that permanent changes to ESF subsidy arrangements could be finalised in the near future, the EMB should seek the FC's approval for freezing the ESF per-class subsidies. Since the EMB's arrangements for freezing ESF per-class subsidies and capping the number of ESF classes eligible for recurrent government subsidies were at variance with the Government's parity of subsidy principle for providing government subsidies to ESF schools, the Committee enquired whether, from a financial policy perspective, the FSTB agreed to Audit's view that the EMB should seek the FC's approval.

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42. The **Secretary for Financial Services and the Treasury** said that the Government would ensure that all financial proposals that required the approval of the FC were submitted to it for consideration in accordance with the requirements under the Public Finance Ordinance.

43. The **Secretary for Education and Manpower** said that the EMB would work closely with the ESF to expedite the review. It would revert to the relevant authorising bodies with concrete proposals on the long-term funding arrangement for the ESF and the way of implementing the arrangement as soon as a decision on the issue had been taken.

44. The Committee noted from paragraph 3.14 of the Audit Report that the fact-finding exercise jointly conducted by the EMB and the ESF, which was originally scheduled for completion in July 2003, had still not yet been completed.

45. In response to the Committee's enquiry, the **Acting Secretary and Chief Executive, ESF** said that:

- as almost half of the ESF senior executive management posts were vacant in the past year, the tight manpower had made it difficult for the ESF to meet the target for the fact-finding exercise; and
- as there were still quite a number of contentious areas that had to be addressed, the ESF would work closely with the EMB to expedite completion of the exercise upon completion of the work associated with the three audit reviews concerning the ESF.

46. The **Deputy Secretary for Education and Manpower** said that:

- the objectives of the fact-finding exercise were to review the cost structure of the ESF and to identify possible areas for savings, with a view to assessing whether the current rate of ESF tuition fees and government subvention were fully justified. This exercise demanded tremendous efforts of both parties. As the EMB did not have direct access to ESF files and records, it needed to rely on the ESF to provide information for completing the exercise;

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- unfortunately, the latter stage of the exercise coincided with a tumultuous period of the ESF during which its Chairman and a number of its senior staff including the Chief Executive had resigned, it was understandable that the Acting Secretary and Chief Executive had experienced a lot of work pressure; and
- as the audit findings provided a very useful reference to the Government, the importance of the fact-finding exercise was not as high as that at the time when the EMB first conducted the exercise.

47. Conclusions and recommendations The Committee:

Reviews of government subsidies to English Schools Foundation schools and international schools

- notes that:
 - (a) government subvention to the English Schools Foundation (ESF) on the parity of subsidy principle was premised on the 1965 Education Policy White Paper in recognition of the need for English schools for English-speaking children, which led to the establishment of the ESF in 1967 through the enactment of The English Schools Foundation Ordinance;
 - (b) similar to private international schools, ESF schools follow a non-local curriculum and their students do not sit for local examination. However, ESF schools are provided with recurrent government subsidies whereas private international schools do not receive the same level of subsidies from the Government, even after the Government's review of its subsidies to international schools in 1995;
 - (c) since 1999, the Education and Manpower Bureau (EMB) has been discussing with the ESF the gradual reduction of its recurrent subsidies to the ESF under a phased programme. The ESF has indicated its willingness to work with the Government for a smooth transition, but has emphasised that the phasing-out programme should stretch over a period of 13 years;
 - (d) the EMB considers that the focus of its discussion with the ESF was not on "whether" recurrent government subsidies to the ESF should be withdrawn, but rather "how" the withdrawal should be phased; and

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- (e) it is the ESF's view that the discussion between the EMB and itself over the years on the future of government subsidies to the ESF was never concluded and that it is an integral part of the local education system. Its position on the parity of subsidy principle remains unchanged and it should be entitled to government funding as other schools in the aided sector;
- expresses concern that there is a divergence of views between the EMB and the ESF on whether ESF schools are no different from private international schools and whether the existing government subsidies to the ESF schools should continue;
- strongly urges:
 - (a) the EMB to expeditiously complete the review of government subsidies to the ESF; and
 - (b) the EMB and the ESF to come to an agreement expeditiously over the future of government subsidies to the ESF;

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- expresses serious concern that:
 - (a) the EMB's arrangements for freezing ESF per-class subsidies and capping the number of ESF classes eligible for recurrent government subsidies are at variance with the Government's parity of subsidy principle for providing government subsidies to ESF schools; and
 - (b) the fact-finding exercise jointly conducted by the EMB and the ESF, which was originally scheduled for completion in July 2003, has not yet been completed;
- notes that:
 - (a) the EMB has reported to the Panel on Education of the Legislative Council the progress of its review of government subsidies to the ESF; and
 - (b) the EMB and the ESF will expedite completion of the fact-finding exercise;

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- recommends that the Secretary for Education and Manpower should:
 - (a) seek the authorisation of the Executive Council and the Legislative Council for the interim measures on providing recurrent government subsidies to the ESF if changes to ESF subsidy arrangements cannot be finalised in the near future; and
 - (b) seek the approval of the Executive Council and the Legislative Council for changes resulting from the EMB's review of government subsidies to the ESF; and

Follow-up actions

- wishes to be kept informed of:
 - (a) the progress of the EMB's review of government subsidies to the ESF;
 - (b) the progress made by the EMB and the ESF in reaching an agreement over the future government subsidies to the ESF; and
 - (c) the results of the fact-finding exercise.

Chapter 3

Corporate governance and Headquarters administration of the English Schools Foundation

The objective of this audit review was to examine the corporate governance of the English Schools Foundation (ESF) as well as the financial and administrative controls of the ESF Headquarters in the provision of education services.

2. The Committee held three public hearings on 10 December 2004 and 10 and 11 January 2005 to receive evidence from the witnesses.

3. **Prof Hon Arthur LI Kwok-cheung, Secretary for Education and Manpower**, made an opening statement at each of the Committee's first two public hearings. His statements are in *Appendices 19 and 20* respectively.

Corporate governance

4. Noting that the Education and Manpower Bureau (EMB) had representation on both the Foundation, i.e. the supreme governing body of the ESF, and the Executive Committee (ExCom), i.e. the executive body of the Foundation, the Committee enquired about:

- the role of the EMB in the Foundation and the ExCom respectively; and
- the reasons for the EMB not monitoring the operation of the ESF.

5. The **Secretary for Education and Manpower** stated at the hearing and in the letter of 8 January 2005, in *Appendix 21*, that:

- the ESF was established by law and enjoyed the powers and privileges conferred on it by The English Schools Foundation Ordinance (the ESF Ordinance). In accordance with the Ordinance, the membership of the Foundation comprised 132 representatives from a wide cross-section of the community, including government officials. The role of these representatives was intended to be advisory in order to allow the ESF the benefit of the views of different community sectors. Had it been envisaged that the Government should play a watchdog role, the ESF Ordinance would not have been introduced by a private Member, and the Government would have been given the necessary statutory powers to direct and monitor the operation of the ESF. As a matter of fact, the ratio of EMB representatives to other representatives on the Foundation was only 3:132. The influence of EMB representatives on the Foundation was indeed very small;

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- for historical reasons, the EMB had one representative on the ExCom. This was a unique arrangement. The Government did not sit on the management committee of any other aided schools or the executive committee of their sponsoring bodies. This suggested that the EMB's ExCom membership was intended to serve a liaison and advisory function, ensuring that the interests of British civil servants with children attending the ESF schools were well served and that relevant policy decisions were adequately communicated. From the way the ESF Ordinance was couched, it was never intended that the Government should micro-manage or monitor the ESF; and
- on many occasions, members of the Foundation and the ExCom had not been provided with all the information that they needed to know in order to discharge their duties effectively. For instance, the ExCom had not been consulted or even informed of the details of the golden handshake packages that the ESF had offered to three of its senior staff upon their leaving the ESF. Under the circumstances, the ExCom would not know that there were cases that had departed from the established practices.

6. It appeared to the Committee that since the EMB had representation on both the Foundation and the ExCom, it had a duty to ensure that the ESF would adopt a high standard of corporate governance. Same as all other members of the Foundation and the ExCom, the EMB representatives had the right as well as the responsibility to request the ESF to provide the necessary information to enable them to discharge their duties effectively. In this connection, the Committee enquired:

- whether the EMB representatives had ever requested the ESF to provide information, where necessary, to enable them to discharge their duties effectively; and
- what action the EMB had taken to ensure cost-effectiveness of the ESF operation, especially after knowing that there might be cost-effectiveness problems in the ESF since late 2002.

7. **The Secretary for Education and Manpower and Mrs Cherry TSE, Deputy Secretary for Education and Manpower**, said that:

- according to law, the ESF might deny the EMB's access to its books and accounts as it received less than half of its income from public money. As the EMB did not have the legal right to have access to the ESF's records, the EMB representatives had encountered great difficulties in obtaining

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information to enable them to discharge their duties effectively. An example was that the ExCom had only been informed of the resignation of the former Chief Executive of the ESF, i.e. Staff C in the Director of Audit's Report (the Audit Report), but not the extra payment made to him upon his departure. The EMB had asked the ESF for details of this case on a number of occasions but in vain;

- the EMB's participation in the ESF operation was on the basis of trust and co-operation. For an organisation which had repeatedly emphasised the outstanding calibre of its staff, and with a successful business person in the chair, it was not reasonable to expect that the ExCom members should, at every ExCom meeting held monthly, take the initiative to ask if there had been any golden handshake proposals, inappropriate payments of entertainment or claims for taxi fare that had not been supported by receipts in the previous month. The EMB did not believe that the ExCom should be occupied with this kind of micro operational matters; and
- in the EMB's view, it should be for the ESF Headquarters senior executive management to bring up to the ExCom for approval cases which were not in line with established policies and/or financial management rules but which merited exceptional treatment. Members of the ExCom should be provided with all relevant information to enable them to make decisions in an intelligent and fully informed manner. As the ESF Headquarters had failed to do so, it was unfair to put the onus on the ExCom members.

8. Given that Prof Felice Lieh MAK had only assumed the ESF chairmanship for nine months, the Committee invited the former Chairman of the ESF to provide a written response on the following:

- his comments on the observations and recommendations of the Audit Commission (Audit) on the various aspects raised in the Audit Report, in particular the part on "Corporate governance";
- during his tenure as the ESF Chairman, whether the government representatives on the Foundation and the ExCom had put forward any views or suggestions on the various aspects covered in the Audit Report. In particular, whether they had raised any concerns about the inadequacy of the corporate governance and Headquarters administration of the ESF; and

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- during his tenure as the ESF Chairman, whether he had discussed with relevant government officials problems relating to the corporate governance of the ESF; if so, the contents of the discussions, the officials with whom he had discussed, and the occasions when the discussions were held; and if not, why not.

9. In his replies of 7 and 17 January 2005, in *Appendices 22 and 16* respectively, **Mr Jal Shroff, former Chairman, ESF**, stated that:

- the large membership size of the Foundation was not conducive to making decisions efficiently. Over the past many years, the Foundation had seldom made any decisions of importance. Important decision-making had been left in the hands of the nine members of the ExCom;
- external members appointed to the Foundation often did not have time or were not interested in attending the Foundation meetings. In his view, the ratio of external members to internal members should be at least 3:1, if the present situation that external members did not always constitute a majority at the Foundation meetings was to be changed;
- the ESF needed to totally review the Regulations of the English Schools Foundation (the ESF Regulations) to ensure that they reflected the changes in the multi-cultural intake of its students as well as the latest educational developments and to ensure that they were in line with the best practices;
- there was an acute need to establish an active audit committee, with one of its representatives from the Government, to monitor and advise the ExCom on all financial matters;
- he did not consider it necessary to establish an advisory body similar to those established by the University Grants Committee funded institutions, as the current four standing committees of the ESF might well serve the advisory function;
- in his opinion, the EMB should play a much more active role to exercise its influence on decisions made at the ExCom meetings dealing with financial matters. To the best of his knowledge, the minutes of the Foundation meetings and the ExCom meetings reflected that no government representative had brought up the question of corporate governance over the last ten odd years;

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- he had been the ESF Chairman for over nine years. During the period, he had met many government officials and had discussed with them various aspects relating to the acquisition of new sites for additional ESF schools, finances of the ESF, lack of school places within the ESF system to cater for children of new arrivals, problems associated with the composition of the Foundation, corporate governance of the ESF, etc. In fact, during his tenure as the ESF Chairman, he had had private discussions with the Permanent Secretary for Education and Manpower on a number of occasions on the composition of the Foundation and the need to make changes at an appropriate time; and
- every single draft budget prepared by the ESF over the last 40 odd years had to be approved by the then Education Department, currently the EMB, before it was implemented. The budget had reflected salaries, school fees, and projected surpluses or deficits.

10. The Committee invited the EMB to comment on the former ESF Chairman's response. The **Secretary for Education and Manpower, Mrs Fanny LAW, Permanent Secretary for Education and Manpower**, and the **Deputy Secretary for Education and Manpower** said, at the hearing and in the letter of 24 January 2005 (in *Appendix 17*), that:

- as regards the suggestion that the EMB should play a much more active role in the ExCom, the EMB was of the view that if the public considered that the EMB should micro-manage the ESF given the recurrent government subsidies provided to it, then the same, if not more stringent, level of control must apply to all aided schools which were almost completely funded by the Government, as well as other subvented organisations in general. This clearly deviated from the policy of not micro-managing subvented organisations, and also went against the policy of school-based management;
- as regards the statement that no government representative had brought up the question of corporate governance at any of the Foundation meetings and the ExCom meetings over the last ten odd years, it should be noted that it was the EMB's practice, as a matter of courtesy and respect to the ESF management, to first bring up its views or proposals to the ESF management for informal discussion. This would allow the ESF sufficient time to examine the proposals, so that well thought out proposals would be raised at the formal meetings of the Foundation or the ExCom at an appropriate time;

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- the EMB had expressed its views on the corporate governance of the ESF on many occasions. An example of this was the pay review process. The EMB had offered its views to the ESF on the composition and terms of reference of the ESF Pay Review Body. Indeed, the EMB had kept informal exchanges with the ESF management on a wide spectrum of issues through channels outside the Foundation and the ExCom. Most of these informal meetings had been attended by the former ESF Chairman and the discussions at those meetings were frank;
- during the course of the informal discussions on a variety of issues between the EMB and the former ESF Chairman, it had been realised that the root of the problem lay on the governance and management structure of the ESF. Unfortunately, due to the various competing priorities and the manpower constraints in the EMB, it had focused its strength on pursuing the education reform over the past few years. For this reason, the EMB had not been able to actively address the problems relating to the governance and management structure of the ESF;
- soon after the current ESF Chairman had assumed her chairmanship, the EMB had discussed with her the problems relating to the governance and management of the ESF. With her agreement, a proposal to reform the governance and management structure of the ESF had been submitted to the Foundation for consideration at its meeting in December 2004. This had demonstrated that the EMB's contribution to the ESF operation was multi-channelled, not confined to formal meetings of the Foundation and the ExCom; and
- on the question of draft ESF budget, there was no requirement under the Education Ordinance or the ESF Ordinance for the ESF to submit its annual estimates for approval by the Government. Although it had been the ESF's understanding that its past submissions were intended for the Government's approval, the EMB had only examined such estimates when considering the level of school fees, calculating grants or in contexts for similar requirements. This generally applied to all categories of schools including aided schools. It was the primary obligation of individual schools to exercise proper financial control and maintain their financial viability.

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11. At the request of the Committee, **Mr John Bohan, Acting Secretary and Chief Secretary, ESF**, provided, via his letter of 4 January 2005 in *Appendix 23*, the attendance of the government representatives at five Foundation meetings and 42 ExCom meetings held in the past five years. In the same letter, he informed the Committee that after examining the relevant minutes of meetings, there had been no mention of the corporate governance and Headquarters administration of the ESF by the government representatives at any of the Foundation meetings and the ExCom meetings held in the past five years.

12. The Committee invited the Director of Audit to comment on the Acting ESF Secretary and Chief Executive's response of 4 January 2005. In his letter of 7 January 2005 in *Appendix 24*, the **Director of Audit** advised that:

- as stated in paragraph 2.19 of the Audit Report, the failure of members to attend Foundation meetings reduced their opportunities to contribute to the ESF. The ESF Regulations prescribed that there were four government representatives on the Foundation. According to the minutes of the five Foundation meetings:
 - (a) all the four government representatives had not attended the two Foundation meetings in December 2000 and December 2001;
 - (b) only one of the four government representatives had attended each of the two Foundation meetings in December 2002 and December 2003; and
 - (c) three of the four government representatives had attended the Foundation meeting in March 2004;
- the government representatives' attendance rate of 25% at the above five Foundation meetings was unsatisfactory;
- according to Appendix 3 to the Acting ESF Secretary and Chief Executive's letter of 4 January 2005, of the 42 ExCom meetings held between March 1999 and October 2004, the government representative had attended 35 of them, representing an attendance rate of 83%. Audit considered this attendance rate acceptable; and

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- Audit's examination of the minutes of the Foundation meetings and the ExCom meetings covering the period September 2000 to April 2004 revealed that there were no recorded views of the government representatives on the corporate governance of the ESF at either the Foundation meetings or the ExCom meetings. There were also no recorded views of the government representatives on the Headquarters administration of the ESF at the Foundation meetings. However, on some occasions, the government representative had expressed views on the Headquarters administration of the ESF at meetings of the ExCom.

13. According to the Acting ESF Secretary and Chief Executive's response of 4 January 2005, the Chief Secretary for Administration (CS) had not attended any of the Foundation meetings in December 2002, December 2003 and March 2004. Of these three Foundation meetings, the Permanent Secretary for Education and Manpower had only attended the one in March 2004. The attendance of other EMB representatives at the two Foundation meetings in December 2002 and December 2003 was also not high. As regards the three ExCom meetings on 28 September 2004, 12 October 2004 and 26 October 2004, the EMB representative had only attended the one on 26 October 2004. According to the minutes of that ExCom meeting, there had been no mention of the corporate governance of the ESF by the attending EMB representative.

14. Based on the above findings, it appeared to the Committee that the level of the EMB's participation in the ESF operation was not as great as that claimed by the EMB. The Committee questioned whether the EMB had been too lax in monitoring the operation of the ESF.

15. The **Secretary for Education and Manpower**, the **Permanent Secretary for Education and Manpower** and the **Deputy Secretary for Education and Manpower** stated, at the hearing and in the Secretary for Education and Manpower's letters of 8 January 2005 and 11 January 2005 (in *Appendix 25*), that:

- contrary to the Acting ESF Secretary and Chief Executive's response of 4 January 2005, the EMB had been represented by Mr Samson LAI, in his capacity as Acting Principal Assistant Secretary for Education and Manpower, at the ExCom meeting on 28 September 2004 while the incumbent Principal Assistant Secretary was on leave;

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- on some occasions, it was the EMB's deliberate decision not to attend certain meetings of the Foundation or the ExCom. For example, the EMB deliberately decided not to attend the ExCom meeting on 12 October 2004 because the meeting was convened to consider the ESF's fund-raising strategy which was squarely an internal matter of the ESF. Moreover, against the background of its discussion with the ESF on the future of the subvention arrangement, the EMB considered its absence at that meeting desirable in order to forestall any unnecessary speculation and accusation of conflict of interests;
- as the minutes of ExCom meetings had not been prepared in a verbatim format, the absence of express reference to comments made by any one member could not be used to deduce that such member had made no contribution to the deliberations at the ExCom meetings;
- the membership of the ExCom included the Permanent Secretary for Education and Manpower or her appointed representative. It had been a long established practice that such representative was the Principal Assistant Secretary for Education and Manpower, or the Assistant Director of Education before the merger. Unless the circumstances required otherwise, this representative would attend the ExCom meetings on behalf of the Permanent Secretary;
- the Government's role on the Foundation had all along been carried out by the then Director of Education, currently the Permanent Secretary for Education and Manpower or her appointed representative. Indeed, all the Foundation meetings in the past five years, except the two most recent ones (i.e. the one on 9 December 2004 which was not included in the ESF's response of 4 January 2005, and the one on 1 March 2004), had been convened to consider routine reports such as the ESF Secretary's reports and the ESF's annual accounts. The EMB was of the view that it would make a bigger contribution by offering advice to the ExCom rather than by receiving routine reports at the Foundation meetings. Hence, in the Government's view, as far as Foundation meetings were concerned, the attendance of one government representative would suffice unless the circumstances required otherwise;
- when important issues were considered by the Foundation or the ExCom, however, the EMB would step up its representation at the respective meetings. For instance, when the Foundation elected its Chairman upon the resignation of the former Chairman, the Permanent Secretary for Education and Manpower and her two designated advisers had all attended the relevant Foundation meeting. Another example was that when the governance

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reform proposal was raised for discussion at the Foundation meeting on 9 December 2004, both the Deputy Secretary and the Principal Assistant Secretary of the EMB had attended the meeting;

- moreover, since late 2002 when the EMB had suspected significant cost-effectiveness problems within the ESF, the EMB had also stepped up its attention to the ESF operation. This was evidenced by the EMB's initiation to conduct the fact-finding exercise jointly with the ESF, which aimed at reviewing the ESF cost structure with a view to identifying possible areas for savings;
- other than meetings, the EMB had also maintained exchanges with the ESF through electronic mails, correspondence and telephone calls. The EMB representative on the ExCom had, from time to time and outside the formal channel, raised questions on the operation of the ESF; and
- the EMB would review its long-term role in the Foundation and the ExCom, including the position currently held by the CS in the Foundation, having regard to the usual practice of not getting involved in the management of individual schools or their sponsoring bodies. The EMB would follow the principle of school-based management, which aimed at devolving more responsibilities to schools and providing them with enhanced flexibility and autonomy in managing their own operation and resources according to the needs of their students, with increased transparency and accountability in their use of public funds at the same time.

16. As revealed in paragraphs 2.16 and 2.20 of the Audit Report, of the nine members of the ExCom, three were ESF staff. Furthermore, the external members of the Foundation had not constituted a majority at any of the Foundation's four annual general meetings held in the 2000-01 to 2003-04 ESF financial years. The Committee was concerned that when decisions relating to ESF staff benefits were required to be made at meetings of the Foundation, there might have been an over-reliance on the internal members.

17. **Prof Felice Lieh MAK, Chairman, ESF**, said that:

- there had been a case in the past in which the proposal to reduce the pay of teaching staff was vetoed by the ExCom at its meeting when the internal members present outnumbered the external members;

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- to avoid possible conflict of interest, a mechanism for declaration of personal interests had already been put in place in the ESF; and
- at present, only non-ESF staff members of the ExCom would be invited to participate in the discussion of staff-related issues.

18. In response to the Committee's enquiry about the details of the reform to be undertaken by the ESF in restructuring its governance and management, the **Chairman, ESF** said at the hearing and the **Acting Secretary and Chief Executive, ESF**, in his letter of 10 December 2004 in *Appendix 26*, advised that:

- at its meeting on 9 December 2004, the Foundation had approved the Draft Guidelines for the Restructuring of the Governance and Management of the ESF. This exercise might necessitate amendments to the ESF Ordinance and its regulations;
- the most fundamental change to be effected was the separation of governance and management roles. In future, the ESF would not operate at two levels, i.e. the Foundation and the ExCom. An ESF Council would be set up to replace the Foundation as the ESF's supreme governing body. The Council would comprise no more than 25 members with a 2:1 ratio of external members to internal members;
- each of the members would serve on an ad personam basis, not representing any constituency. The members would sign a code of conduct and would undertake to abide by it. There would be a register of members' interest. The staff members elected would not concurrently hold office in staff associations. The members of the Council would elect a chairman, a vice-chairman and a treasurer from amongst its external members. The Council would review its effectiveness every six years and the results of the review would be published in the ESF annual reports;
- there would be a number of standing committees of the Council. They might include an audit committee, a management committee, an academic committee, a staff council, and a joint council of parent and teacher associations;
- an audit committee had been set up to help the ESF monitor its finances and improve the cost-effectiveness of its operation. The audit committee comprised three members, the Chairman of which had been appointed by the ExCom from amongst its external members with sound audit, financial and

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accounting experience. The audit committee would report to the ExCom. Indeed, it had already held four meetings to follow up on the recommendations put forward by Audit and the Independent Commission Against Corruption; and

- a task force appointed by the ExCom would work out the details of the restructuring in consultation with the new Chief Executive who would assume office in February 2005. Open consultation would also be conducted. A timetable for implementing the proposed restructuring had been drawn up and provided in the Draft Guidelines. Hopefully, the new governance and management structure would be approved by the Foundation in July 2005.

19. In response to the Committee's further enquiry as to whether the ESF would expect the Government to play a monitoring role in the ESF Council in the future, the **Acting Secretary and Chief Executive, ESF**, in his letter of 18 January 2005 in *Appendix 27*, said that the ESF would welcome the EMB to appoint one to two members to the new ESF Council. The precise role of the EMB representative(s) would be worked out by the ESF task force in consultation with the EMB.

20. In view of the changing circumstances in the ESF, the Committee doubted the need for the continued existence of the Foundation Office. The Committee asked whether each ESF school should, in line with modern practice, be given the responsibility to manage its own operation instead of relying on a central management system which was quite costly. The Committee also enquired about the percentage of the total expenditure on the Foundation Office to the total expenditure on the entire ESF.

21. In response, the **Chairman, ESF** said that:

- the total expenditure on the Foundation Office accounted for 4.2% of the total expenditure on the entire ESF; and
- in deciding whether the Foundation Office should be retained, there were two major considerations. First, in the absence of the Foundation Office, whether the ESF as a whole would be able to achieve the best use of resources. Second, how the education quality of individual ESF schools could be maintained. The ESF needed to carefully consider the likely implications before a decision on the matter could be taken.

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22. The Committee noted that section 10(1) of the ESF Ordinance empowered the ESF to make regulations for the composition, internal management, operation, administration and control of the Foundation and ESF schools. Section 10(2) further provided that it was not necessary for any regulations made under this section to be published or laid on the table of the Legislative Council.

23. According to the legal adviser to the Committee, the legislative status of the ESF Regulations had been put in issue in the case of *English Schools Foundation & Anor v Bird* ([1997] 3 HKC). The court held that the regulations were subsidiary legislation despite section 10(2). This implied that the regulations made under this section should be published in the Gazette and tabled in the Legislative Council as other subsidiary legislation. Given that the reform of governance and management structure currently undertaken by the ESF might necessitate amendments to the ESF Ordinance and its regulations, it was advisable that the ESF took the opportunity to consider repealing section 10(2) of the ESF Ordinance so that subsidiary legislation in the form of regulations made under the Ordinance was required to be published in the Gazette and tabled in the Legislative Council.

Financial management

24. Paragraph 3.3 of the Audit Report stated that, as shown in the audited financial statements of the ESF for its past three financial years, the ESF had surpluses of \$40 million in 2000-01, \$46 million in 2001-02 and \$18 million in 2002-03. However, its liabilities significantly exceeded its current assets at the end of each of these financial years.

25. In his opening statement made at the first hearing, the **Secretary for Education and Manpower** raised the following questions:

- since cashflow of schools with a long history should be quite stable and predictable, what were the special circumstances that had kept recurring every year to have barred the ESF from better managing its income and expenditure pattern to smoothen its cashflow? and
- while the ESF had been able to run on surplus towards year end, where had the money gone during the year when the ESF was receiving tuition fees from parents?

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26. The Committee asked about the ESF's comments on the above questions. In his letter of 4 January 2005, the **Acting Secretary and Chief Executive, ESF** explained that:

- day-to-day income and expenditure was predictable from year to year. However, capital expenditure did not necessarily have a smooth pattern. The ESF funded capital expenditure was investment in new and refurbished facilities that would directly benefit students. This was over and above the amounts provided by the Government for the provision of new facilities. The Foundation's position on this was set out in paragraph 3.5 of the Audit Report. This was further exemplified on page 9 of the ESF's submission of 10 December 2004 (in *Appendix 18*); and
- it would be possible for the Foundation to arrange its finances so that an overdraft was never incurred. However, this would be contrary to usual commercial practice because no commercial organisation would deny itself access to credit. In the absence of such an overdraft facility, projects that would benefit ESF students would be delayed unnecessarily. This would not be value for money for stakeholders.

27. According to paragraph 3.4 of the Audit Report, the net current liabilities of the ESF increased by 74% from \$186 million as at 31 August 2001 to \$324 million as at 31 August 2003. At the same date, the ESF used a bank overdraft of \$99 million to finance its expenditure. Given that the EMB had a copy of the ESF's audited accounts, the Committee asked whether the EMB had been aware of the ESF's cashflow position and overdraft problem.

28. The **Deputy Secretary for Education and Manpower** replied at the hearing and in her letter of 24 January 2005 that:

- the EMB was aware of the ESF's overdraft problem. Upon receiving the routine estimates from the ESF, the EMB had indicated to the ESF the need to maintain a smooth cashflow; and
- in more recent years, the EMB had also noted that due to some non-recurrent reasons, e.g. lower income arising from the SARS outbreak and the commissioning of capital upgrading works in some ESF schools, the negative cashflow in the ESF at the end of its financial year had increased. This was an issue that the EMB had looked into in the context of its examination of the ESF's estimates and audited accounts. The EMB had also, during its informal exchanges with the ESF management, referred to the scope for

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evening out the ESF's cashflow, especially given the rather stable and predictable spending patterns of educational establishments.

29. The Committee noted from paragraph 3.16 of the Audit Report that the ESF had accepted that it was necessary to make improvement to the arrangement for individual ESF schools to maintain bank balances. The Committee asked about the details of the improvement measures and the timing for implementation.

30. In his letter of 10 January 2005 in *Appendix 28*, the **Acting Secretary and Chief Executive, ESF** provided a summary of the updated progress of the actions taken by the ESF in response to Audit's various recommendations. Regarding the arrangement for individual ESF schools to maintain bank balances, the Committee was advised that:

- the Foundation had entered into an alternative arrangement with its bankers in January 2005 to offset credit balances on its accounts with any debit balances on other accounts; and
- the ESF was examining the adoption of a central cash management and payment system similar to those adopted by large commercial organisations, without the need for each ESF school to maintain its own bank account.

Staff remuneration and recruitment

31. According to Figure 5 in paragraph 4.2 of the Audit Report, the total amount of responsibility allowances paid to ESF teaching staff in the 2002-03 ESF financial year was as high as \$37 million. Apart from salary, ESF teaching staff had also received other staff benefits such as contract gratuities, and housing and medical benefits. Moreover, according to Figure 7 in paragraph 4.20, the 25% contract gratuities received by ESF teaching staff were the highest when compared to those of the teaching staff of the seven largest private international schools in terms of student number. Table 2 in paragraph 4.22 of the Audit Report also revealed that, compared to the seven largest private international schools, the ESF also had the highest percentage (66%) of teaching staff receiving responsibility allowances. Besides, ESF teaching staff in receipt of such allowances received the highest average amount (\$98,600 a year). The Committee:

- questioned the need for paying the responsibility allowances; and
- enquired whether the ESF would review the remuneration packages of its teaching staff so as to ensure that they were broadly in line with those of its counterparts in Hong Kong.

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32. The **Acting Secretary and Chief Executive, ESF** advised that:

- responsibility allowance was given to a staff member appointed to take up responsibilities in addition to the primary responsibilities of the post he was holding. Higher responsibility allowances were normally given to department heads in important subjects like English and Science;
- the salaries of ESF teaching staff were set 14 years ago based on those of the teaching staff in the United Kingdom. Their subsequent salary adjustments had followed those of the local civil service. Since 2002, following a decision in 2000 to stop the overseas packages, remuneration levels of ESF teaching staff had been based on the need for recruiting and retaining staff of the highest quality. To secure and retain highest quality staff, the ESF had to compete in the international market, thus requiring it to offer internationally competitive terms and conditions to its teaching staff;
- the competition for the highest quality staff sought by ESF schools was fierce. It was highly desirable for ESF schools to have a stable teaching force, as excessive turnover of teaching staff was detrimental to the effectiveness of schools and caused additional expenditure and extra workload on recruitment. As revealed in Table 3 in paragraph 4.25 of the Audit Report, the turnover of ESF teaching staff had increased against the background of the 4.42% salary reduction effected in 2004; and
- as a matter of fact, the percentage of ESF staff employed on old terms and conditions of service, i.e. overseas terms, had reduced substantially in recent years and the staff employed on new terms, i.e. local terms, cost about 10% less than the average figures cited in the Audit Report. There would be continued financial savings as a result of the teaching staff on overseas terms leaving the ESF.

33. The **Chairman, ESF** informed the Committee that:

- the ESF had established a Remuneration Study Group (RSG) to conduct comprehensive reviews of the remuneration packages of its teaching staff. The RSG had met five times and would report to the ExCom in June 2005;
- given that most of the ESF teaching staff were recruited from overseas, and in order to ensure that their remuneration packages remained competitive and were in line with comparable levels in both local and overseas markets, in January 2005, the RSG had appointed an independent consultant to conduct a

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research on the remuneration of teaching staff in overseas countries. The scope of the research had already been agreed upon. The consultant would start work in February 2005 and would submit its report to the RSG in June 2005; and

- the level of contract gratuities and responsibility allowances for ESF teaching staff would be examined in the context of the review conducted by the RSG. In her view, each component, say the 25% gratuity, should not be examined on its own but should rather be considered as part of the total package. In reviewing the remuneration level, one of the most important considerations was to ensure that the totality of the remuneration packages was sufficient to attract and retain the internationally accomplished staff sought by the ESF.

34. **The Secretary for Education and Manpower, the Permanent Secretary for Education and Manpower and the Deputy Secretary for Education and Manpower** responded that:

- similar to the ESF, local international schools also had to recruit their teaching staff from overseas. Therefore, they should be facing the same situation as the ESF. In the EMB's view, the remuneration packages of the teaching staff of local international schools could provide useful reference to the ESF in its review of the remuneration packages of its teaching staff;
- the membership of the RSG comprised one ESF school principal, three ESF teaching or non-teaching staff members, two parent representatives and two community representatives;
- over the past few years, the Government had implemented a total salary reduction of over 10% (i.e. 4.42% + 3% + 3%). The second 3% cut had just taken effect from 1 January 2005. However, the pay cut effected in the ESF over the same period was only 4.42%. In late 2002, the ESF had initially planned to implement a 10% pay cut. The plan had subsequently been abandoned because of insufficient staff support; and
- the EMB did not understand why the review of the remuneration packages of ESF teaching staff had only started recently, which was two years after the initial 10% pay cut proposal was put forward. The EMB also doubted the need for the ESF to spend some four months on conducting a research on the overseas recruitment market, given the availability of local remuneration data.

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35. **Mrs Gloria NG WONG Yee-man, Parents Representative, ESF**, stated that of the 763 ESF teaching staff, only 143 were still on overseas terms. She had seen the progress made by the ESF in respect of teaching staff remuneration packages. She cautioned that a drastic reduction of the remuneration level would create conflicts between staff, which would in turn affect the education quality and the effectiveness of schools. While supporting a review of the remuneration packages of ESF teaching staff, she hoped that the matter would be handled in a gradual and orderly manner.

36. In response to the Committee's question as to whether the RSG's consultant could expedite its work, the **Chairman, ESF** said that:

- as the consultant had conducted a number of similar reviews in the past for large organisations, such as the Hospital Authority and some local universities, it might already have some information on hand that might help expedite the ESF's review. She would convey the Committee's request to the consultant;
- as in any other large organisations, the implementation of a pay cut proposal was no easy task. To achieve success, the whole process must be conducted in an open and fair manner; and
- in her view, whether the recommendations in the RSG's report would be adopted would not simply be the decision of the RSG and the ExCom. Parents and even the public might also participate in the process as the report would be open to all stakeholders. Therefore, the composition of the RSG should not be an issue.

37. The Committee asked whether the contract gratuities and responsibility allowances for new ESF teaching staff, or existing ESF teaching staff upon renewal of their contracts, would be adjusted downwards and, if so, when.

38. The **Acting Secretary and Chief Executive, ESF** replied that as the RSG had yet to complete its review of the remuneration packages of ESF teaching staff, the contract gratuities and responsibility allowances for teaching staff would remain at the current levels for the time being. Whether they needed to be reduced would depend on the outcome of the RSG's review.

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39. The **Secretary for Education and Manpower**, the **Permanent Secretary for Education and Manpower** and the **Deputy Secretary for Education and Manpower** stated that:

- the teaching staff of the primary-cum-secondary school operated by the ESF Educational Services Limited only received 10% gratuities. All the native English-speaking teachers employed by the Government received 15% gratuities. As regards local international schools, they normally offered 15% to 20% gratuities to their teaching staff; and
- according to the EMB's knowledge, many of the ESF staff were employed on contract. However, they would continue to receive 25% gratuity upon renewal of their contracts, regardless of the rates of gratuities offered by other comparable educational institutions.

40. The **Acting Secretary and Chief Executive, ESF** responded that:

- the ESF had more than 80% of its staff employed on finite contracts. He anticipated that there would be a strong adverse reaction from the ESF staff if their gratuities were to be reduced upon renewal of their contracts;
- according to the Employment Ordinance, under certain circumstances, finite contracts had the characteristics of a continuous contract of employment. Thus, the ESF would exercise caution in examining the matter; and
- the ESF was taking steps to re-draft the staff contracts to allow greater flexibility. In the revised contracts, the ESF management would be empowered to change the salary of a staff member once a year. Such change might take the form of increment or reduction.

41. In response to the Committee's enquiry, the **Chairman, ESF** confirmed that apart from teaching staff, the ESF would also review the remuneration packages of the staff of the Foundation Office.

42. According to paragraphs 4.29 and 4.30 of the Audit Report, the ESF made extra payments equivalent to 10 months' salaries to Staff A, Staff B and Staff C upon their leaving the ESF. Apart from Staff A, whose extra payment upon his leaving the ESF had been approved by the ExCom, Audit could not find records of the ExCom's decisions regarding the extra payments made to Staff B and Staff C upon their leaving the ESF. In

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this connection, the Committee asked whether the approval of the ExCom had been sought before making the extra payments to Staff B and Staff C and, if not, the reasons for that.

43. The **Acting Secretary and Chief Executive, ESF** replied at the hearing and in his letter of 4 January 2005 that:

- no formal policy had been set down concerning the making of extra payments to ESF staff upon their departure. In the three cases cited in Table 4 in paragraph 4.29 of the Audit Report, for the purpose of effective management of the Foundation and the ESF schools, the staff concerned had not been required to work during the respective notice periods;
- the decisions regarding Staff B and Staff C had been taken by officers of the Foundation pursuant to section 9 of the ESF Ordinance. These officers were ExCom members independent of any constituent groups; and
- the ESF had agreed that in future, the approval of the ExCom would be obtained before making extra payments to staff leaving the ESF and such approvals would be minuted.

44. The **Secretary for Education and Manpower** drew the Committee's attention to the following:

- after careful examination of the minutes of the relevant ExCom meetings, the EMB found that the ExCom had only been informed of the departure of the three staff in question. Only in one case, i.e. Staff A, had the ExCom been consulted on the extra payment made. In that particular case, the ExCom had been told that the resignation had been accepted "in accordance with the Conditions of Service" of the staff. However, the ExCom had not been informed that it should indeed be the resigned officer who should have paid compensation to the ESF for the short notice given for his departure; and
- in respect of Staff B and Staff C, the ExCom had only been informed of their resignations. No mention of the extra payments had been made. The EMB had only become aware of the golden handshake arrangement for Staff C through an anonymous letter to the press several months after the departure of the staff concerned. In respect of the payment to Staff B, the EMB believed that the ExCom members would have still been kept in the dark if not for the Audit Report.

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45. The **Acting Secretary and Chief Executive, ESF** informed the Committee of the following new information, which had come to his knowledge after his telephone conversations with Mr Jal Shroff, former Chairman of the ESF, on 7 January 2005:

- the ExCom had met on 23 June 2003 before the termination of the service of Staff C. Seven members of the ExCom had attended that meeting, during which two resolutions had been passed to the effect that the employment of Staff C be terminated and that Mr Shroff, in the capacity of ESF Chairman, be authorised to deal with such termination including but not limited to discussion with Staff C, giving the relevant notice, agreeing on the terms of cessation at Mr Shroff's discretion and generally all such acts as would be necessary to effect the termination; and
- the minutes of the above ExCom meeting had been circulated to all those who had attended the meeting.

46. He added that the minutes of the ExCom meeting on 23 June 2003 had not been entered in the ESF's minute books. This was the reason why Audit and he himself had not been aware of this ExCom meeting. The minutes of that meeting had only been provided to him by Mr Shroff on 7 January 2005. At the request of the Committee, the **Acting Secretary and Chief Executive, ESF** provided, via his facsimile message of 11 January 2005 in *Appendix 29*, a copy of the minutes of the ExCom meeting on 23 June 2003.

47. In response to the Committee's enquiry as to whether the terms of cessation of Staff C had been reported back to the ExCom subsequent to the discussion at the ExCom meeting on 23 June 2003, the **Secretary for Education and Manpower** advised, in his letter of 18 January 2005 in *Appendix 30*, that:

- according to the minutes of the ExCom meeting on 27 June 2003, the ExCom had only been informed of the resignation of Staff C. No report had been made on the terms of cessation of the staff member; and
- contrary to the advice of the Acting Secretary and Chief Executive of the ESF, the minutes of the ExCom meeting on 23 June 2003 had not been provided to those who had attended the meeting.

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48. The Committee also invited the former ESF Chairman to provide a written response on the following:

- details of his discussions with other ExCom members and/or ESF Headquarters senior executive management concerning the arrangements in regard to the extra payments made to Staff A, Staff B and Staff C, as well as the justifications for offering such payments to them; and
- whether the discussions had been held at meetings or outside meetings, and whether there had been any papers recording the details of the discussions.

49. In his reply of 17 January 2005, **Mr Jal Shroff, former Chairman, ESF**, advised the Committee that:

- in any “monetary” settlement made with senior staff, the ESF’s criteria had always been to keep a balance between the “cost” and the interest of its students and the reputation of the ESF;
- in every case where dismissal was involved, extensive consultation had been carried out not only with ExCom members but, where appropriate, with the respective school council members. In many cases, legal advice had also been sought to ensure that the interest of the ESF was protected and non-disclosure agreements had been signed; and
- his comments on each of the three cases were as follows:

Staff A: This involved a head office staff member. Dismissal negotiations had been finalised by the ESF Secretary and approved by the ExCom and minuted;

Staff B: This involved a head teacher who had resigned in the middle of an external inspection of the school. After due consultation, the ESF Secretary had decided that it was in the interest of the students that the officer should not continue in his post. In view of his 20 odd years of service in the ESF, a special case had been made for him to go on paid leave up to his last date of resignation. The Secretary was wrong not to have this minuted at one of the ExCom meetings; and

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Staff C: This involved the Chief Executive of the ESF. At its meeting on 23 June 2003, the ExCom had authorised him, in the capacity of ESF Chairman, to negotiate “as would be necessary to effect the termination”. The Chairman of the Management Committee had accompanied him in his discussions with Staff C to finalise details of the termination. He had nothing further to add regarding this case.

50. As the Committee has been provided with more information on the three cases concerning extra payments made to Staff A, Staff B and Staff C upon their leaving the ESF, it invited the Director of Audit to provide his latest comments on these cases after considering the new evidence.

51. The **Director of Audit** provided, in his letter of 21 January 2005 in *Appendix 31*, the following latest comments on the three cases:

- Staff A: As stated in paragraph 4.30 of the Audit Report, the extra payment made to Staff A upon his leaving the ESF had been approved by the ExCom. This approval had been recorded in the minutes of the ExCom meeting. Audit considered this arrangement a good practice;
- Staff B: As stated in paragraph 4.30 of the Audit Report, Audit could not find records of the ExCom’s decisions regarding the extra payment made to Staff B upon his leaving the ESF. In his reply of 17 January 2005, the former ESF Chairman commented that the Secretary was wrong not to have this minuted at one of the ExCom meetings. It was not clear whether this extra payment had been approved by the ExCom. Audit’s observations and recommendations on this case were stated in paragraphs 4.31 and 4.32 of the Audit Report respectively; and
- Staff C: (a) As stated in paragraph 4.30 of the Audit Report, Audit could not find records of the ExCom’s decisions regarding the extra payment made to Staff C upon his leaving the ESF. Having regard to the new information relating to the departure of Staff C provided by the Acting Secretary and Chief Executive of the ESF at the hearing on 10 January 2005 and by the Secretary for Education and Manpower in his letter of 18 January 2005, Audit considered it unacceptable that the

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minutes of the ExCom meeting on 23 June 2003 had not been entered in the ESF's minute books. As stated in Regulation 2.3 of the ESF Regulations, minutes of the proceedings of every meeting of the Foundation, ExCom, Standing Committee, School Council or any committee shall be entered in a book kept for that purpose and after confirmation signed by the chairman of such meeting or of the following meeting, and shall when so entered and signed be prima facie evidence of the facts therein stated; and

- (b) so far, there was no evidence which showed that the contents of the minutes of the ExCom meeting on 23 June 2003 provided by the former ESF Chairman had been agreed by all those who had attended the meeting. Even if there was such evidence, Audit still considered it unacceptable that:
 - (i) the ExCom had authorised the former ESF Chairman to agree at his discretion with Staff C the terms of cessation, without the need to seek the ExCom's final approval; and
 - (ii) the former ESF Chairman had not reported at an ExCom meeting following the making of an extra payment to Staff C.

Staff housing benefits

52. According to paragraphs 5.3 and 5.7 of the Audit Report, as at 1 April 2004, the ESF owned 208 staff quarters and leased 11 staff quarters (10 for senior staff and 1 for teaching staff). The total annual rent of the 10 leased senior staff quarters paid by the ESF amounted to \$6.8 million. However, at the same date, the ESF had 13 vacant ESF-owned Teaching-staff Grade quarters with an estimated total annual rental value of \$2.6 million. The Committee wondered whether such arrangement had led to wastefulness. The Committee also asked whether the ESF had formulated any plan to dispose of its surplus staff quarters.

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53. The **Acting Secretary and Chief Executive, ESF** responded at the hearing and in his letters of 4 and 10 January 2005 that:

- the 208 ESF-owned staff quarters were mainly divided into two categories, namely Senior-staff Grade quarters and Teaching-staff Grade quarters, according to the size of the quarters. Allocation of these quarters was based on the grades of the staff concerned. Over the years, there had been occasions where a vacant staff quarters was not suitable to be taken up by a staff member of a different grade. For this reason, the ESF had leased quarters from the open market for some of its staff. He did not regard this arrangement as a “waste”;
- in September 2004, four newly-appointed ESF senior staff, whose predecessors had previously been accommodated in ESF-leased quarters, had been allocated ESF-owned quarters. These ESF-owned quarters had previously been occupied by ESF teaching staff. There would be more ESF-owned quarters available in September 2005, which would also be used to accommodate senior staff. This new arrangement would reduce the total rental cost of leased staff quarters paid by the ESF; and
- the ExCom would carefully review Audit’s recommendation in paragraph 5.31(a) of the Audit Report concerning disposal of ESF surplus staff quarters, having regard to the long-term needs of the ESF and the financial security conferred by the ownership of such fixed assets. A paper on this subject would be submitted to the ExCom by June 2005.

54. The Committee noted from paragraph 5.23 of the Audit Report that, as at 1 April 2004, the ESF had leased 30 of its surplus staff quarters to ineligible staff. Audit estimated that of these 30 quarters, 21 (70%) had been let below market rent. The Committee questioned whether the ESF had sought professional advice when benchmarking the rental values of its quarters for letting to ineligible staff.

55. The **Acting Secretary and Chief Executive, ESF** said that:

- at the initial stage, the ESF had only leased its surplus quarters to its staff. Thus, it had a limited knowledge of the open property market. As a result, the level of rents of the quarters leased out by the ESF had been rather low; and

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- the ESF had changed its policy and was now leasing out its surplus quarters on the open market through estate agents. It now had knowledge of the market rental values of its quarters. Clear guidelines had also been drawn up to ensure fairness in the leasing out and the sale of ESF staff quarters. Staff had been required to follow the guidelines to ensure that ESF staff quarters were leased out at market rates and that maximum rental income was derived.

56. Paragraph 5.28 of the Audit Report stated that Audit could not find records which showed that prior approval for the sale of four staff quarters in June and July 2002 had been given by the ExCom, or by the Chairman or the Vice-chairman of the ExCom, before the signing of the sales agreement by ESF staff. The Committee queried who had handled the sale of these quarters and whether it had been done without proper authorisation.

57. The **Acting Secretary and Chief Executive, ESF** said that:

- the sale of ESF staff quarters had been authorised by the ExCom in 1994, following its endorsement of the report of a consultancy study on the issue;
- of the six ESF quarters sold between the 2001-02 and 2003-04 ESF financial years, which included the four quarters mentioned in paragraph 5.28 of the Audit Report, only the approval records of two of the quarters had been missing. He believed that similar to the sale of the other four quarters, the sale of these two quarters should have also gone through the required process of obtaining approval from the Chairman and the Vice-chairman of the ExCom. The failure of the ESF to provide evidence in this regard might be due to misplacement of these approval records; and
- the ESF had put in place a better system for keeping its records. It would ensure that in future, all sales of ESF staff quarters would require the prior approval of the ExCom.

58. The Committee also invited the former ESF Chairman to explain why the sale of the four ESF surplus quarters without prior approval had occurred. In his reply of 17 January 2005, **Mr Jal Shroff, former Chairman, ESF**, stated that:

- to the best of his knowledge, the ExCom had discussed the possibility of selling off certain old properties at an appropriate time, as these properties had involved high maintenance and was becoming uneconomical to hold on to. The Chairman, the Vice-chairman, the Treasurer and the Secretary of the Foundation had been given authority to make the final decision;

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- the ESF had also employed the services of one or more estate agents to advise it on all property transactions; and
- the auditor of the ESF, KPMG, had audited the ESF's accounts annually. He understood that all contracts dealing with the sale or purchase of ESF's properties had been properly executed as per the requirements in section 12(4) of the ESF Ordinance.

59. Figure 5 in paragraph 4.2 of the Audit Report revealed that quarters expenses amounted to \$18 million, i.e. 2% of the total staff expenditure in the 2002-03 ESF financial year. In reply to the Committee's enquiry, in his letter of 18 January 2005, the **Acting Secretary and Chief Executive, ESF** advised that of the \$18 million, 22% were quarters expenses for the ESF Headquarters.

60. According to paragraph 5.2(b) of the Audit Report, the ESF still had 143 teaching staff employed on overseas terms who were entitled to staff quarters benefits. In view of the large amount of money spent on quarters by the ESF, the Committee asked whether the ESF would consider offering housing allowance to its staff instead of providing staff quarters.

61. The **Acting Secretary and Chief Executive, ESF** said that:

- it was the long-term goal of the ESF to lease out all its staff quarters on the open market in order to maximise its income;
- the ESF had introduced a Housing Allowance Scheme in 2001 for teaching staff employed on local terms. Under the Scheme, eligible staff were paid monthly allowances calculated as a percentage of the rents or mortgage interests paid by them. After the introduction of the Scheme, the ESF's financial commitment on staff quarters had decreased significantly; and
- as regards the 143 teaching staff who were still entitled to staff quarters benefits, it would be a matter for the ExCom to consider in consultation with the new Chief Executive of the ESF.

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Staff medical benefits

62. In response to the Committee's enquiry about the progress made by the ESF in taking forward Audit's recommendations in paragraph 6.14(a) to (c) of the Audit Report, the **Acting Secretary and Chief Executive, ESF** said at the hearing and in his letter of 10 January 2005 that:

- the ESF had proceeded with obtaining proposals from insurers on the following:
 - (a) engaging a medical insurance company to provide a medical scheme for its non-teaching staff and their dependants as well as a dental scheme for all ESF staff and their dependants, with reference to similar schemes of other local educational institutions; and
 - (b) setting an annual maximum amount of reimbursable dental expenses for each member of ESF senior staff and teaching staff and each of their dependants; and
- the exercise was scheduled for completion by 28 February 2005.

63. As requested by the Committee, the **Acting Secretary and Chief Executive, ESF** undertook to keep the Committee informed of the outcome of the above exercise.

64. **Conclusions and recommendations** The Committee:

Corporate governance

- expresses concern that the Education and Manpower Bureau (EMB) has not ensured that the English Schools Foundation (ESF), which receives substantial recurrent government subsidies, adopt a high standard of corporate governance, whilst noting that the EMB only has a small representation on the Foundation and its Executive Committee (ExCom) and that the Government's policy is to not micro-manage;
- condemns the ESF Headquarters senior executive management for its failure to ensure that the ESF and its schools adopt a high standard of corporate governance and to exercise proper financial and administrative controls to achieve value for money in the operations of the ESF and its schools, as evidenced by the following:

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- (a) the administration of some ESF schools was conducted in a chaotic and negligent manner, and the school administration guidelines provided by the ESF were fundamentally inadequate, as revealed in Chapter 4 of the Committee's Report on the subject "School administration of the English Schools Foundation";
 - (b) the ESF's existing arrangement for an internal auditor reporting directly to the Financial Controller is not sufficient to help the Foundation discharge its monitoring functions effectively;
 - (c) the approval of the ExCom was not sought for extra payments made to two senior staff upon their leaving the ESF in the 2002-03 ESF financial year, and the minutes of the ExCom meeting which discussed issues concerning the termination of the employment of a senior staff member had not been entered in the ESF's minute books;
 - (d) prior approval had not been sought from the ExCom for the sale of four ESF staff quarters in June and July 2002;
 - (e) the ESF leased 10 staff quarters for its senior staff at a total annual rent of \$6.8 million, when it had 13 vacant ESF-owned Teaching-staff Grade quarters of an estimated total annual rental value of \$2.6 million;
 - (f) the ESF had been paying the rates and management fees of leased staff quarters, as long as the monthly rent (excluding rates and management fees) of the quarters did not exceed the rent entitlement of the staff concerned;
 - (g) the ESF reimbursed a senior staff member for the expenses on treatment in a first-class ward at a hospital, when the staff member was only entitled to receive treatment in a second-class ward; and
 - (h) most of the ESF staff having an annual budget for entertainment expenses used up all, or a large portion of, their budgets. Of the total entertainment expenses reimbursed to staff in the 2002-03 ESF financial year, 77% were related to staff functions;
- expresses concern that the large size of the Foundation's membership, standing at 132, is not conducive to making decisions effectively;

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- expresses serious dismay that:
 - (a) the external members of the Foundation did not constitute a majority at any of the Foundation's four annual general meetings held in the 2000-01 to 2003-04 ESF financial years. As a result, when decisions relating to ESF staff benefits were required to be made at meetings of the Foundation, there might have been an over-reliance on the internal members; and
 - (b) large percentages of internal and external members failed to attend Foundation meetings;
- expresses serious dismay and finds it unacceptable that the ESF's existing arrangement for an internal auditor reporting directly to the Financial Controller is not sufficient to help the Foundation discharge its monitoring functions effectively;
- acknowledges that:
 - (a) the Foundation has approved the draft guidelines for restructuring the governance and management of the ESF, and a task force appointed by the ExCom has started work on the proposed restructuring. The major changes proposed include:
 - (i) separating the governance and management roles; and
 - (ii) replacing the Foundation by the ESF Council as the supreme governing body of no more than 25 members with a 2:1 ratio of external members to internal members; and
 - (b) the ESF has set up an audit committee, the Chairman of which is appointed by the ExCom from amongst external members with audit, financial and accounting experience. The audit committee will report to the ExCom;
- recommends that the ESF should:
 - (a) conduct a review on the role of the Foundation Office including the need for its continued existence;

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- (b) adopt measures to ensure that external members will constitute a majority at each of the respective meetings of the Foundation and the ExCom;
- (c) issue reminders to the related organisations if the attendance rates of their representatives at Foundation meetings are low;
- (d) amend the Regulations of the English Schools Foundation to the effect that ESF staff members of the ExCom would abstain from voting on matters concerning ESF staff benefits at its meetings;
- (e) consider repealing section 10(2) of The English Schools Foundation Ordinance so that subsidiary legislation in the form of regulations made under the Ordinance is required to be published in the Gazette and tabled in the Legislative Council;
- (f) ensure that its internal audit office is staffed by well qualified and experienced personnel reporting directly to the audit committee; and
- (g) require its internal audit office to prepare annual audit programmes, to be approved by the audit committee, for conducting reviews covering major and high-audit-risk activities of the ESF, including the ESF Educational Services Limited;

Financial management

- expresses serious concern that as at 31 August 2003:
 - (a) ESF current liabilities of \$355 million were more than 11 times its current assets of \$31 million; and
 - (b) while the ESF used a bank overdraft of \$99 million to finance its expenditure, its Foundation Office and schools held bank deposits of \$17 million;
- notes that:
 - (a) the Foundation entered into an alternative arrangement with its bankers in January 2005 to offset credit balances on its accounts with any debit balances on other accounts; and

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- (b) the ESF is examining the adoption of a central cash management and payment system similar to those adopted by large commercial organisations, without the need for each ESF school to maintain its own bank account;
- recommends that the ESF should:
 - (a) take action to reduce its net current liabilities; and
 - (b) adopt a more prudent method of budgeting and avoid relying on bank overdraft;

Staff remuneration and recruitment

- expresses serious concern and has reservations about the appropriateness of the following:
 - (a) the salaries of most of the senior staff of the Foundation Office were set on the basis of the salary of a Civil Service Directorate Grade officer, and the salary scale of ESF school principals was set 14 years ago based on a similar scale in the United Kingdom;
 - (b) in the 2003-04 school year, the estimated average annual remuneration of \$947,400 per ESF teaching staff member was the highest when compared with that of the teaching staff of the seven largest private international schools in terms of student number;
 - (c) ESF teaching staff received the highest contract gratuity and responsibility allowance benefits when compared with the seven largest private international schools;
 - (d) different ESF schools adopted different policies on the allocation of responsibility allowances; and
 - (e) half of the members of the Remuneration Study Group (RSG), which comprises one ESF school principal, three ESF teaching or non-teaching staff members, two parent representatives and two community representatives, established by the ESF to conduct reviews of the remuneration packages of its teaching staff are its own staff;

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- notes that:
 - (a) the RSG will report to the ExCom in June 2005; and
 - (b) the ESF will draw up central guidelines by 30 April 2005 on the payment of responsibility allowances to teaching staff for compliance by its schools, with reference to the practices adopted by private international schools;
- recommends that:
 - (a) the ESF should take into consideration Audit's findings on the remuneration of the teaching staff of the seven largest private international schools, and immediately conduct a review of the remuneration packages of its senior staff with a view to ensuring that they are broadly in line with those of similar posts in other local educational organisations;
 - (b) the membership of the RSG should not be drawn from ESF's own teaching and non-teaching staff; and
 - (c) the ESF should implement as soon as possible new remuneration packages on newly recruited teaching staff, and on existing teaching staff over a period of time, taking into account the effects of the new remuneration packages on their financial commitments;
- asks the ESF to forward the report of the RSG to the Committee. The Committee will then invite the Director of Audit to review the report and to inform the Committee of his comments;
- expresses alarm and strong resentment over the following:
 - (a) the minutes of the ExCom meeting held on 23 June 2003, during which two resolutions were passed to the effect that the employment of Staff C be terminated and that the former Chairman of the ESF be authorised to deal with such termination, had not been entered in the ESF's minute books;
 - (b) the ExCom authorised the former Chairman of the ESF to agree at his discretion with Staff C the terms of cessation, without the need to seek the ExCom's final approval;

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- (c) the former Chairman of the ESF did not report at an ExCom meeting following the making of an extra payment to Staff C; and
 - (d) the approval of the ExCom was not sought for extra payments made to two senior staff, i.e. Staff B and Staff C, upon their leaving the ESF in the 2002-03 ESF financial year;
- urges the ESF to:
- (a) record, if given, the approval of the ExCom in its meeting minutes regarding extra payments to ESF senior staff upon their leaving the ESF;
 - (b) enter all minutes of ExCom meetings in its minute books;
 - (c) refrain from delegating to any person the authority to agree on the terms of cessation of a senior staff member without the approval of the ExCom; and
 - (d) ensure that the approval of the ExCom is obtained before making extra payments to its senior staff upon their leaving the ESF;
- expresses serious concern that in the 2002-03 and 2003-04 ESF financial years, eight ESF interview teams travelled to the United Kingdom and Australia to conduct interviews for recruiting ESF school principals and teaching staff;
- notes that the ESF:
- (a) will reduce the number of its school principals travelling overseas to interview applicants; and
 - (b) will reduce the time spent by its interview-team members overseas by conducting more video-conference interviews;

Staff housing and medical benefits

- expresses dismay that:
- (a) as at 1 April 2004, the ESF leased 10 staff quarters for its senior staff at a total annual rent of \$6.8 million. However, at the same date, it had 13 vacant ESF-owned Teaching-staff Grade quarters with an estimated total annual rental value of \$2.6 million; and

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- (b) in addition to the rent, the ESF had been paying the rates and management fees (without a specified maximum amount) of the quarters, irrespective of the rent entitlement of the staff member, so long as the monthly rent (excluding rates and management fees) of a leased quarters did not exceed the rent entitlement of the staff member concerned;
- notes that the ESF:
 - (a) has taken action in respect of Audit's recommendations on:
 - (i) accommodating eligible staff in its own staff quarters, instead of leasing quarters for them, as far as possible;
 - (ii) leasing the vacant staff quarters to its staff and outsiders to generate rental income; and
 - (iii) selecting those appropriate ESF-owned Teaching-staff Grade quarters for re-grading as Senior-staff Grade quarters for allocation to its senior staff; and
 - (b) will take action in respect of Audit's recommendations on:
 - (i) seeking the approval of the ExCom for paying the rates and management fees of ESF-leased quarters for its senior staff, irrespective of their rent entitlements; and
 - (ii) conducting a review of the rental-value level of staff quarters for its senior staff with reference to the housing benefits provided by other local educational institutions;
- recommends that the ESF should:
 - (a) consider offering housing allowance to its staff instead of providing staff quarters; and
 - (b) strictly adhere to the maximum monthly rent entitlement of its staff;

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- expresses serious concern that:
 - (a) if the ESF does not take action to reduce its surplus quarters, the number surplus to requirements will progressively increase to 199 in the 2030-31 school year, due to the retirement of teaching staff eligible for staff quarters; and
 - (b) as at 1 April 2004, of the 30 ESF-owned staff quarters leased to ineligible staff, 21 (70%) were let below market rent. Audit's estimates showed that the difference between the market rent and actual rent of these 21 staff quarters amounted to \$1.1 million a year;
- expresses astonishment and finds it unacceptable that prior approval had not been sought from the ExCom before the sale of four ESF staff quarters in June and July 2002;
- notes that:
 - (a) the ESF will negotiate with the Government on the removal of the non-assignment clauses in the government leases of its staff quarters at the Braemar Heights and at the Beacon Hill School;
 - (b) it is ESF practice to seek professional advice when benchmarking market rental values of its staff quarters for letting to ineligible staff, and the ESF will file and retain such advice; and
 - (c) in future, all sales of ESF staff quarters will require the prior approval of the ExCom;
- recommends that the ESF should formulate a policy and a plan for disposing of its surplus staff quarters;
- expresses serious concern that:
 - (a) the staff of the Foundation Office do not have the medical expertise to assess the medical claims under its in-house medical scheme for its non-teaching staff and their dependants, and under its in-house dental scheme for all its staff and their dependants, and that the two schemes require substantial staff resources; and

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- (b) the ESF does not set an annual maximum amount of reimbursable dental expenses for each of its senior staff and teaching staff and their dependants;
- expresses astonishment and finds it unacceptable that in mid-2001, an ESF senior staff member was reimbursed the expenses on treatment in a first-class ward at a hospital. However, this staff member was not entitled to receive the treatment in this hospital without the written confirmation from the doctor concerned and without the approval from the Foundation Office, and he was only entitled to receive the treatment in a second-class ward;
- notes that the ESF:
 - (a) has proceeded with obtaining proposals from insurers on the following, and the exercise is scheduled for completion by 28 February 2005:
 - (i) engaging a medical insurance company to provide a medical scheme for its non-teaching staff and their dependants and a dental scheme for all ESF staff and their dependants, with reference to similar schemes of other local educational institutions; and
 - (ii) setting an annual maximum amount of reimbursable dental expenses for each member of ESF senior staff and teaching staff and each of their dependants; and
 - (b) has agreed to seek and record the prior approval of the ExCom if the medical benefits received by an ESF staff member exceed his entitlement. In emergency cases, the ESF will seek delegated authority for the Chief Executive or the Human Resources Director to approve emergency treatment;

Entertainment expenses

- expresses serious dismay that:
 - (a) in the 2002-03 ESF financial year, most of ESF staff having an annual budget for entertainment expenses used up all, or a large portion of, their budgets. Of the total \$291,639 entertainment expenses reimbursed to these staff, 77% were related to staff functions; and

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- (b) the ESF has not set a maximum limit on reimbursable entertainment expenses allowed for each participant in each function. As a result, the amount of entertainment expenses reimbursed for each participant in a function was as high as \$1,000;
- notes that the ESF has implemented Audit's recommendations on strictly enforcing its revised policy on reimbursement of entertainment expenses which:
 - (a) prohibits reimbursement of entertainment expenses relating to staff functions; and
 - (b) requires ESF staff submitting claims to clearly state the name of each ESF participant and his capacity; for guests, their names and the organisations they represent; and the purpose of the function;
- recommends that the ESF should set up a new system so that only designated staff of the ESF may submit claims for reimbursement of entertainment expenses on a need basis; and

Follow-up actions

- wishes to be kept informed of:
 - (a) the progress of the ESF's review on the role of the Foundation Office including the need for its continued existence;
 - (b) measures adopted by the ESF to ensure that external members will constitute a majority at each of the respective meetings of the Foundation and the ExCom;
 - (c) the progress of implementing the restructuring of the governance and management of the ESF;
 - (d) Audit's comments on the RSG's report on the review of the remuneration packages of ESF teaching staff;
 - (e) the ESF's decision as to whether housing allowance will be offered to its staff instead of providing staff quarters; and
 - (f) any further development and progress made in implementing the other recommendations put forward by Audit and the Committee as well as related improvement measures.

Chapter 4

School administration of the English Schools Foundation

The objective of this audit review was to examine the administration of the English Schools Foundation (ESF) schools. The Audit Commission (Audit) had identified areas where school administrative practices could be improved.

2. At the beginning of the Committee's public hearing, **Hon Albert Jinghan CHENG** declared that he had recently been nominated by the House Committee of the Legislative Council to serve on the Foundation, i.e. the supreme governing body of the ESF, on behalf of the Council with effect from 29 October 2004. He was also an ESF school parent. He had not participated in the activities of the ESF. In order to safeguard the impartiality and integrity of the Committee, he decided that he would not take part in the examination of the three chapters in the Director of Audit's Report No. 43 relating to the ESF. He would not participate in the public hearing, nor in the discussion and compilation of the Committee's Report on these chapters. He then withdrew from the hearing.

3. **Hon Abraham SHEK Lai-him** declared that he was appointed a school council member of the South Island School of the ESF from late November 2004. As the appointment had just taken effect, he had not attended any meeting of the school council. In order that he could take part in the examination of the three chapters relating to the ESF without compromising the impartiality and integrity of the Committee, he had already resigned from the membership of the school council.

4. **Prof Hon Arthur LI Kwok-cheung, Secretary for Education and Manpower**, declared that his son had studied at an ESF school 28 years ago. **Mrs Fanny LAW, Permanent Secretary for Education and Manpower**, also declared that her two sons had attended ESF schools.

5. The **Secretary for Education and Manpower** and **Prof Felice Lieh MAK, Chairman, ESF**, respectively made an opening statement at the Committee's public hearing. Their statements are in *Appendices 32 and 33* respectively.

Corporate governance of schools

6. Paragraph 2.24 of the Director of Audit's Report (the Audit Report) stated that a school council was responsible for the overall governance of a school. To discharge their duties, school council members needed to attend regularly school council meetings. The Committee was concerned that, as revealed in paragraphs 2.26 to 2.28, in the 2001-02 and 2002-03 school years, councils of eight schools held meetings three times a year, which was

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the minimum number of meetings required by the ESF. The council of one school (School 1) had not held any meetings for a period of 23 months from 13 December 2000 to 13 November 2002.

7. Paragraph 2.32 of the Audit Report further revealed that, notwithstanding the guidance notes issued by the ESF, 12 of the 15 ESF schools did not require council members to declare their personal interests, financial or otherwise, which might conflict with their roles. The other three schools had not documented the declarations made by their council members. The Committee questioned whether the ESF agreed that these cases reflected that the administration of the ESF schools was chaotic.

8. The **Chairman, ESF** responded that:

- the ESF considered it seriously negligent on the part of some schools not to have required council members to declare their personal interests which might conflict with their roles. The ESF recognised that school councils played an important role in school governance. In the reform to be carried out, the ESF would require all school council members to declare such personal interests. It would also require all school councils to meet at least three times a year; and
- the ESF knew that there were problems with the administration of School 1 and the school principal had been dismissed in 2003. As a matter of fact, both the former ESF Chief Executive and former ESF Chairman had already resigned, thus fulfilling the requirement for accountability.

9. The Committee noted that as ESF schools were subsidised by the Government, the public were more concerned about the possible conflict of interests on the part of its school council members. The Committee asked whether the ESF had already required all school council members to declare their interests so as to ascertain whether there was any conflict of interests.

10. **Mr John Bohan, Acting Secretary and Chief Executive, ESF**, said that:

- the ESF had already sought guidance on issues such as conflict of interests through the ICAC investigations. A report had been received and three further reports were being awaited; and

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- about one-quarter of the membership of each school council were members of the school management, viz. the chairman of the council, the principal and the Secretary of the Foundation or his representative. The other constituencies were community representatives, parent representatives and teacher representatives. Therefore, even without declaring an interest directly, a member's interest was obvious as he represented his constituency.

11. In his letters of 10 January 2005 and 1 February 2005, in *Appendices 28 and 34* respectively, the **Acting Secretary and Chief Executive, ESF**, provided a summary of the progress of the actions taken by the ESF in response to Audit's recommendations and the updated position. On the question of frequency of school council meetings and declaration of conflict of interests, the Committee was advised that:

- the ESF had issued letters to school councils/ school council members reminding them of the minimum requirement for meetings, and encouraging school councils to meet six times a year and set up sub-committees to help fulfil their roles and responsibilities. In addition, Audit's recommendations would be incorporated in the revised booklet "Guidance for School Councillors". After consultation with stakeholder groups, the revised guidance would be effective by 30 June 2005; and
- declaration registers had been prepared to record the interests of school council members.

12. The Committee further asked:

- whether the resignation of the former Chief Executive and former Chairman of the ESF was due to School 1's not holding any council meeting in 23 months or other reasons; and
- about the root of the chaos and negligence in the administration of some ESF schools.

13. The **Chairman, ESF** stated that:

- the resignation of the two persons was due to many other reasons, all of which were related to mismanagement; and

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- the root of the problem was two-fold. First, there was no separation of management and governance functions in the management structure of the ESF, leading to a lack of checks and balances in the system. Second, there was a personnel problem. The lack of checks and balances had, in turn, resulted in a lack of accountability. People tended to think that they were always doing things right.

14. The **Acting Secretary and Chief Executive, ESF** supplemented that the ESF was established in 1967 with the enactment of The English Schools Foundation Ordinance (the ESF Ordinance). At that time, the ESF only had two schools which were managed according to the Ordinance and a set of regulations made under the Ordinance. The ESF had continued to grow in the past few decades, but the management structure had not changed. The management structure which had been suitable for a small organisation was no longer suitable for a big one. There was already a will within the ESF to change.

15. Given that the ESF received substantial government subsidies annually, the Committee enquired how the ESF ensured that there would be proper monitoring and control systems in future, thereby preventing the recurrence of chaos and negligence in school administration. The Committee also asked the Chairman, ESF whether, after assuming the ESF chairmanship for nine months, she was satisfied with the management of the ESF schools.

16. The **Chairman, ESF** responded that:

- as revealed in the Audit Report, the management standard of different schools varied. Some schools were well-managed while some were not. The ESF would step up its monitoring of individual schools. In addition, the principals of many schools had been changed and the new principals were very experienced in governance and management. For example, the administration of School 1 had seen significant improvement in the last 18 months after the change of its school principal. It scored high marks in the recent school review conducted by inspectors from the United Kingdom (UK);
- a reform of the ESF governance structure had begun following the Foundation's approval of the Draft Guidelines for the Restructuring of the Governance and Management of the ESF at its meeting on 9 December 2004. The most fundamental change to be effected was the separation of governance and management roles. An ESF Council was to be set up and it would

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replace the current 132-strong Foundation as the ESF's supreme governing body. The Council would comprise no more than 25 members with a clear majority of external members. Each of the members would serve on an ad personam basis, not representing any constituency. The Council would not participate in operational management. A Senior Management Team, headed by the Chief Executive and accountable to the Council, would be set up to take charge of the day-to-day running of the schools;

- a task force would be appointed by the ESF Executive Committee (ExCom) to work out the details of the restructuring in consultation with the Chief Executive designate who would assume office in February 2005. Consultation would also be held. Hopefully, the new management structure would be approved by the autumn of 2005. Amendments to the ESF Ordinance would also be necessary; and
- although there were deficiencies relating to school administration and management, ESF school teachers were of a high professional standard. ESF schools had consistently been providing high-quality education in the past 30 odd years and would continue to do so. The good examination results and high university entrance rates of ESF graduates were all evidence of the quality of education provided by ESF Schools.

17. As the Government provided a significant amount of recurrent subsidies (totalling \$299 million in the 2002-03 ESF school year) to the ESF, the Committee asked whether the Education and Manpower Bureau (EMB) had any representation on the councils of the 15 ESF schools and, if not, whether it would consider sending representatives to sit on the councils so as to step up monitoring of the schools.

18. The Committee also referred to paragraph 2.35(c) of the Audit Report in which the Secretary for Education and Manpower had said that he was concerned that the ESF Headquarters might not have given sufficient or sufficiently clear guidelines to ESF schools. The Committee enquired why the EMB had not been able to discover and rectify the ESF's management and governance problems earlier.

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19. The **Secretary for Education and Manpower** and the **Permanent Secretary for Education and Manpower** stated that:

- the EMB had a representative on the ExCom but none in the school councils. The EMB did not participate in the school management committee of individual schools, nor their day-to-day operational management, be they ESF or aided schools; and
- it was not the EMB's intention to micro-manage schools. Moreover, as government subsidies constituted only about 30% of the ESF's income, the EMB had been declined access to the ESF's finances.

20. **Mrs Cherry TSE, Deputy Secretary for Education and Manpower**, added that:

- as the EMB's representative, she attended the Foundation meeting on 9 December 2004. While the Foundation had approved the guidelines and principles for the new governance structure, the details of the restructuring were to be worked out by a task force; and
- according to section 7 of the ESF Ordinance, the Foundation should establish an ExCom and school councils. The Foundation should be the supreme governing body over the ExCom, the school councils, the schools and any committees established thereunder. The ExCom, the school councils, the schools and the other committees should comply with any resolutions made by the Foundation. Such provisions in the ESF Ordinance reflected that the ESF enjoyed a high degree of autonomy.

21. The Committee asked whether:

- after the establishment of the new governance structure of the ESF, the EMB could issue clear guidelines on school management to the ESF Headquarters to ensure that mistakes committed in the past would not recur; and
- the ESF considered it appropriate for the EMB to issue guidelines on governance and management to the ESF.

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22. The **Secretary for Education and Manpower** said that the EMB would like to co-operate fully with all school sponsoring bodies, including the ESF. As a matter of fact, the EMB did not have the statutory power to issue guidelines on the monitoring and operation of the ESF. He hoped that the ESF would want to co-operate with the EMB.

23. The **Chairman, ESF** said that guidelines should be agreed by both parties. If, through discussion, the ESF and the EMB could draw up some guidelines which were agreeable to both parties, she would not rule out the possibility of accepting such guidelines.

24. The Committee noted Audit's recommendations in paragraph 2.22 of the Audit Report that the ESF should encourage its school councils to participate actively in the management and implementation of significant school activities and consider setting up appropriate sub-committees to further their involvement in key decisions on significant school matters. The Committee enquired about the progress made in implementing these recommendations.

25. The **Acting Secretary and Chief Executive, ESF** replied at the hearing and in his letter of 10 January 2005 that the recommendations would be implemented through the revision of the booklet "Guidance for School Councillors". To meet the training needs of school council members, the existing training programme for school councillors would be extended, beginning with the course on 22 January 2005.

Strategic planning

26. According to paragraph 3.26 of the Audit Report, in developing school plans, all the 15 ESF schools had set out the criteria for assessing the performance of school programmes and the persons responsible for implementing, monitoring and evaluating the programmes. Most schools had conducted the evaluations. However, three schools had not carried out any evaluation of their programmes.

27. In paragraph 3.30, the Secretary for Education and Manpower had said that periodic external validation was a necessary ingredient of a holistic quality assurance mechanism. He also suggested that the ESF might consider inviting the relevant authorities (e.g. the Office for Standards in Education (Ofsted) of the UK and/or the European Council of International Schools) to conduct regular, periodic external evaluation of ESF schools.

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28. The Committee asked:

- why the EMB did not conduct external evaluation of ESF schools by making reference to the standards adopted by the relevant authorities in overseas countries; and
- whether the EMB wanted to play any role in the evaluation of ESF schools, as in the case of government and aided schools.

29. **The Secretary for Education and Manpower, the Permanent Secretary for Education and Manpower and the Deputy Secretary for Education and Manpower** stated that:

- the EMB only conducted inspections on public sector schools. Each of the public sector schools would be inspected in all aspects once every four years. The EMB did not have the legal power to direct how the ESF should evaluate its schools. Similarly, private independent schools and schools under the Direct Subsidy Scheme were responsible for evaluating their schools by themselves; and
- the EMB cared about the standard of governance of all schools in Hong Kong. Therefore, it would be happy to offer professional assistance to any school or school sponsoring body if requested. However, if the EMB was asked to help in evaluating the quality of the non-local curriculum offered by the ESF, it would need to discuss with the ESF before deciding on the appropriate degree of participation.

30. To ascertain whether the ESF's system of school evaluation was effective, the Committee asked:

- how the ESF conducted school evaluation; and
- about the results of the school evaluations conducted in the past and whether any school had failed to meet the required standard.

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31. The **Acting Secretary and Chief Executive, ESF** responded that:

- the ESF implemented a three-tier approach to school evaluation. At the first level, each school carried out self-evaluation and measured itself against its development plan. At the second level, the central education team conducted reviews of schools on a regular cycle to validate the school's self-evaluation. There were set parameters and criteria for such reviews. Not many such reviews had been carried out as the education team had only been brought up to full strength recently. There would be more reviews in the future. At the final level, the ESF invited Ofsted inspectors from the UK to conduct external evaluation of the schools; and
- school self-evaluation was not seen as a "pass or fail" exercise. Its purpose was to identify areas for improvement and to strive for continuous improvement. As for external evaluation, only one school had received a poor report. The Beacon Hill School had been given a very poor report by the Ofsted inspectors in 2002. After improvement programme had been implemented, the Ofsted inspectors were invited to review the school again in 2004. The Ofsted inspectors commented that the school had made enormous progress since the last inspection and it was now a highly effective school. This reflected that the ESF's quality assurance mechanism was effective.

32. In response to the Committee's request, the **Acting Secretary and Chief Executive, ESF** provided, in his letter of 20 December 2004 in *Appendix 35*, the inspection/review reports on ESF schools conducted in the past three years. In the same letter, he also provided a note written by the ESF's Education Development Director explaining the details of the three-tier approach to school evaluation, and the procedures governing the review conducted by the ESF's central education team.

33. Noting that the EMB had representation on both the Foundation and the ExCom, the Committee enquired whether the EMB had monitored the performance of ESF schools through such channels.

34. The **Secretary for Education and Manpower** and the **Deputy Secretary for Education and Manpower** said that:

- the Foundation was the supreme governing body within the ESF establishment. Its membership comprised representatives from a wide cross-section of the community, including government officials, to allow the

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ESF the benefit of the views of all sectors of the community. The ratio of EMB representatives and other members on the Foundation was 3:132. The influence of EMB representatives on the Foundation was very small;

- the EMB had one representative on the ExCom. The EMB had been participating in the ExCom on the basis of trust and co-operation. According to the ESF Regulations, the Chief Executive of the ESF or his representative sat on every school council. It was reasonable for the EMB to expect that the Chief Executive or his colleagues would bring up problems, if necessary, to the ExCom. The ExCom would not know that there were problems with the management of schools if it was not informed of such problems; and
- before attending an ExCom meeting, the EMB representative studied all the relevant documents carefully and, where necessary, sought clarification. However, it was impossible for the EMB representative to ask at every ExCom meeting whether there were any schools which had problems or had received poor evaluation reports.

35. The Committee asked whether the ESF would welcome the EMB's participation in the evaluation of its schools. The **Chairman, ESF** and the **Acting Secretary and Chief Executive, ESF** said that the ESF would welcome participation by EMB inspectors in the evaluation of its schools. There was no need to amend the ESF Ordinance in order to implement such an arrangement.

36. In his letters of 20 December 2004 and 4 January 2005, in *Appendices 35 and 36* respectively, the **Acting Secretary and Chief Executive, ESF** informed the Committee that in November 2004, the ESF and the EMB had agreed on a mutual exchange of evaluators on school inspections. On 9 December 2004, the ESF's Education Development Director had sent an invitation to the Chief Inspector of the EMB for the latter's inspectors to participate in the ESF's school reviews.

37. Having regard to the statements that the EMB could not exercise control over the ESF due to its small representation on the Foundation and the ExCom and it had to rely on the co-operation of the ESF, the Committee asked about the relationship between the EMB and the ESF in the past.

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38. The **Permanent Secretary for Education and Manpower** stated that although the EMB and the ESF had a harmonious relationship in their daily encounters, the EMB had had difficulties in obtaining information from the ESF. The scope for co-operation had widened since the current ESF Chairman had assumed office.

39. The **Chairman, ESF** stated that:

- she did not have a good understanding of the conflicts between the ESF and the EMB in the past. As both the ESF and the EMB worked for the benefits of students and for the provision of quality education, she saw a large scope for their co-operation; and
- in many aspects, the ESF and the EMB had a partnership relationship. For example, when the Canadian Overseas International College went bankrupt, the EMB had turned to the ESF to launch the rescue operation that resulted in the opening of the Phoenix International School in 2002. The Bauhinia School was opened in response to Invest Hong Kong's appeal for more international school places for the expatriate community. All these reflected that there was trust between the ESF and the EMB.

40. The Committee noted from paragraph 3.12 of the Audit Report that different schools had different planning cycles for their school development plans. It asked how the ESF would unify the cycles. The **Acting Secretary and Chief Executive, ESF** replied that the development plans produced recently had already adopted a uniform planning cycle.

Budgeting and cash management

41. According to paragraphs 4.16 to 4.18 of the Audit Report, with the exception of three schools, ESF schools adopted a bidding system to assess the funding needs of their departments. The bidding system ensured that a school's budget allocation was more responsive to its overall strategies and the competing needs of its individual departments. Audit had recommended that the ESF should require the three schools to adopt such a system for budget allocation purpose.

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42. The Committee noted that the ESF had stated in paragraph 4.19 that it would consider Audit's recommendations, having regard to the fact that school councils and principals required a degree of independence to meet the unique circumstances of each school. It appeared to the Committee that the ESF did not fully agree to Audit's recommendation. The Committee asked:

- about the ESF's position on the matter and whether it agreed that a school's adoption of a bidding system for budget allocation would not undermine the school's autonomy; and
- the ESF's criteria for determining whether a school should use a bidding system.

43. The **Acting Secretary and Chief Executive, ESF** explained that:

- the bidding system was a reasonable approach and a good way for helping the school management determine the priorities between the funding needs of individual departments within the school. However, a school's priorities were identified through the school planning process and set out in its development plan. The school would decide how to spend its funds having regard to the plan. Therefore, in determining whether to use a bidding system, an important consideration would be to avoid overturning the priorities set in the school development plan by such a system; and
- the ESF had been careful in its response to Audit's recommendation because different schools had different circumstances and different culture. Some schools were more used to bidding systems but some teachers did not like them. While this was not a reason for not accepting the recommendation, some flexibility should be given to the school council and the management to determine the extent to which the bidding system should be used.

44. The **Chairman, ESF** supplemented that only three of the 15 schools had not adopted the bidding system in their budget allocation process. It would not be too difficult to encourage them to adopt the system, particularly as two of the three school principals had already been changed. However, the unique circumstances of the schools should be taken into account in deciding how far the system should be adopted e.g. whether it should apply to major expenditure items only or to small items as well.

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45. The Committee noted from paragraph 4.36 of the Audit Report that the ESF had a high level of overdraft at the end of its financial year. It asked:

- about the reasons for the overdraft and the amount of overdraft interest paid in the past two years; and
- whether the schools had been requested to share the interest.

46. The **Acting Secretary and Chief Executive, ESF** responded that:

- the ESF had not experienced financial difficulties. The use of bank overdraft was a normal commercial operation which most firms would use. The overdraft facility had been used during the summer months when fee income was low and expenses (e.g. payment of staff gratuities and building maintenance works) were high. The duration of the overdraft in the last five years ranged from zero, three, six, up to the maximum of 59 days; and
- schools had not been asked to share the interest costs of the overdraft. The amount of overdraft interest paid in the last five years varied from \$0, \$6,000, up to the maximum of \$362,000. The amount was insignificant compared to the ESF's budget of \$1 billion.

47. The Committee noted from paragraph 4.34 of the Audit Report that each school managed its own surplus funds and maintained its own bank account. The Committee enquired whether the ESF would request its schools to place their surplus funds with it to help reduce its overdraft, as recommended by Audit.

48. The **Acting Secretary and Chief Executive, ESF** replied that:

- the ESF had not formally demanded that schools should place their surplus with its bank account at the end of the year, although this had been done on an informal basis for a number of years; and
- the ESF was considering as a matter of priority an alternative arrangement with its bankers to offset credit balances on the ESF's accounts with any debit balances on other accounts, so that the ESF would pay interest on the smallest possible amount.

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49. In his letter of 1 February 2005, the **Acting Secretary and Chief Executive, ESF** informed the Committee that the ESF had entered into the alternative arrangement with its bankers on 20 January 2005.

50. In response to the Committee's question about the reasons for the different amounts of surplus funds retained by the 15 schools, the **Acting Secretary and Chief Executive, ESF** said that:

- the ESF gave the schools the same budgets for the same class structures. The amount of surplus funds that a school retained depended on how it had decided to spend it. The ESF encouraged the schools to spend their money according to their school development plans. For instance, some schools had a saving for capital projects and might want to change all the furniture at the school. Thus, they would not spend all their saving in one year but would carry it forward. That was reasonable; and
- at the central level, the ESF could improve the situation by exercising a closer supervision of the schools' financial plans to make sure that they tied in more closely with their development plans.

Financial and administrative matters

51. The Committee was concerned that some ESF schools had not properly managed the reimbursement of travelling expenditure for official duties. As revealed in paragraph 5.33 of the Audit Report, of the six schools visited by Audit, one did not always require its staff to properly substantiate claims for reimbursement of taxi fares. As shown in Case 1, the claimant submitted claims for taxi fares amounting to \$1,450 and \$863 in the 2002-03 and 2003-04 school years respectively. However, 90% of the claims were not supported by receipts or details of the journeys. The Committee asked whether some staff members had abused the system of reimbursement of travelling expenditure.

52. The **Acting Secretary and Chief Executive, ESF** responded that:

- he could not conclude from this case whether there was an abuse. He considered the case to be a failure to keep proper records; and
- the ESF agreed with Audit's recommendation that it should require its schools to ensure that, in processing claims for reimbursement of travelling expenditure, the claimant submit receipts and details of journeys. A policy on the reimbursement of travelling expenditure was being implemented.

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53. The Committee noted from paragraph 5.36 of the Audit Report that, in the 2002-03 school year, School 14 had organised two meetings for its Senior Management Team in a hotel and the total cost was \$15,776. After realising that the cost of arranging meetings in the hotel was high, in the following school year, the school held its Senior Management Team meetings at the school sports hall. The Committee was concerned that there might have been similar cases in the past in which schools were not frugal on staff functions. The Committee asked whether the ESF could ensure that schools would practise frugality in future.

54. The **Chairman, ESF** agreed that schools should be frugal. The ESF would not be complacent even when some schools had several millions of surplus funds. It would check if there were opportunities where schools could achieve greater savings. One of the duties of the ESF's new audit committee would be to ensure value for money.

55. According to paragraph 5.21 of the Audit Report, in March 2004, the ExCom decided that the ESF should not reimburse entertainment expenses on staff functions. However, according to paragraph 5.22, the ExCom decided that the revised policy would take effect from September 2004. The Committee questioned:

- why the ExCom did not implement the revised policy immediately after it had made a decision in March 2004; and
- whether the six-month lag between the decision and the implementation of the decision indicated a lack of resolve on the part of the ESF to plug the loophole in reimbursement of entertainment expenditure.

56. The **Acting Secretary and Chief Executive, ESF** explained that:

- the previous guidelines on the use of principals' entertainment allowances had been in force since the 1980s. Under the guidelines, principals were allowed to use the funds to entertain their staff. For example, they might use funds for a Chinese New Year lunch for their office staff, or entertain their teaching staff at the end of an academic year. On 8 March 2004, the ExCom decided very quickly to change that policy and implement a new one. Subsequently, a number of principals complained bitterly that the ExCom had changed the policy in the middle of the financial year and upset their plans for specific functions. After considering their complaint, the ExCom decided that the revised policy should be implemented from the beginning of the new financial year; and

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- there was not a lack of resolve on the part of the ExCom. The concession was made because the ExCom understood the feelings of the staff affected by the new policy. Actually, the ExCom was very firmly behind the new policy which was now enforced completely across the board.

57. Noting that Audit had identified a number of problems in the school administration of the ESF and put up many recommendations, the Committee asked about the time frame for the ESF to implement Audit's recommendations, and whether the ESF had a system in place to ensure that the irregularities identified in the Audit Report would be rectified.

58. The **Chairman, ESF** said that:

- the ESF had a system of project tracking. A list of things to do against dates was considered at every ExCom meeting. Audit's recommendations would be incorporated into the list so as to enable the ExCom to check whether and when actions were taken; and
- in the past, the ESF did not have an audit committee. On 23 November 2004, the ExCom approved the establishment of such a committee. The committee would be able to help the ESF monitor its finances and improve the cost-effectiveness of its operation.

59. The Committee further asked:

- about the ESF's internal audit arrangements, including the number of staff discharging such function, before the establishment of the audit committee;
- whether the ESF considered that its Headquarters staff had the necessary financial expertise to run an organisation with an annual budget \$1 billion and whether the Foundation Office should be strengthened; and
- whether the ESF would consider other more effective and efficient alternatives of managing its finances.

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60. The **Chairman, ESF** responded that:

- at present, Headquarters expenditure accounted for 4.1% of the ESF's total budget. While the ESF's total budget was large, the management of the finances might not be too complicated as 70% of the budget was spent on teachers' pay, school expenses, etc. The ESF had a treasurer who was very experienced in financial management. When the new Chief Executive assumed office, she would have to consider the reorganisation of the Foundation Office; and
- in the past, there had not been a structure in the ESF for carrying out the internal audit function. There was only one internal auditor who reported to the Financial Controller directly. The internal auditor had no supporting staff. The newly appointed audit committee comprised three members with sound audit, financial or accounting experience. It would be responsible for examining the annual accounts and monitoring the scope and effectiveness of the work of the internal audit service. It would also consider any audit related matters, including issues arising from the Audit Report and the Public Accounts Committee's Report. The audit committee was expected to produce a preliminary report after December 2004.

61. In response to the Committee's request, the **Acting Secretary and Chief Executive, ESF**, in his letter of 23 December 2004 in *Appendix 37*, provided an ExCom paper which set out the powers and duties of the ESF's audit committee. He also advised that the audit committee would report to the ExCom.

Human resources management

62. According to paragraphs 7.18 to 7.22 of the Audit Report, the ESF had not set any guidelines on the conduct of performance appraisal of school staff. While most of the 15 ESF schools conducted regular performance appraisal of their teachers, 10 schools and 11 schools did not regularly appraise the performance of their principals and non-teaching staff respectively. In six schools, the principals had never been formally appraised. There was even one school principal whose performance had never been appraised in the past 17 years. The Committee considered that in any accountable organisation, there should be a proper system for appraising the performance of different ranks of staff, particularly the supervisory staff. The Committee queried why there was a lack of such system in the ESF and how the ESF ensured the quality of the school principals.

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63. The **Acting Secretary and Chief Executive, ESF** responded that:

- it was true that the ESF had not set up a performance appraisal programme across the board. To rectify the situation, guidelines on the conduct of performance appraisal would be established through the relevant committees of the Foundation. The ESF had also included in its development plan for the period 2004 to 2007 the setting up of a formal performance appraisal system based on the guidelines and the conduct of regular performance appraisals of school staff. The development plan would be processed through the relevant committees of the Foundation;
- although there had been a lack of a formal appraisal system, some school councils had been vigorous in checking the performance of their school principals. About a year ago, a school council conducted an exhaustive review on its principal and then recommended that the ExCom should not renew that principal's contract; and
- a performance appraisal on its own did not tell the full picture. The ESF had put in place the system of school self-evaluation and school review by the central education team. These were other pillars of the system.

64. In response to the Committee's question, the **Chairman, ESF** stated that if performance appraisals were not conducted in future, the Chief Executive of the ESF should be held responsible. In fact, in the past two years, the ESF had already dismissed those school principals whose performance was not satisfactory. The Beacon Hill School was an example. The school's performance had improved significantly after the change of the school principal.

65. The Committee further enquired about the performance appraisal system in respect of public sector schools and whether the ESF would consider adopting that system.

66. The **Permanent Secretary for Education and Manpower** said that since the promotion of school-based management in 2000, the EMB had required all its schools to put in place a performance appraisal system for staff. The school principal's performance was appraised by the school supervisor. Some school principals had even taken the initiative to conduct 360-degree appraisal on themselves so that their staff could also assess their performance.

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67. The **Chairman, ESF** said that it would not be difficult to devise and implement a performance appraisal system. What mattered was the co-operation of the staff. In the past, staff had strong objection to adopting an appraisal system. However, perhaps due to the change in culture, they had now accepted that all staff members should have their performance assessed.

68. **Conclusions and recommendations** The Committee:

- acknowledges that the objective of the audit review is to examine the administration of English Schools Foundation (ESF) schools, and the Committee has therefore focused on matters pertaining to that objective rather than the quality of education provided by ESF schools;

Overall audit observations

- expresses serious dismay that:
 - (a) there were chaos and negligence in the administration of some ESF schools; and
 - (b) the school administration guidelines provided by the ESF were fundamentally inadequate and that some schools had not taken more initiative to ensure propriety and to achieve value for money in their operation;
- acknowledges that:
 - (a) the ESF is revising the Schools' Circulars/Administrative Memoranda to help schools deal with various administrative matters;
 - (b) the ESF will provide adequate support to schools in implementing its guidelines through more systematically programmed seminars and school visits; and
 - (c) the newly created audit committee of the ESF will oversee the programme of internal audits;

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Corporate governance of schools

- expresses serious concern that:
 - (a) with the exception of one school, the composition of school councils did not include alumni;
 - (b) most ESF school councils had not specifically set out their delegated decision-making powers; and
 - (c) some school councils did not participate in major school activities as recommended by the ESF, e.g. councils of most schools did not participate in formulating staff development policies and plans (11 councils) and in setting targets and priorities for curriculum development (8 councils);
- expresses dismay that:
 - (a) the council of one school did not hold any meetings during a period of 23 months when the post of Chairman of the school council was vacant; and
 - (b) most schools did not require council members to declare their personal interests which might conflict with their roles;
- acknowledges that:
 - (a) more alumni may be invited to join school councils once alumni lists are complete;
 - (b) each school council will itemise delegated decision-making powers, and a bi-annual agenda item will be initiated by ESF representative to review the delegated powers of the school council;
 - (c) the ESF will rewrite the roles of school council members so as to encourage them to participate actively in significant school activities;
 - (d) sub-committees will be set up to help school councils fulfil their roles and responsibilities more effectively;

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- (e) the ESF has issued letters to school councils reminding them of the minimum requirement of meetings and encouraging them to meet six times a year; and
- (f) school council members will be required to declare their personal interests which may conflict with their roles, and declaration registers have been prepared to record the interests of the members;

Strategic planning, budgeting and cash management

- expresses concern that:
 - (a) some schools had not consulted their councils, non-teaching staff, parents of students, students and the ESF in the development of their school plans;
 - (b) some schools produced development plans covering only one to two years, and that different schools had different planning cycles, which were also inconsistent with the ESF's cycle;
 - (c) some schools produced less comprehensive development plans focusing only on certain areas of school activities;
 - (d) some schools had not carried out any evaluation of their programmes in accordance with their development plans;
 - (e) some schools had not regularly sought the views from some stakeholders regarding their needs and expectations;
 - (f) many schools had not developed formal procedures for budgetary planning and control;
 - (g) most schools did not provide a clear linkage of their budgets to their development plans;
 - (h) some schools did not have a bidding system to assess the funding needs of their departments;
 - (i) many schools did not submit their budgets to their councils for approval, nor regularly inform their councils of the use of school funds against the approved budgets;

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- (j) some school councils had not been involved in monitoring the use of funds against the school financial plans or budgets in the past three school years;
 - (k) some schools did not have effective control measures to ensure that budget holders managed their budgets effectively;
 - (l) some schools did not have any specific plans for using their surplus funds; and
 - (m) most schools did not have the practice of preparing cash-flow projection to help them manage their cash more effectively;
- acknowledges that:
- (a) a working group will produce guidance on school development planning to assist schools in the planning process;
 - (b) the ESF will require its schools to produce a longer-term development plan which will be in alignment with the ESF education development plan;
 - (c) the ESF will issue good practice guides to its schools to help them ensure that all significant aspects of school activities are included in their development plans;
 - (d) procedures for performing school reviews have been written to ensure that schools conduct evaluations of their programmes against their current development plans. In November 2004, the ESF and the Education and Manpower Bureau agreed on a mutual exchange of evaluators on school inspections;
 - (e) a revised self-evaluation strategy will be drafted to ensure that schools seek stakeholders' views regarding their needs and expectations, and that schools will incorporate stakeholders' views into their school development plans;
 - (f) the ESF will issue guidelines to assist schools in budgetary planning and control, and that all school councils will need a finance sub-committee to deal with budgetary matters;

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- (g) the ESF will require all schools to cost their development plans and use the cost projections in compiling annual budgets;
 - (h) the role of principals in school budgeting will be included in the revised guidance for school councils;
 - (i) from September 2005, all schools will start to report regularly their financial performance to their councils;
 - (j) the ESF will revise the guidance to school councils on the approval of school budgets and ensure consistent implementation at schools;
 - (k) monitoring the use of school funds against the approved budgets will be a regular agenda item in school council meetings;
 - (l) the ESF will remind schools of the best practice for recording and monitoring the expenses incurred by budget holders;
 - (m) the ESF will discuss with schools the strategic use of their reserves, and that schools will also have to report to school councils their need for retaining surplus funds;
 - (n) the ESF has entered into an alternative arrangement with its bankers to offset credit balances on its accounts with any debit balances on other accounts;
 - (o) training on cash-flow projections will be provided to school councils and administrative staff, where necessary; and
 - (p) the ESF will revise the guidance to school councils to provide for the setting up of finance sub-committees in schools to help monitor the use of school funds and the cash-flow position;
- urges the ESF to require its schools:
- (a) which do not have a bidding system for assessing the funding needs of their departments to adopt such a system for budget allocation purpose; and
 - (b) to establish formal policies and control procedures on virements of funds between budgets;

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Financial and administrative matters, procurement and energy management

- expresses serious dismay that:
 - (a) the ESF did not regularly revise its school circulars and administrative memoranda to ensure that they are up-to-date, and some of them had not been revised since the 1980s and 1990s;
 - (b) some ESF schools had not set up their own internal control procedures to suit their particular circumstances;
 - (c) the guidelines on internal control principles/procedures provided by the ESF to schools were inadequate, and that the internal control procedures of some schools were generally crude;
 - (d) some schools had spent too generously on staff functions;
 - (e) the ESF had not set any guidelines on the provision of staff welfare and benefits by schools, and that the provision was made solely at schools' discretion;
 - (f) the propriety in managing travelling expenditure for official duties by school staff could have been improved;
 - (g) some schools did not record and check their assets properly, thus rendering their asset registers not reliable as a tool for asset management;
 - (h) the ESF had not drawn up a set of clear and comprehensive procurement guidelines to facilitate schools in procuring goods and services at best prices;
 - (i) schools generally did not properly document the quotations obtained for the procurement of goods and services;
 - (j) schools had not, as far as possible, coordinated their purchase orders for similar goods and services and had not taken advantage of bulk-purchase discounts to achieve savings; and
 - (k) many schools had not conducted cost-benefit analysis of leasing versus outright purchase of school equipment;

School administration of the English Schools Foundation

- expresses dismay that:
 - (a) instead of charging the expenditure on staff functions to a single account to facilitate monitoring and control, the six schools visited by the Audit Commission (Audit) had charged the expenditure to different accounts;
 - (b) schools had incurred expenses for those goods and services which were desirable but not essential;
 - (c) some schools had not selected the most economical tariff available for their electricity accounts; and
 - (d) some schools had not implemented energy saving measures;
- acknowledges that:
 - (a) an audit committee was established in late November 2004 and it will report to the ESF Executive Committee;
 - (b) the ESF internal auditor is updating the school circulars and administrative memoranda;
 - (c) the ESF will place all updated and new circulars and memoranda on its website as soon as they are approved;
 - (d) the ESF internal auditor has already started to update internal control procedures for schools;
 - (e) the ESF plans to consider systematic auditing of internal control and to review the use of time in auditing;
 - (f) the ESF will revise the structure of accounts of its schools so that all entertainment expenditure is charged to one single account;
 - (g) the ESF will consider the appropriateness of setting aside an annual sum to be spent by its schools on staff functions;
 - (h) the ESF will formulate a policy on the provision of staff welfare and benefits by its schools;
 - (i) a policy on the reimbursement of travelling expenditure is being implemented;

School administration of the English Schools Foundation

- (j) the ESF will review the spending patterns of schools;
- (k) the ESF has issued revised procedure on asset recording and checking;
- (l) the ESF has issued procurement guidelines for schools;
- (m) the requirement for schools to properly document the quotations for the procurement of goods and services has been made mandatory;
- (n) the practice of central purchasing is being implemented for purchase of high-value items such as information and communication technology equipment;
- (o) the ESF will consider setting up a mechanism in the long run to coordinate the purchase of other goods and services of high volume and/or high value;
- (p) the ESF will urge individual schools to always plan and coordinate the purchasing requirements;
- (q) the ESF will give more guidance on documenting the practice of conducting cost-benefit analysis of leasing versus outright purchase of school equipment;
- (r) the ESF will require its schools to select the most economical tariff available for their electricity accounts; and
- (s) the ESF will disseminate the practices of energy saving measures implemented by some of its schools to other schools;

Human resources management, other income and support

- expresses alarm and finds it unacceptable that:
 - (a) some schools did not properly record, in an assessment form, the interviewer's assessment of an applicant showing his relative merits together with the reasons for recommending or not recommending him for appointment;
 - (b) most schools did not seek the approval of their school councils to endorse the most suitable applicant for appointment to school posts;

School administration of the English Schools Foundation

- (c) the ESF had not set any guidelines on the conduct of performance appraisal of school staff. As a result, some schools did not have a proper arrangement for conducting regular performance appraisal of their staff;
 - (d) salary increments were granted to ESF staff automatically, taking no account of work performance;
 - (e) some candidates on the ESF supply teacher list had not been registered with the Education and Manpower Bureau as registered teachers; and
 - (f) some unregistered teachers had worked as supply teachers in some ESF schools;
- acknowledges that:
- (a) the ESF has issued a school circular to require its schools to document in an assessment form the assessment of an applicant for school posts;
 - (b) the ESF recognises the need for school councils' involvement in decisions on staff appointments and will establish appointment sub-groups in school councils for ratifying the appointments;
 - (c) the guidelines on the conduct of performance appraisal will be established through the relevant committees of the Foundation;
 - (d) the setting up of a formal performance appraisal system based on the guidelines and the conduct of regular performance appraisals of school staff are stated initiatives in the ESF's Development Plan 2004-07 which will be processed through the relevant committees of the Foundation;
 - (e) the ESF agrees in principle that a mechanism for awarding salary increments to its staff should be devised;
 - (f) the establishment and utilisation of supply teacher lists is now being reviewed;
 - (g) the ESF has insisted that the policy on the employment of only qualified teachers is strictly enforced, and will give serious consideration to establishing a centrally administered supply teacher list; and

School administration of the English Schools Foundation

- (h) the ESF will implement the audit recommendations stated in paragraphs 8.8, 8.15 and 8.21 of the Director of Audit's Report;
- urges the ESF to devise a mechanism for awarding salary increments to its staff; and

Follow-up action

- wishes to be kept informed of any further development and progress made in implementing the various recommendations made by Audit and other improvement measures.

Chapter 5

Grant of land at Discovery Bay and Yi Long Wan

The Audit Commission (Audit) carried out a review of the holiday resort and residential developments at Discovery Bay (DB) and Yi Long Wan of Lantau Island. The review focused on the following aspects:

- change in concept of the DB development;
- provision of facilities in the DB development;
- changes in Master Layout Plans (MLPs) and premium implications of the DB development; and
- site boundaries of the DB and Yi Long Wan developments.

2. The Committee held four public hearings on 8, 13 and 16 December 2004 and 12 January 2005 to receive evidence on the findings and observations of the Director of Audit's Report (the Audit Report). Representatives of the Administration attended all the four hearings. At the invitation of the Committee, Sir David Akers-Jones, former Chief Secretary (CS), attended the hearing on 12 January 2005.

Evidence obtained at the public hearings on 8, 13 and 16 December 2004

Change in concept of the Discovery Bay development

3. According to paragraphs 2.5 to 2.7 of the Audit Report, in December 1973, the Executive Council (ExCo) was informed that the basic concept of the DB development was to create a self-contained recreation and leisure community with a wide variety of recreational facilities. On 6 July 1976, the ExCo was informed that the user condition restricted the use of the land to the purposes of a holiday resort with limited residential and commercial purposes. Having considered the lease conditions, the ExCo advised and the then Governor ordered that the land at DB should be granted to a developer (Developer A) for a holiday resort and residential/commercial development at a premium of \$61.5 million.

4. The Committee also noted from paragraph 2.3 of the Audit Report that the original concept of the DB development envisaged local families coming on day trips or purchasing holiday homes, and international tourists staying at budget or luxury class hotels, making use of the non-membership (i.e. public) and membership golf courses, tennis courts, swimming pools and other facilities. However, as it transpired, no public golf course or hotel was built in the DB.

Grant of land at Discovery Bay and Yi Long Wan

5. It appeared to the Committee that there had been a fundamental change in the concept of the DB development. The Committee questioned whether the change was against the ExCo's decision of 6 July 1976 and went against public interest as some facilities that were supposed to be made available to the public were eventually not provided.

6. **Mr Michael SUEN Ming-yeung, Secretary for Housing, Planning and Lands**, responded that:

- the overall concept of the DB development came into place in 1973. At that time, Lantau Island was a barren piece of land and going there was a difficult trip. The development concept of the DB site was more like a dream which the developer would like to realise. As the development was a huge investment project, the developer should be given some flexibility in the implementation process to take account of commercial considerations and other relevant factors, like the demands of the public, and be allowed to amend the development concept accordingly;
- as he was not responsible for the project, he could only rely on the documents available to understand the situation at that time. He understood that the developer considered that the original facilities were no longer timely and proposed other replacement facilities, such as a promenade and a beach. The change was approved by the then Secretary for the New Territories (SNT); and
- according to the lease conditions of the DB site, the whole site should be developed in conformity and in accordance with the MLP to be approved by the SNT. Hence, the SNT was empowered to approve changes to the facilities.

7. In response to the Committee's request, the **Secretary for Housing, Planning and Lands** provided, in his letter of 11 December 2004 in *Appendix 38*, the relevant extracts from the lease conditions of the DB site which authorised the SNT to approve subsequent changes to the development. He also said that under General Conditions Nos. 1 and 2, and Special Conditions Nos. 6, 7 and 19, the authority to approve the construction and demolition of buildings on the lot and to approve the MLP rested with the SNT.

Grant of land at Discovery Bay and Yi Long Wan

8. The Committee asked the Secretary for Housing, Planning and Lands whether he would report back to the ExCo, if he were the SNT at that time authorised by the ExCo to implement its decisions and if he were to make decisions that did not comply with the ExCo's authorisation.

9. The **Secretary for Housing, Planning and Lands** replied in the affirmative. He said that, regarding the public golf course, as replacement recreational facilities had been proposed by the developer, the SNT was empowered to approve its deletion. However, he had doubts about not reporting to the ExCo on the deletion of the hotels, as this was a fundamental change.

10. In view of the Secretary for Housing, Planning and Lands' reply, the Committee asked whether, in his opinion, the SNT had hidden facts from the ExCo and, if so, the kind of rules that the SNT had violated.

11. The **Secretary for Housing, Planning and Lands** said that:

- his understanding of the situation was based on the available documents and minutes of meetings. While he considered that it was inappropriate that the changes in the DB development had not been brought back to the ExCo, he might come to another conclusion if he knew the actual situation and all the relevant information at that time. Thus, it would not be fair for him to criticise the SNT; and
- as mentioned in the Audit Report, the officers concerned had held meetings and discussed the matter thoroughly before deciding not to report to the ExCo. They considered that the changes were still within the scope of the original ExCo approval.

12. The Committee understood from paragraph 2.6 of the Audit Report that the ExCo's permission in December 1973 for the DB development to proceed was given subject to satisfactory safeguards being included in the lease to ensure that the development would take place in accordance with Developer A's undertakings. Paragraph 2.8 further stated that on 10 September 1976, the SNT executed the lease for the DB development. However, the lease conditions did not specify the maximum and minimum gross floor area (GFA), and the gross site area of the facilities (such as the resort accommodation) to be provided by Developer A. In addition, the lease conditions did not restrict the owners to using their flats as holiday homes only.

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13. As the ExCo decided in July 1976 that the land at DB should be granted for the purpose of a holiday resort, but the lease conditions drawn up in September 1976 did not include such a restriction, the Committee asked:

- whether the Administration agreed that the lease conditions went against the ExCo's decision and, if so, why this had happened; and
- who drew up the lease conditions.

14. The **Secretary for Housing, Planning and Lands** said that, as described in paragraph 2.8 of the Audit Report, the ExCo was aware that the lease conditions did not restrict the owners to using their flats as holiday homes only. He did not know why it had happened.

15. In his letter of 8 January 2005 in *Appendix 39*, the **Acting Director of Lands** stated that the Lands Department (Lands D) had no record of how the lease conditions were drawn up or by whom.

16. As the development concept of the DB in 1976, as reflected in the lease conditions, already deviated from the concept plan approved by the ExCo in 1973, the Committee wondered whether the land grant executed by the SNT on 10 September 1976 was legal.

17. In his letter of 11 December 2004, the **Secretary for Housing, Planning and Lands** clarified that:

- the ExCo Memorandum in December 1973 intended to seek approval-in-principle for the DB development project to proceed. In crystallising the concept into a concrete proposal, the whole package was submitted to the ExCo in July 1976, with a copy of the "Particulars and Conditions of Exchange" attached as an annex to the ExCo Memorandum. This annex, except for some very minor details on the lots to be surrendered and the dates in the original blanks to be subsequently inserted, was basically the same as the eventual "Particulars and Conditions of Exchange" signed between the SNT and the developer on 10 September 1976; and

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- the ExCo noted the deviation from the 1973 concept, the safeguards in response to the requirement of the ExCo in 1973, and most importantly the terms and conditions of the Conditions of Exchange. In brief, the ExCo took the decision in July 1976 on an informed basis. Therefore, the land grant was made by the SNT in September 1976 with full authority conferred by the ExCo.

18. According to paragraph 2.24 of the Audit Report, the Secretary for Housing, Planning and Lands had said that when the ExCo approved the DB Outline Zoning Plan (OZP) on 11 March 2003, it was aware of the planning intention for DB and he did not consider it necessary to seek the ExCo's endorsement of the development concept of DB.

19. As there had been significant changes to the development concept of DB in the past 30 years and such changes were effected by amendments to a number of MLPs rather than through a proper procedure, the Committee queried why the Secretary for Housing, Planning and Lands considered that it was not necessary to seek the ExCo's specific endorsement of the change in the concept of the DB development.

20. The **Secretary for Housing, Planning and Lands** explained that:

- during the 30 years from 1973 to 2003, a lot of developments had taken place at DB and such developments were witnessed by the public. Everyone knew what its community was like nowadays. There was no question of the development concept not being clear. On the other hand, there had not been any OZP for the DB area in the past 30 years. Therefore, in 2003, the Administration sought the ExCo's approval for an OZP for the DB area which specified the zones that should be used for residential, open space or other purposes;
- he shared the concern that there was a risk of abuse of power when land use control was achieved by the MLPs and one or two officers could make decisions without being monitored. But the situation had changed significantly since then. There was now an OZP for DB. The level of control imposed by an OZP was much more stringent than that by an MLP. The OZP contained all the details as to what was allowed or not allowed. If necessary, notes could be added to an OZP to the effect that certain extra procedures would have to be gone through if changes were to be made;

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- if the land use specified in an OZP was to be changed, an application had to be made to the Town Planning Board (TPB) according to the Town Planning Ordinance. The TPB had to gazette the application and the public could lodge an objection in accordance with the Ordinance. If objections were received, the TPB had to hold hearings and go through other statutory procedures. Ultimately, approval had to be sought from the Chief Executive-in-Council. In other words, the whole process was open and statutory and the public were allowed to play a part in it; and
- the current procedure ensured that government officers could not circumvent the proper procedure or make decisions without seeking prior approval from the relevant authorities. As the purpose of going back to the ExCo had been served, there was no need to report to the ExCo again.

21. The Committee referred to paragraph 2.19 of the Audit Report in which the then Deputy Secretary for Lands and Works had said that “as flat owners were free to use their flats either as first or holiday homes, the original resort concept could not be enforced”. The then Principal Assistant Financial Secretary (PAFS) had said that as the change had been taking place, there was no point in formally approving the change in concept. The Committee asked the Secretary for Housing, Planning and Lands whether, in his opinion, the PAFS was wrong in concluding that there was no need to seek approval from the ExCo regarding the change in concept because the change had been taking place.

22. The **Secretary for Housing, Planning and Lands** responded that:

- he personally was not clear about the original resort concept. If the original concept envisaged local people buying condominium units and staying there only during the weekend but not on the weekdays, he could not understand. When people bought a condominium unit, they would just move in and it became a residential unit. This was in fact what had happened. The households in DB all lived there. From this angle, he accepted and considered it not unreasonable to say that the original resort concept could not be enforced;
- while he accepted the rationale behind that statement, he did not accept the conclusion reached by the officers. As described in paragraph 2.20(b) and (c) of the Audit Report, the then Development Progress Committee (DPC) agreed that the requirement to build one or more hotels could be made optional rather than obligatory, and the proposal to change the overall concept of the development would not require formal approval. He did not accept that

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hotels could be changed to residential units. The officers should have brought the case back to the ExCo; and

- he also considered that there were problems with the then CS's view that "there was no need to go to ExCo or the Land Development Policy Committee as the development followed on from the development so far approved and did not represent a major change in principle" (as mentioned in paragraph 2.21 of the Audit Report). There had indeed been a major change in the development concept.

23. As the Secretary for Housing, Planning and Lands also considered that there were problems with the decision of not reporting to the ExCo, the Committee questioned why he did not rectify the mistakes but allowed their perpetuation. It appeared to the Committee that by seeking the ExCo's endorsement of the OZP for DB, the Administration had tried to impose control on something wrong instead of putting it right.

24. The **Secretary for Housing, Planning and Lands** responded that:

- the Administration had already rectified the situation. The MLP, which was a loose form of control, had been upgraded to statutory control under the Town Planning Ordinance; and
- DB was already a community. It had existed for a long time and people were living there. It was impossible to start from scratch again. It was most important to understand what the problem actually was and solve it. The Administration had reported the development concept of DB to the ExCo. The ExCo knew the situation and approved the OZP.

25. The Committee further asked whether the Administration, in seeking the ExCo's approval of the OZP, had informed the ExCo of the history of the DB development and all the changes and omissions that had occurred since 1973, or whether it had only informed the ExCo of the latest situation of DB.

26. The **Secretary for Housing, Planning and Lands** replied that the subject of the paper to the ExCo was the OZP, not the DB development. It did not contain the same amount of details as the Audit Report. The Administration's intention was to inform the ExCo of DB's latest development. Given the Committee's view, he would consider making a separate report to the ExCo on the matter if necessary.

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27. Subsequently, the **Secretary for Housing Planning and Lands** informed the Committee that after consideration, in order to put the matter beyond doubt, he decided that he would go back to the ExCo to seek its endorsement of the development concept of DB.

28. According to paragraphs 2.11 and 2.14 of the Audit Report, MLP 4.0, which changed the character of the development from a holiday resort to a garden estate, was approved by the SNT. As mentioned in paragraph 2.21, it was the CS who decided that there was no need to seek the ExCo's approval. Noting that the Secretary for Housing, Planning and Lands had mentioned the risk of abuse of power, the Committee asked whether the decisions as described in these two paragraphs were cases of abuse of power, given that the SNT and the CS were the same person, Sir David Akers-Jones.

29. The **Secretary for Housing, Planning and Lands** responded that when he mentioned the risk of abuse of power, he was referring to the possibility of such a loophole in the system. He did not mean that any officer had abused his power. Abuse of power was a very serious accusation and it had a high legal threshold. With the information he had in hand, he could not make a judgement that someone had abused his power.

30. As requested by the Committee, the **Acting Director of Lands**, in his letter of 8 January 2005 in *Appendix 39*, provided the minutes/notes of the meetings held on 18 October 1977 and 19 October 1977 relating to the consideration of MLP 4.0 by the Administration. The **Secretary for Housing, Planning and Lands**, in his letter of 10 January 2005 in *Appendix 40*, provided the minutes of the DPC meetings held on 10 October 1985 and 14 November 1985 concerning the Administration's decision at that time that there was no need to report to the ExCo regarding the change in the concept of the DB development.

31. To ascertain whether it was common in the past for the Government to accept changes in the development concept of a project, the Committee asked:

- whether, in the 1970s and 1980s, there was any project which, similar to the DB development, had undergone a change in development concept from a holiday resort with recreational and leisure facilities to a first-home community; and
- whether there was any project the development concept of which was not allowed to be changed.

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32. The **Secretary for Housing, Planning and Lands**, in his letter of 10 January 2005, advised that there was no other project for recreational and leisure facilities similar to that of the DB granted in 1970s and 1980s. Therefore, the question of whether changes in development concept of such development had been approved or rejected did not arise.

33. The Committee noted from paragraph 2.14(a) of the Audit Report that one of the reasons for the SNT to approve MLP 4.0 was that “the basic concept of building a resort was continued”. The Committee asked whether, in the Lands D’s opinion, the changes proposed in MLP 4.0 were changes to the basic concept of the DB development.

34. In his letter of 8 January 2005 in *Appendix 39*, the **Acting Director of Lands** stated that the resort concept was still a substantial element in MLP 4.0, but the introduction of “garden houses” appeared to have introduced the likelihood of permanent residence in a significant amount of the GFA. Although this did not conflict with the conditions of grant, there was a change.

35. According to paragraph 2.26 of the Audit Report, the Director of Lands agreed with Audit’s recommendation that he should, for a land grant for a development involving a particular concept, incorporate effective provisions into the lease conditions or other contract documents so that the provisions would be enforceable for implementing the concept. The Committee asked how the Lands D would implement the recommendation.

36. **Mr Patrick LAU Lai-chiu, Director of Lands** explained that when there were special development projects, the Lands D issued project agreements which stated the development concepts and how they could be realised. The project agreements and the lease conditions were back to back.

Provision of facilities in the Discovery Bay development

37. According to the lease conditions of the DB site, the grantee should erect, maintain and keep in use on the site a leisure resort and certain “minimum associated facilities”, which should include a public golf course and a cable car system. However, Developer A subsequently applied for the deletion of the public golf course and the cable car system. In February 1982, the then Secretary for City and New Territories Administration (SCNTA) approved MLP 5.0, by which the public golf course was deleted. In February 1985, the Director of Lands approved the deletion of the cable car system upon the approval of MLP 5.1.

Grant of land at Discovery Bay and Yi Long Wan

38. Against this background, the Committee queried why:

- as the public golf course and the cable car system were approved by the ExCo and specified in the lease conditions, the SCNTA alone could decide that the facilities could be deleted; and
- the Lands D at that time had not acted in accordance with the lease conditions but approved the deletion of the facilities.

39. The Committee also referred to paragraph 3.6 of the Audit Report in which the then Principal Government Land Agent (PGLA) said that because of the importance attached to the golf course proposal, the public golf course requirement was more particularly referred to in a special lease condition. The Committee questioned why, as mentioned in paragraph 3.9, the City and New Territories Administration (CNTA) had not carried out a research on the demand for golf facilities before it approved the deletion of the public golf course which was a special facility in the entire development.

40. The **Secretary for Housing, Planning and Lands** responded that:

- as described in paragraph 3.8 of the Audit Report, there had actually been discussions within the Government regarding whether a modification of the lease conditions was required to reflect the deletion of the public golf course. The then Recreation and Culture Department (R&CD), which was responsible for the policy on recreational facilities, had been consulted and it welcomed the proposal that other recreational facilities would be provided in place of the public golf course. On the other hand, the Highways Department representative objected to the deletion. Paragraph 3.10 further mentioned the view of the Registrar General's Department that there was no need to modify the lease conditions; and
- all these reflected that discussions had been held among the relevant departments and the responsible officers had gone through certain procedures. The decisions were not made by one single person. However, he did not have any information to show why such decisions were made or the basis for the decisions.

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41. The **Director of Lands** responded that:

- a lease usually contained many terms and provisions which were not laid down by the Lands D alone. Nowadays, when the Lands D received a request for lease modification, it would look at the terms that needed to be modified and consult the relevant policy bureau or department. If necessary, it would convene an inter-departmental meeting to consider the request. In other words, the decision would not be made by a single department. However, there had to be a department to formally approve the lease and the Director of Lands was responsible for formally signing the lease;
- the same mechanism should be applicable at that time. That was why the then Lands D did consult the R&CD. The R&CD welcomed the proposal. The Lands D had not overruled the recommendation of the R&CD because the latter was the expert department on whether a public golf course was required. He believed that the then Director of Lands had made the decision at the time, on behalf of the Government, upon the advice of the R&CD. It was not that the Lands D had made a decision unilaterally to delete those items; and
- as the R&CD had stated that it welcomed the proposal, a research on the demand for golf facilities were not necessary. As a matter of fact, the decision to delete the public golf course was made in February 1982. The suggestion of a research was put up after the decision had been made.

42. According to paragraphs 3.7 and 3.8 of the Audit Report, inter-departmental discussions were held in mid-1982 after the SCNTA had approved MLP 5.0 which removed the requirement for the provision of the public golf course. The Committee asked whether there were records showing that there had been inter-departmental discussions on the matter before MLP 5.0 was approved.

43. In his letter of 8 January 2005, in *Appendix 39*, the **Acting Director of Lands** stated that there were no records of any inter-departmental discussions on the deletion of the public golf course prior to the approval of MLP 5.0 in February 1982. There were also no documents showing why the then Commissioner for Recreation and Culture welcomed the proposal that other recreational facilities would be provided in place of the public golf course.

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44. Given that the public golf course was specified in a special lease condition, the Committee enquired whether the Administration agreed that the lease conditions should have been modified before deleting the requirement to provide the golf course.

45. The **Director of Lands** stated that:

- according to the memorandum issued by the then Registrar General (Land Officer) to the then Government Land Agent (Disposal) on 3 March 1983 (in *Appendix 41*), it was the former's view that there was no need to modify the lease conditions; and
- the arrangement for control of land use at that time was very different from that of today. When the land at DB was granted, it was stated clearly in the lease conditions that the scale of development of DB and other restrictions were to be controlled by the MLPs in addition to the lease conditions. In other words, the MLPs and the lease conditions of the DB site had equal standing and effect. Hence, the MLPs could be amended without modifying the lease conditions. However, this might not be the arrangement nowadays.

46. As the public golf course was proposed by the developer and later removed upon the developer's application, the Committee questioned why the Government seemed to have allowed the developer to have his way every time.

47. The Committee further referred to paragraph 3.16 of the Audit Report which mentioned that the provision of the cable car system was mandatory under the lease. However, in September 1982, Developer A said that the popularity, safety factor and the financial viability for this system were open to question. The system was no longer necessary as all the major roads in DB had been built. In January 1983, the Government agreed to the deletion of the system. The Committee noted that cable car was not a new invention. The tram system had been in use in the urban area for a long time. Back in the 1980s, there was already a cable car system in the Ocean Park. The Committee asked why the Government had accepted the reasons put forward by the developer.

48. The Committee was also aware that there had been recent media reports which related the whole issue to political decisions. It was reported that the colonial government had accepted changes to the MLPs out of the fear that, if the DB project failed, it could be taken over by a bank tied to the former Soviet Union. The Committee asked whether the Administration had any information pointing to a political transaction.

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49. The **Secretary for Housing, Planning and Lands** and the **Director of Lands** stated that:

- the project was massive and the development period was very long. Initially, the developer came up with a concept. However, during the implementation, a lot of changes took place in society and things kept evolving. Thus, the Government had to accept some changes. Actually, the SNT, and later the SCNTA, was empowered by Special Condition 6(b) of the lease conditions to approve amendments to the MLPs;
- the developer allowed non-members to play in the existing private golf course in DB on Mondays, Tuesdays and Fridays by prior arrangement. Perhaps the responsible officers decided to remove the requirement for the provision of the public golf course because of the lower demand for such facility at that time. While a lot of people were interested in playing golf nowadays, people might not be as enthusiastic back in the 1980s;
- regarding the cable car system, it seemed that the Government accepted the views of the developer at that time. But the reason behind the decision was not known; and
- the file records that they had gone through did not contain any information concerning political consideration.

50. The Committee noted that while the public golf course and the cable car system had been deleted in the MLPs, they were still provided in the lease conditions for the DB site. It asked whether the Administration might now amend the MLP again to include these facilities in the MLP.

51. The **Director of Lands** said that the MLPs and the lease conditions of the DB site had the same status and were equally binding. When a certain item was deleted in the MLP, the item could be regarded as having been deleted from the lease. In his letter of 8 January 2005, in *Appendix 39*, the **Acting Director of Lands** added that the Administration could not unilaterally amend the MLP.

Grant of land at Discovery Bay and Yi Long Wan

Changes in Master Layout Plans and premium implications

52. According to paragraphs 4.2 to 4.7 of the Audit Report, in 1979, Developer A agreed to replace the public golf course by some active public recreational facilities in the same area or elsewhere within the DB site. However, as far as could be ascertained from the Lands D's records, Audit could not find a list of the specific replacement public recreational facilities, showing the site area and locations, which Developer A should provide. There was also no verification of the specific as-built facilities with those agreed with Developer A to ensure that they had in fact been built. The Committee asked why the Administration had not been serious in dealing with the matter.

53. The **Secretary for Housing, Planning and Lands** responded that the incidents were not acceptable and should not have happened. No matter whether it was land matters or other government activities, there was always a need to record the things to be done clearly because the Administration had to make sure that the relevant objectives were met at the end of the day.

54. According to paragraphs 4.17 and 4.21 of the Audit Report, the Lands D had only charged premium for the changes made in MLPs 5.6, 5.7 and 6.0E1. It had not charged premium for the changes made in the MLPs after the land grant and prior to 7 June 1994 (i.e. MLPs 3.5, 4.0, 5.0, 5.1, 5.2, 5.3, 5.4 and 5.5). The Government might have suffered loss in revenue. In addition, the Lands D had not documented the reasons for not assessing and/or charging premium for those MLP changes. The Committee asked whether the Administration considered this acceptable.

55. The **Director of Lands** responded that, having constructed the situation at that time according to the file records, he had the following understanding:

- a Land Policy meeting was held on 25 May 1987 to consider, inter alia, the Land Policy Meeting Paper LPM 3/87 (the paper and minutes of the meeting are in *Appendices 42 and 43* respectively). The paper stated that MLP 3.5 permitted a total of 592,716 m² of GFA to be used for residential, commercial and hotel uses which, from land perspective, was called revenue-generating GFA. When MLP 3.5 was approved as MLP 4.0, the GFA had to be converted from the imperial system to the metric system. In the process, the total permitted revenue-generating GFA was wrongly converted to 607,000 m². The correct figure should have been 608,510 m². So, in MLP 4.0, there was a shortage of 1,510 m². The mistake was not discovered in the subsequent amendments to the MLPs, including MLPs 5.0, 5.1, 5.2, until the relevant government departments considered MLP 5.3;

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- after lengthy discussion, the Lands Policy meeting decided that from then onwards, the figure 608,510 m² would be used as the basis for future negotiations over any premium to be charged for increases in GFA in future;
- he deduced that the position at the time was that if the revenue-generating GFA of DB exceeded 608,510 m², then a premium would be charged. However, if there was an increase in GFA but the total permitted GFA of 608,510 m² was not exceeded, premium would not be charged. His deduction was supported by a letter dated 25 November 1989 from the then Director of Buildings and Lands to Developer A (in Appendix IV to the Acting Director of Lands' letter of 8 January 2005 in *Appendix 39*);
- no premium had been charged for the changes made in MLPs 5.3, 5.4 and 5.5 because the total revenue-generating GFA did not exceed 608,510 m². When it came to MLPs 5.6, 5.7 and 6.0E1, the Lands D had charged a premium because that figure was exceeded; and
- as regards why the Lands D had not charged any premium although there was a change in land use, thereby bringing about a change in value, the file records did not mention whether there were any guidelines at that time stating that an increase in land value due to a change in land use was a consideration for charging a premium.

56. The Committee noted from paragraph 4.15 of the Audit Report that in October 1985, when the proposal to delete the public golf course and the cable car system was discussed by the DPC, it was stated in the DPC discussion paper that modification of Special Condition 5(b) of the lease conditions would be required. The paper also mentioned that a formal modification of the lease conditions subject to consideration of a premium and administrative fee should be made for the changes. The Committee queried why, despite the DPC's view, the Lands D had not assessed the premium implications of the changes in the MLPs.

57. The **Director of Lands** responded that the matter considered by the DPC was whether a premium should be charged if there was a modification of lease conditions. In fact, the public golf course and the cable car system had been deleted from the MLP, not from the lease conditions. The lease conditions had not been changed on the advice of the Registrar General. As mentioned in the Audit Report, the DPC had not expressed any opinion on the modification of the lease conditions when it agreed with the changes made in MLP 5.1. Perhaps that was why premium was not discussed.

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58. According to Table 3 in paragraph 4.16 of the Audit Report, some of the changes in the MLPs involved change in land use and increase in the GFA of housing accommodation. The Committee wondered why the Administration had not charged premium for the change in land use and the resulting enhancement in land value. The Committee further asked whether the Administration had the determination to recover the premium from Developer A according to the existing policy.

59. The **Director of Lands** responded that according to legal advice, the Government had given approval for changing the MLPs and a premium was not charged at that time. There would be great difficulties if the Government was to ask the developer to pay a premium after more than 20 years. This would violate the estoppel principle.

60. The **Secretary for Housing, Planning and Lands** responded that he had strong determination in going through all relevant information to see if the Administration had omitted to charge any premium that should have been charged. However, the Administration would take the matter forward only after this first stage was completed and if there was evidence showing that there was such a problem. The Administration could not recover something that was not substantiated.

61. To understand the policy in the 1970s and 1980s on the charging of premium when approving change in land use, the Committee asked:

- whether the relevant land authorities at that time were empowered to charge premium when approving changes in MLPs;
- whether the policy at that time allowed the relevant authorities not to charge premium on change in land use when approving changes in MLPs;
- whether there were cases in the 1980s in which premium was not charged on similar change in land use; and
- whether it was normal practice in the 1970s and 1980s that premium would not be charged as long as the GFA of a site did not exceed a certain limit even though there was a change in land use.

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62. In his letter of 8 January 2005, in *Appendix 39*, the **Acting Director of Lands** informed the Committee that:

- the authority to charge premium was not lacking;
- the policy on changes of use requiring lease modifications had remained constant, in that where such a lease modification would bring about an increase in value, a premium was charged. In respect of changes in use involving only a change in MLP, however, it was apparent that in the 1970s and 1980s no charge was made (as long as there was no increase in total GFA). There was no specific policy statement on this issue at that time;
- the Lands D had no record of premium being charged for an MLP change not involving a lease modification in the 1980s; and
- in the 1970s and 1980s, it was the normal practice not to charge premium for changes to MLPs which did not require a modification of the lease as long as there was no increase in total GFA.

63. The Committee invited Audit's comments on the Acting Director of Lands' reply that it was the normal practice in the 1970s and 1980s not to charge premium for changes to MLPs which did not require a modification of the lease as long as there was no increase in total GFA. In his letter of 1 February 2005, in *Appendix 44*, the **Director of Audit** advised that:

- *“Normal practice” not substantiated:* As far as could be ascertained from the Lands D's records, the Acting Director of Lands' statement was not substantiated in either the Lands Administration Office Instructions (LAOI) or the Revenue Assessment Manual (RAM). Audit was not aware of any approval from the ExCo for such “normal practice”;
- *Increase in total GFA and change in user mix:* The increase in total GFA and changes in user mix (mentioned in Note 3 in paragraph 2.8, paragraph 2.10 and Table 3 in paragraph 4.16 of the Audit Report), were as follows:

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User	MLP 3.5 GFA (m ²)	MLP 4.0 GFA (m ²)	MLP 4.0 increase/ (decrease) over MLP 3.5 GFA (m ²)	
(a) Housing accommodation	–	524,000	524,000	
(b) Resort accommodation	401,342	–	(401,342)	} (Note 1)
(c) Hotel accommodation	140,284	32,000	(108,284)	
(d) Commercial	51,097	45,000	(6,097)	
(e) Others	<u>41,341</u>	<u>40,600</u>	<u>(741)</u>	
Total GFA per MLP	634,064	641,600	7,536	
Discrepancy (Note 2)			<u>1,510</u>	
Increase in total GFA			<u>9,046</u>	

Note 1: In April 1977, the ExCo was informed of the GFA of the resort and hotel accommodation.

Note 2: According to the Lands D, the discrepancy was due to a conversion error (from square feet to square metres).

- as shown in the above table, the approval of MLP 4.0 in January 1978 had resulted in:
 - (a) an increase in total GFA over that approved in MLP 3.5; and
 - (b) a significant change in user mix, particularly the deletion of the resort accommodation and the addition of 524,000 m² housing accommodation GFA.

The then New Territories District Planning Division of the Town Planning Office had also commented in mid-October 1977 that there was a corresponding increase of residential areas;

- while the then SNT was delegated the authority to approve changes to MLPs, Audit was not aware that he had been given any explicit authority to not charge premium if there was enhancement in value arising from changes in lease conditions;

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- *Changes to MLP:* the Director of Lands had stated that the MLPs and the lease conditions of the DB site had equal standing and effect. Therefore, any modification of the MLP (such as the increase in the total GFA and the significant change in user mix in MLP 4.0 over MLP 3.5) would in substance tantamount to a modification of the lease conditions;
- *Deletion of public golf course and cable car system constituted lease modifications:* The provision of the public golf course and the cable car system was a mandatory requirement stipulated in Special Condition 5(b) of the lease of the DB development. Moreover, because of the importance attached to the public golf course proposal, the developer's responsibility to maintain the public golf course was more particularly referred to in Special Condition 54(c) of the lease. In the circumstances, the deletion of the public golf course in MLP 5.0 in February 1982 and the cable car system in MLP 5.1 in February 1985, constituted modifications of the lease conditions; and
- to conclude, Audit maintained its view that the Government might have suffered losses in revenue. The Lands D had not assessed the implications, financial or otherwise, of the deletion of the facilities, and the reasons for not assessing and/or charging premium for the changes in those MLPs were not documented.

64. In order to ascertain whether the Government had suffered losses in revenue, the Committee asked:

- about the total revenue generated by the entire DB development in the past 30 years; and
- for an estimation of the premium involved in each of the changes made in the MLPs prior to 7 June 1994 based on the market conditions at the time when the changes were made.

65. In his letter of 10 January 2005, the **Secretary for Housing, Planning and Lands** advised that as far as the Lands D was concerned, a total of some \$2.09 billion had been collected in respect of the DB development. This figure comprised land premium, government rent up to 1996-97 (government rent was collected by the Rating and Valuation Department after 1997), premium charges for changes to the MLP, waiver fees and rental for short term tenancy (STT) and administrative fees.

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66. On the question of premium, the **Director of Lands**, in his letter of 25 January 2005 in *Appendix 45*, stated that:

- on the basis of file records, the original premium of \$61.5 million charged for the DB development land exchange was based on an estimated sale price of \$300/ft² which was applied to the total GFA for all the uses permitted (i.e. without distinguishing between commercial, residential and hotel);
- this valuation was supported by the analysis of the two public land auctions in Mui Wo conducted in 1973. These land auctions produced a ground floor shop value at about \$300/ft² and upper floor residential flat value at about \$200/ft² which the Lands D believed were adopted as the benchmark for valuing the DB at that time. Moreover, the unit land cost (commonly known as accommodation value) derived from the estimated sale price also compared favourably with that of two land exchanges in Mui Wo and Cheung Chau for hotel development in the early 1970s; and
- the application of \$300/ft² to the total GFA permitted under the approved MLP meant that the enhancement, if any, in subsequent changes to the MLP had already been captured in the approval of the first MLP by adopting the highest use value among the mix in calculating the land premium to be paid by the developer upfront for the grant. This had obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted GFA was not exceeded. That being the case, the Lands D did not consider it appropriate to compute the premium for each of the changes made to the MLP prior to 7 June 1994.

67. In response to the Committee's request, the **Director of Audit**, in his letter of 1 February 2005, commented that:

- according to Section 7 of the Land Administration Policy on Modification and Administrative Fees (amended on 1 April 1984), as a general rule for lease modification, "Premium will normally be required representing the difference in value between the lot as formerly restricted and as modified The general principle relating to the assessment of modification premia is that the lessee must pay for any enhancement in the value of the lot deriving from the modification". In other words, premium assessment should be done by comparing the current land values under the modified lease conditions (and/or MLP) and the original lease conditions;

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- having regard to the above general rule, the unit land cost (accommodation value) and the valuation benchmark (i.e. ground floor shop value) adopted at the date of execution of the lease conditions were not relevant to the premium assessment of a lease modification at a later date; and
- in view of the above, Audit did not concur with the Director of Lands' views that "adopting the highest use value among the mix in calculating the land premium to be paid by the developer upfront for the grant had obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted GFA was not exceeded.". Furthermore, there had been an increase in total GFA and changes in user mix since the change from MLP 3.5 to MLP 4.0. Audit therefore also did not concur with the Director of Lands' conclusion that he did "not consider it appropriate to compute the premium for each of the changes made to the MLP prior to 7 June 1994".

68. In his letter of 16 February 2005, in *Appendix 46*, the **Director of Lands** responded to the Director of Audit's comments on the charging of premium in the present case contained in his letter of 1 February 2005, as follows:

- the basic considerations underlying the handling of the DB case in the 1970s and 1980s were:
 - (a) since the subject land grant contained an MLP clause to enable the Administration to exercise detailed control over the implementation of the development within the approved parameters stipulated in the lease conditions, premium would not be charged on each and every occasion when amendments to the MLP were made, unless such changes would require lease modification and/or there was an increase in the total permitted GFA (for revenue generating purposes). This practice adopted for cases under similar situations in that period was also adopted in this case;
 - (b) the premium for the land transaction concerned was calculated according to the highest land use value among any of the permissible mix as specified in the MLP. This meant that Government was able to capture the highest revenue income at the outset without any downside risk due to fluctuations in the property market. On the part of the developer, the certainty in its financial commitment under the land transaction plus the flexibility of being able to make more timely decisions in response to

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changes in market conditions would arguably be essential for a project of this magnitude and nature; and

- (c) on the above basis, the manner that the original premium was calculated had obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted (revenue-generating) GFA was not exceeded;
- regarding Audit's comments on the "normal practice" in the 1970s and 1980s, the Lands D's response, as provided in the letter of 8 January 2005, was factual to the best of its knowledge. Most land administrative practices evolved over time in the light of experience and changes in circumstances and the Lands D did not come into existence until 1982. The Lands D's understanding of the practice prevailing two to three decades ago should not be negated simply by the Director of Audit being unable to locate any written material to substantiate its statement;
 - regarding Audit's comments on "increase in total GFA and change in user mix", it had to be stressed that, despite the changes to the GFA in various MLPs up to MLP 5.5, the revenue-generating GFA did not exceed the permitted maximum of 608,510 m² as determined by the Land Policy meeting held on 25 May 1987;
 - Section 7 of the Land Administration Policy on Modification and Administrative Fees remained a valid rule for general application for assessing premium arising from lease modifications. The case in question was not inconsistent with this section; and
 - in conclusion, the Lands D strongly disagreed with the views held by the Director of Audit in his letter of 1 February 2005, especially that "the Government might have suffered losses in revenue", having regard to the manner that the original premium was calculated. The Director of Audit's suggestion that a series of further premiums should have been collected for changes in the development mix up to 608,510 m² (revenue-generating GFA) would constitute double charging since the facts established indicated that the developer, at the time of the original grant, had already paid for the flexibility of varying the development mix subsequently reflected in successive MLPs.

69. The Committee asked whether the CS, who decided that there was no need to seek the ExCo's approval for the change in concept, was behind the decision of not charging premium for the changes in the MLPs.

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70. The **Secretary for Housing, Planning and Lands** and the **Director of Lands** responded that:

- as mentioned in the Audit Report, the DPC had a meeting in October 1985. The chairman of the DPC was the then Secretary for Lands and Works, Mr Todd, and the meeting was attended by representatives of various government departments. The DPC agreed on a number of things collectively. But there was no decision on lease modification or premium payment; and
- there was no record of any person specifically approaching the CS for an instruction as to whether a premium should be charged. Therefore, it could not be concluded that the CS should be held responsible for the decision made at that time.

71. According to paragraph 4.18 of the Audit Report, the Lands D's RAM stated that "When giving approval to Master Layout Plan, which leads to giving consent/variations of restrictions under certain conditions, the Director may impose conditions (including payment of fee and appropriate admin. fee) as he considers appropriate". However, Audit noted that the RAM did not provide a definition of "certain conditions", and the word "may" implies that the charging of fee was discretionary. It was not clear under what conditions, and how, such discretion would be exercised. The LAOI also did not stipulate clearly that the Lands D should charge MLP approval fee.

72. The Committee asked whether:

- some government official had exercised discretion over the charging of premium in the case of DB, resulting in losses in government revenue; and
- the word "may" in the RAM should be changed to "shall" so that the charging of fee was mandatory rather than discretionary.

73. The **Director of Lands** clarified that:

- according to legal advice, "certain conditions" referred to certain lease conditions, not certain circumstances. The whole sentence in the RAM meant giving approval to MLP under certain provisions of the lease, not in a certain situation for discretionary power to be exercised. Thus, there was no question of the Director of Lands being given too much discretionary power; and

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- the Director of Lands did need some flexibility in discharging his duty as it was hard to foresee all factors relevant to land matters. While the Director of Lands was given some discretionary power, it was not exercised casually. The exercise of such flexibility was not subject to personal preference and was properly recorded. Moreover, there were monitoring mechanisms in place nowadays, such as the Independent Commission Against Corruption, Audit, the Ombudsman, etc.

74. The Committee asked how the Lands D would amend the RAM and LAOI in response to Audit's recommendations in paragraph 4.23 of the Audit Report. The **Acting Director of Lands** provided the wording of the amendments to the RAM and LAOI in his letter of 8 January 2005 in *Appendix 39*.

Site boundaries of Discovery Bay and Yi Long Wan developments

Setting out of site boundaries

75. According to paragraph 5.5 of the Audit Report, in September 1976, the Government granted the DB site to Developer A. However, up to July 2004, i.e. after a lapse of 28 years after the land grant, the Lands D had not yet set out the site boundaries of the DB development. The Committee questioned the Lands D's reason for not setting out the site boundaries.

76. The **Director of Lands** and **Mr AU YEUNG Ping-kwong, Deputy Director of Lands/Survey and Mapping**, stated that:

- the then Public Works Department was responsible for setting out the site boundaries. After some boundaries had been set out, the work was suspended in 1977 for more than half a year due to an industrial action of the surveying staff; and
- it was not the case that there were no boundaries of the site. Actually, the boundaries were shown on the plan relating to the land grant. However, as the site was very big, the surveying staff had not yet put boundary marks on ground in order to avoid possible abortive work.

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77. On the reason for the long delay in completing the work, the **Director of Lands** said that:

- in a letter of 16 March 1983 from the then Director of Lands, Mr Todd, to Developer A (in Annex F of Appendix II to the Acting Director of Lands' letter of 8 January 2005 in *Appendix 47*), it was stated that “ the present MLP No. 5 is not subject to Government survey and can only be a guide to your Company's present and future intentions. In other words neither plan at this stage is really satisfactory. It may therefore be more appropriate to await the issue of the Crown Lease at the end of the whole development whereupon Government will carry out a survey of the lot boundaries.”. It appeared that it was the Government's position in 1983 that as the DB project was still going on, the Government should resolve all the discrepancies upon the completion of the whole project. At that time, the Government thought that the development would be completed in the not too distant future. When a Crown Lease was produced, the matter would also be dealt with;
- as it transpired, the development was still going on and the pegging had not yet been done. However, in 2002, there was a complaint about the occupation of government land by the DB golf course. Despite the fact that the development was still in progress, the Lands D considered that it should set out the boundaries. It would complete the dimension plan by mid-January 2005. Lands D staff would then place the boundary marks on the site accordingly, thus setting out the site boundaries; and
- there was no record to show why no one had raised the need to set out the site boundaries during 1983 and 2002. Perhaps the Lands D staff had relied on the 1983 letter and wanted to set out the boundaries upon the completion of the entire project.

78. In his letter of 24 January 2005, in *Appendix 48*, the **Director of Lands** informed the Committee that the dimension plan survey for the DB development boundary had been completed by the District Survey Office/Islands, and the setting out work would be completed by the end of March 2005.

79. The Committee further asked:

- whether the Lands D considered that it was wrong not to set out the boundaries in the past three decades as this might have resulted in encroachment on government land; and

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- when the Lands D would complete the setting out of boundaries for sites granted but the boundaries of which had not yet been set out.

80. The **Director of Lands** responded that:

- he did not know the actual thinking of the responsible officials at that time. As time had advanced and land was very precious in Hong Kong, he agreed that the practice today should be different. The Lands D considered that for a developing project with a long period of development, it should not wait until the development was completed before carrying out its work. If the project was divided into several stages, the Lands D could carry out certain work at each stage, thereby reducing the possibility of encroachment on government land; and
- the Lands D planned to complete the setting out of boundaries for sites granted in eight months.

81. Regarding the measures taken by the Lands D to set out the boundaries of a government site before disposal of the site, the **Director of Lands**, in his letter of 8 January 2005 in *Appendix 47*, stated that:

- sites for public auction or tender were normally fenced and their boundaries would be set out before sale; and
- for sites granted by private treaty grant and extension, the plans in question included boundary dimensions and bearings, and the site area to facilitate the design of the development. The site boundaries would be set out on ground in advance or within three months after the completion of the land transaction so that the positions of the boundary marks could be shown to the landowner or his/her representative. Thereafter, it was the landowner's responsibility to protect the boundary marks placed on ground.

Encroachments on government land at Discovery Bay and Yi Long Wan

82. According to paragraphs 5.14 to 5.16 of the Audit Report, the Lands D had been aware of encroachments on government land at the DB golf course since early 1980s. The Committee questioned why the Lands D had not taken timely actions to rectify the encroachments.

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83. The **Director of Lands** responded that:

- Developer A had applied to the Government in 1981 and 1996 for renting a piece of government land at Wong Chuk Long, on an STT basis, for accommodating the fourth and fifth holes of the golf course at DB. The application in 1981 was not processed as the Government thought at the time that it would be more appropriate to deal with the problem when the Government Lease was issued after the whole DB development was completed. This was reflected in the then Director of Lands' letter of 16 March 1983. The application in 1996 was rejected as the land fell within the proposed extension of the Lantau North Country Park; and
- in 1998, the Lands D required Developer A to reinstate the land concerned. In 2002, the developer applied for an STT for the third time. At that time, the Government had decided that the land concerned would not be included in the Lantau North Country Park area. Because of this factor and other practical considerations, in July 2002, the Lands D approved the STT for the land concerned to be used as part of the golf course.

84. The Committee enquired whether the exclusion of the encroached government land from the boundary of Lantau North (Extension) Country Park was partly due to the fact that Developer A had repeatedly applied for an STT for the land.

85. In his letter of 24 January 2005, the **Director of Lands** stated that:

- the boundary of Lantau North (Extension) Country Park originally proposed in 1996 on the one hand included part of the golf course area on the encroached government land but on the other hand excluded another part on the encroached government land. Following consultation among concerned government departments, the Director of Agriculture, Fisheries and Conservation excluded the entire encroached area from the proposed boundary of Lantau North (Extension) Country Park in 1999. This was reflected in the draft map for the Lantau North (Extension) Country Park gazetted in July 2001 and the DB OZP gazetted in September 2001; and
- there was no information on record that the STT applications by Developer A had influenced the determination of the proposed boundary of an extended Lantau North Country Park.

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86. Given that the developer had applied for an STT in 1981, the Committee asked why the Administration had not processed the application promptly so that STT rent could be collected earlier.

87. The Committee also referred to paragraph 5.18 of the Audit Report which revealed that after rejecting Developer A's second application in 1998, the Lands D had asked the developer to reinstate the land. However, the Lands D had not taken follow-up action to ascertain whether the land had been reinstated. The Committee asked why this had happened.

88. The **Director of Lands** stated that:

- it appeared to be the then Government's intention to resolve the problem by rectifying the lot boundaries after the whole project had been completed rather than granting an STT to the developer. The Government had not suffered any loss in revenue because, after the STT was granted, the Government had collected rent from the developer with effect from the time of occupation, i.e. October 1982; and
- he could not find an explanation in the records with regard to why the Lands D had not taken follow-up action at that time to ascertain if the land had been reinstated. Perhaps the staff concerned had not followed through the procedure.

89. The Committee further asked whether it was a normal arrangement in the 1980s for the Government not to take timely rectification action on encroachment on government land for the reason that the development concerned was still on-going. The **Acting Director of Lands**, in his letter of 8 January 2005 in *Appendix 47*, stated that this approach was not the normal arrangement in the 1980s to address encroachment on government land.

90. The Committee asked about the measures that the Administration would take to ensure that encroachment on government land was rectified in a timely manner. The **Director of Lands** stated that:

- the Lands D had an established procedure for dealing with encroachment on government land. Depending on the nature and extent of the encroachment, different actions would be taken; and

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- if the encroachment was of a small scale, the Lands D would regularise it by granting an STT. For example, if a house owner encroached on a piece of government land in front of a small house in the New Territories and turned it into a garden, the Lands D might consider leasing the land to the house owner on an STT. This was because the land concerned was not big and even if it was not encroached on, it was not very useful. By doing so, the Lands D could also ensure that the land would not be used for other worse purposes and could bring in revenue. If the encroachment was very serious, the Lands D would ask the person concerned to reinstate the land or might even consider instituting prosecution.

91. The **Secretary for Housing, Planning and Lands** added that the Administration would ensure that the officers concerned would follow through the above established procedure.

92. According to paragraph 5.23 of the Audit Report, the Islands District Council member who complained about the deletion of the public golf course and the proposed STT in July 2002 was dissatisfied that the Government tried to resolve the encroachment problem by issuing the STT as this would undermine the Government's bargaining power. The Committee asked whether the Administration agreed to such a view.

93. The **Secretary for Housing, Planning and Lands** and the **Director of Lands** stated that:

- the purpose of regularising encroachments on government land by way of STTs was indeed to ensure that the Government would not suffer financial losses due to unauthorised use of the land. This was because the rent under an STT was assessed on full market rent basis; and
- if necessary, the Government could require the occupier of the land to reinstate the land and prosecute the occupier. However, under some circumstances, it would be more practicable to issue an STT so that the occupier could continue to use the land while the Government could collect rental at the market rate.

94. The Committee noted from Appendix B of the Audit Report that there was a provision concerning the rate of payment for any excess or deficiency in area of the site in General Condition 5(a) of the lease conditions of the Yi Long Wan development, but not in those of the DB development. The Committee asked about the reason for the discrepancy.

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95. The Committee further noted that there was also encroachment on government land at the Yi Long Wan site. However, it seemed that the Administration had been more proactive in dealing with the problem at Yi Long Wan. As both the DB and Yi Long Wan developments were located on Lantau Island and developed in the same period, the Committee asked why different approaches had been adopted in addressing the land encroachment problems on the two places.

96. In his letter of 8 January 2005, in *Appendix 47*, the **Acting Director of Lands** explained that:

- the records of Master Lease Conditions in the Lands D showed that between the grant of the lot at Yi Long Wan in 1975 and the DB in 1976, there was a change in approach and the rate of payment condition was dropped; and
- the golf course encroachment at DB was, and remained, an unbuilt open area operated by a single entity. The grant of an STT was the appropriate means to regularise it. The circumstances of the encroachment at Yi Long Wan, involving two privately owned residential blocks in multiple ownership constructed partially outside the lot, were quite different from those of DB and therefore warranted different treatment.

97. According to paragraph 5.15 of the Audit Report, Developer A had said that the extension of the area for the golf course had been agreed to at prior meetings with the SNT. The Committee enquired whether:

- there were records of those meetings;
- the Lands D had ascertained with the SNT at that time the truthfulness of Developer A's claim of agreement; and
- it was because of the SNT's agreement, as claimed, that the Lands D had been more lenient in dealing with Developer A.

98. In his letter of 8 January 2005, in *Appendix 47*, the **Acting Director of Lands** said that the Lands D's files did not contain any record of discussions between the SNT and Developer A. Similarly, the Lands D did not have any file record showing whether or not it had ascertained with the SNT the truthfulness of Developer A's claim of agreement.

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99. Regarding the encroachment at Yi Long Wan, the Committee noted from paragraph 5.42(b) of the Audit Report that the Registrar General's Department had said in 1983 that despite the undertaking, it would be difficult to ask Developer B to pay a premium for the extra piece of land. The Committee asked whether it was possible for the Lands D to recover the premium nowadays.

100. The **Director of Lands** responded that:

- although Developer B had undertaken in December 1980 to pay a premium for the extra piece of land, in January 1983, it requested the Lands D to confirm that there would be no premium for revising the site boundary. This meant that it had withdrawn his undertaking. According to the file records, Developer B was in great financial difficulties at that time and could not pay the premium at all. That was why the matter had not been followed up by the Registrar General's Department; and
- legally, the Administration could ask the grantee for the Yi Long Wan site to pay the premium. However, the developer for the site almost did not exist nowadays and the flats had been sold. The Administration would have to discuss with more than 200 owners to recover the premium. Even if one owner disagreed to pay, there would be a lot of problems. It was doubtful whether the Administration could collect any premium.

101. The Committee noted that the Government could take prosecution action against encroachment of government land. The Committee enquired why the Administration had not prosecuted Developer A which had occupied government land illegally for more than 20 years.

102. The **Director of Lands** responded that:

- there were guidelines in the LAOI setting out the circumstances under which STTs should be granted. The Lands D's policy did allow it to regularise encroachments by granting STTs. In view of the fact that the land concerned had been occupied by Developer A for several decades, the Lands D considered it more pragmatic to grant it an STT rather than prosecuting it and asking it to reinstate the land;

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- in fact, the Ombudsman had stated in her report that she agreed with the Lands D on the proposed course of action (i.e. granting an STT). She considered the case to be a fait accompli where events had left the Lands D with little alternative; and
- another reason for granting an STT to Developer A was that, as pointed out in paragraph 5.24(c) of the Audit Report, the occupation of the land had been acknowledged in writing in 1983 by the Director of Lands on the basis that formal documentation would be issued at a later date. It could be argued that a form of tenancy had been in place. If the Lands D took prosecution action in 2003, there might be a legal dispute.

103. To ascertain whether the rent for 21 years paid by Developer A for the occupation of the government land (paragraph 5.26 of the Audit Report referred) was reasonable, the Committee asked:

- about the amount and basis of the rent paid;
- the amount of rent originally proposed by the Lands D; and
- the estimated amount of revenue that could have been generated by the encroached pieces of land if they had not been used by Developer A.

104. **Mr LAU Chi-ming, District Lands Officer/Islands, Lands D**, said that the rental was calculated on the basis of the full market rate at 1982 when the occupation of the land took place and then reviewed every three years thereafter according to the prevailing market rates at the respective times.

105. The **Director of Lands** and the **Acting Director of Lands** stated, at the public hearing and in the letter of 8 January 2005 in *Appendix 47* respectively, that:

- an STT was a contract between the Government (as the landlord) and a private party (as tenant). Developer A had given verbal consent to disclosing the amount of STT rent paid. The total amount of rent paid for the 21-year period from October 1982 to October 2003 was \$7.23 million. This was a negotiated amount;
- the negotiated rental was based on evidence of market transactions. The figure initially proposed in the negotiation by the Lands D was \$11.2 million for the same period; and

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- the three encroached areas were remote and hard to access. The areas adjoining the encroached land at Wong Chuk Long were either steep sloping government land or private land owned by Developer A. As regards the other two encroached areas, they were largely sloping areas. The Lands D did not consider that they were capable of separate alienation or use by any party other than Developer A and, as such, no revenue would have been generated if they had not been used by Developer A.

106. The Committee questioned why the Lands D allowed the STT rental to be cut by such a large extent after negotiation, notwithstanding that the developer had encroached on government land for a long time. It seemed that the Government had treated big developers much more leniently than small landlords.

107. The **Director of Lands** explained that:

- STT rental, like land premium, was very often determined by negotiations. The professional surveyors in the Lands D would make an analysis and valuation of the rental with the benefit of all relevant information and their expertise. However, valuation was not an exact science. Different surveyors would hold different views on the valuation of a site;
- regarding the encroachment by the golf course, the Lands D made a valuation and proposed that \$11.2 million should be charged. During the negotiations with the developer, it also presented its data. Such negotiations were very common in land premium matters. Having considered the arguments and evidence of both sides, the Lands D was of the view that the developer's appeal was not unjustified. Therefore, the proposed rental was reduced to \$7.23 million. In deciding to accept the amount, the Lands D took into account the Crown rent back in 1981, the remote location of the encroached areas and the fact that their commercial value was almost zero. The Lands D had also made reference to the rent for a government site used for gardens after 1982 as well as the rateable value; and
- the occupation of government land at DB for the operation of a golf course was a very special case. It did not mean that the Lands D would adopt the same approach in dealing with others who encroached on government land. The case was special in that the DB development had its own unique development history, the developer had indeed applied for an STT with the Government at different times but the applications were rejected for various reasons, and the Government had intended to resolve the matter after the

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whole development had been completed. The case did not reflect the Government's overall policy.

108. It appeared to the Committee that the Director of Lands' reply, that there was a relationship of landlord and tenant between the Government and Developer A, suggested that the developer's encroachments on the government land was legal. Moreover, instead of penalising the developer, the Lands D had allowed the developer to bargain the STT rental with it. In the end, the Lands D accepted a smaller amount. The Committee asked the Secretary for Housing, Planning and Lands whether:

- he considered Developer A's encroachments on government land legal and the rent of \$7.23 million reasonable; and
- he agreed that the Administration was not doing its best to protect public money.

109. The **Secretary for Housing, Planning and Lands** responded that:

- there was a division of duties within the Government. While a bureau secretary had to shoulder the responsibilities for all the departments under his purview, the secretary would not know everything about the daily operations of these departments; and
- it was most important to have proper systems in place. Being a bureau secretary, he was responsible for overseeing the systems. As for daily operations, since these were very trivial, he could not look at each and every one of them in detail and had to rely on the Director. In turn, the Director would also have to rely on his subordinates. Officers of different ranks in a department had different responsibilities.

110. The Committee queried why the Secretary for Housing, Planning and Lands considered issues relating to public money trivial. The **Secretary for Housing, Planning and Lands** responded that:

- he had mentioned that he would not look at trivial issues in general, but not that public money was trivial. As the Lands D was responsible for those issues, he would see if it had discharged its duties properly;

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- as regards whether Developer A's occupation of government land was legal, he could not make a personal judgement as he was not a professional. Presumably, the Lands D had discussed with the Department of Justice before stating that a form of tenancy had been in place. He had not seen the relevant legal advice; and
- he did not know about the STT rent in 2003. The assessment of STT rent fell within the Lands D's daily operation. It did not have to report the assessment to him and he did not need to ask about that.

111. In response to the Committee's enquiry about the legal basis of the view that a form of tenancy had been in place, the **Director of Lands**, in his letter of 24 January 2005, stated that:

- in considering Developer A's application for an STT in July 2002, the Lands D had taken legal advice on the status of the encroached land. The advice was that the Government had acknowledged the occupation of the land by Developer A in a series of correspondence over a number of years since March 1983 and had indicated in writing that the encroachment would be regularised upon issue of the Crown Lease at the completion of the whole development when the Government would carry out a survey of the lot boundaries. In October 1996, Developer A applied for an STT of the encroached land. This was rejected at that time as the land was within the proposed extended limits of the Lantau North Country Park. Developer A reactivated his application for an STT in mid-2002, and this was approved in July 2002;
- based on the above sequence of events and course of conduct by the Government in its dealings with Developer A regarding the encroached land between the time when the Government became aware of the encroachment in 1982 and the issuance of a formal STT in 2002, the legal advice was that a form of tenancy would have been created; and
- since Developer A had been occupying the encroached land with the full knowledge and acquiescence of the Government in the period (with the intention of regularisation upon the completion of the development of DB), it could not be said to be a trespasser. It was a tenant at will from the Government, subject to agreement of boundaries and any other terms, including rent or mesne profits payable for the period of its occupation prior to issuance of the formal STT. It was on this basis that the Government was entitled to demanding the payment of the rent or mesne profits for the period from 1982 to mid-2002.

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Evidence obtained at the public hearing on 12 January 2005

112. Upon the Committee's request, **Sir David Akers-Jones** provided written comments on the various issues mentioned in the Audit Report in which he was involved as the then SNT, SCNTA or CS. His written response dated 5 January 2005 is in *Appendix 49*.

113. At the Committee's public hearing on 12 January 2005, **Sir David Akers-Jones** made an opening statement, the full text of which is in *Appendix 50*. In summary, he said that:

- he was over 77 years old and had retired for more than 17 years. It was very difficult for a man of his age and who had been out of Government for so long to recall things that took place over 25 years ago. The time lapse and lack of access to information made it very difficult to recollect details;
- his involvement in the DB matter was very limited and took place over the short period of time between 1977 and 1982 when he was the SNT. By 1982, the functions of the SNT and its successor, CNTA, had been taken over by the Secretary for Lands and Works and the Lands D. Thus, many departments had reviewed his work;
- during the period when he was the SNT, he had a very capable team of estate surveyors and legal advisers and he relied on their expertise and assistance when making decisions. There were well defined and established procedures and officials within a clear chain of command with no-one acting alone. In his experience, there were proper contemporaneous records of transactions and he was very surprised to find that many documents had not been kept or were now missing. Before he made any decision, there would be input from various other departments;
- neither the Director of Audit nor the Public Accounts Committee had ever previously made any recommendations or comments on the DB development when he was the SNT or any time thereafter until recently, after 25 years;
- at the time when he was the SNT, there was no planning control legislation in place in the New Territories. Also, there were few proposed developments of the size of DB at that time. In the early 1970s, DB was a barren rocky area without any infrastructure or development;

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- the original developer, Mr Edward WONG, had a good innovative idea but it later went into liquidation after heavily mortgaging the property to the bank. The whole DB project was at substantial risk of not proceeding at all and there were concerns that the mortgagee bank might take possession of the land. Accordingly, it was important that the development be permitted to proceed with a certain degree of flexibility. This more flexible approach was allowed by the ExCo granting to the developer the land at DB for a holiday resort/commercial development, as opposed to a previously restrictive approach adopted by the ExCo to restrict the use of land merely for the purposes of a holiday resort with limited residential and commercial use;
- it was the lease conditions that specified the planning intention of the land (there being no OZP). The MLP under the lease conditions was a mechanism for giving control with a degree of flexibility. The lease conditions were drafted by a senior official in the Registrar General's Department. The MLP provisions incorporated into the lease conditions were clear;
- given the barrenness, long distance, the lack of infrastructure and difficulty of access to urban areas of Hong Kong in the 1970s and there being no precedent for such an idea, it would have been difficult to assess its popularity in terms of how many people would buy holiday homes or use the recreation facilities or if it would have been different had a hotel been built. In addition, it would have been hard to assess the value of a hotel development as opposed to a holiday home development in respect of such a risky development. In any event, the estate surveyors in those days would have made their best valuation assessments at that time and he would have followed their advice and legal advice when making any decisions;
- he believed that DB was a resort and would remain one, with its fine recreational golf and yacht club facilities, the access by the public to the golf during the week, the beach fronts and restaurant cafes and landscaping in the area. If there were no flexibility allowed by the ExCo and the MacLehose and subsequent Administrations, the development would not have been commercially viable and would not have been anywhere near the success it was today; and
- while he was the SNT, he had no better or worse relations with developers and other tycoons than other senior officials then and now. He was not asked to be a director, albeit an independent non-executive director, of the DB developer until 2000, some 13 years after his retirement as the CS.

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114. Regarding Sir David Akers-Jones' query as to why Audit had taken up this subject for review only recently but not earlier, the **Director of Audit** explained that the review arose from a complaint about the DB development and the Legislative Council had also dealt with the complaint in 2002.

115. The Committee noted that according to the ExCo paper of July 1976, DB should be developed into a holiday resort with limited residential and commercial purposes. Thus, the residential and commercial developments should be ancillary to the holiday resort development. However, it turned out later that the residential and commercial developments became primary while the resort development was only secondary. The Committee asked Sir David why, at that time, he considered that the actual development of DB was not out of step with the ExCo's decision.

116. The Committee also referred to paragraph 2.17 of the Audit Report which mentioned that, in July 1985, the PGLA of the Lands D had said that "the form this development has taken to date, i.e. that it is very much less of a tourist resort (both for overseas and local tourists) and more of a typical residential development". The Committee asked Sir David whether he was aware of such views within the Government at that time.

117. **Sir David Akers-Jones** responded that:

- a resort could take many forms. The fact that there were now 15,000 people living in DB did not preclude it from being considered a resort. Similarly, the hotels and high-rise buildings in Phuket, Miami, Blackpool, Brighton, Nice, Cannes or Monte Carlo did not prevent any of these places being considered a resort. In his opinion, the inclusion of residential and commercial development in DB was part of the growth of a resort as it developed;
- as reflected in the Explanatory Statement in the DB OZP of 2003, the DB development "is primarily a car-free environment evolved from the original concept of a holiday resort approved in 1973. This intention [of a resort] is still maintained by the existing and planned provision of a diversity of recreation facilities". Hence, the development of DB had conformed with the description that it was a resort and it remained to be so. It was in line with the ExCo's decision of 1976; and

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- in 1985, he had retreated from the scene into being the SCNTA. He was not present at those meetings when the PGLA's views were raised. However, he was aware of the general way the DB development was proceeding, including high-rise buildings taking the place of low-rise buildings. He would also have been aware of the comments like those raised by the PGLA.

118. The Committee pointed out that at present the public could only play at the DB golf course during non-holidays. There was no resort accommodation or hotel but only residential development at DB. The Committee asked why he still considered that the original resort concept had not been changed.

119. **Sir David Akers-Jones** stated that:

- he still considered the DB development a resort although it had changed somewhat from the early concept. The hotel GFA was allowed to be reduced because reasonable men would not insist upon a developer building a vast number of hotel rooms if nobody was going to occupy them. Having decided that the amount of hotel accommodation needed at that time was much less, it was reasonable to switch the spare GFA to housing accommodation. Although the balance of residential, commercial and hotel development had been switched flexibly, the total GFA had remained constant in many years; and
- members of the public could go to DB and use the recreational facilities there, including the beach. They could not use the club because it was a membership club. As for the other facilities, some were private for the residents of DB and some were open to the public. In fact, the developer, instead of providing a public golf course, had imported 300,000 cubic metres of sand from China to fill up the once muddy foreshore, turning it into a beach which was 700 metres long, backed by a promenade and trees.

120. Regarding the discussion by the DPC in 1985 about the need to report the change in the concept of the DB development to the ExCo, the Committee asked why Sir David, as the then CS, decided that there was no need to do so (paragraph 2.21 of the Audit Report referred). The Committee also asked whether the decision was made upon the developer's request and whether he had tried to circumvent the ExCo for some reasons.

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121. **Sir David Akers-Jones** responded that:

- the background of the issue was that, in 1985, the Joint Declaration had just been approved by the British Parliament. The Governor and the ExCo were very occupied. The Governor was beginning a long period of shuttling between Beijing and London. As the CS, he had to shoulder additional administrative responsibilities. Hence, they were under great pressure;
- notwithstanding the above, the main reason for not going back to the ExCo was that the resort development had continued and the development up to that time did not represent a major change in principle; and
- he had not wanted to circumvent the ExCo and he had not received any request from the developer. It was a matter of whether the ExCo should be bothered with decisions that could be properly made by the SNT, who was authorised by the lease conditions to make those decisions. If the ExCo had wanted the decision to be referred back to it, it would have said so. The Secretary for Lands and Works had said that, in his view, it was not necessary to refer to the ExCo and he agreed with him.

122. The Committee asked about the details of the Secretary for Lands and Works' view and whether, with hindsight, Sir David considered that the matter should have been reported back to the ExCo.

123. **Sir David Akers-Jones** stated that:

- on the question of whether the matter should be reported back to the ExCo, Mr Todd, the Secretary for Lands and Works had minuted to him, then CS. It was stated in the file minute (in *Appendix 51*) that "The question arises whether, in view of the initial ExCo approval in 1976 and the potentially controversial changes now contemplated, ExCo approval need be sought at this stage. I would think probably not but would be grateful for your advice."; and
- Mr Todd was a very reliable person. He acted upon Mr Todd's recommendation.

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124. The Committee questioned why, as the CS, Sir David had simply acted upon his subordinate's advice. **Sir David Akers-Jones** stated that Mr Todd, the Secretary for Lands and Works, was an immediate subordinate, not a junior one. Mr Todd was virtually on the same level as he himself as far as seniority was concerned. Mr Todd was a man on whose judgement he could rely.

125. According to Sir David Akers-Jones' written response, in 1977, when Mr WONG's business went into liquidation and the development was in the hands of the mortgagee bank, another developer took over the development with the encouragement of the Hong Kong Government. It appeared to the Committee that if the DB project was taken over by the mortgagee bank, it would not leave the land idle and might look for another developer. The Committee asked why the Government intervened in commercial operation at that time and did not allow the mortgagee bank, which was a bank tied to the former Soviet Union, to take over the development, and why no tendering exercise was held. The Committee asked whether these were due to political considerations.

126. **Sir David Akers-Jones** responded that:

- there should be no other company which wanted to take over a development at the then remote Lantau Island. The new developer was a company owned by Mr CHA Chi Ming, who was well known to the Administration. He was a prominent person and had made a great contribution to Hong Kong. The trust that the Administration put in him then had been amply rewarded; and
- as the original developer had gone into liquidation, the development was in the hands of the Official Receiver. The then Governor-in-Council had to make the decision about what to do with the development. The Official Receiver advised that this was the best solution and the Governor-in-Council made a decision in the best interests of Hong Kong.

127. The Committee then turned to the SCNTA's approval of MLP 5.0 in February 1982 which removed the requirement for the provision of the public golf course. In his written response, Sir David Akers-Jones gave a detailed description of the administrative procedures for dealing with changes to MLPs. It was stated that the views of all departments were taken into account in approving MLPs for the New Territories, and "I [the SNT] would not have approved a MLP or changes to a MLP or any land transaction that had to be dealt with by me without a full discussion with the PGLA. If the PGLA/NT thought a premium or other conditions of approval were justified, he would have recorded it and action would have been taken."

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128. According to the above description, there should be records of the discussions about the deletion of the public golf course and the approval of MLP 5.0 at that time. However, the Committee was informed by the Lands D that there were no records of any inter-departmental discussions on the deletion of the golf course prior to the approval of MLP 5.0 in February 1982. There were also no documents showing why the then Commissioner for Recreation and Culture welcomed the proposal that other recreational facilities would be provided in place of the public golf course. The Committee therefore asked:

- why there were no such records; and
- whether there had indeed been inter-departmental discussions relating to the public golf course and MLP 5.0 at that time.

129. **Sir David Akers-Jones** stated that:

- he was also surprised that many documents were now missing; and
- the question of whether there should be a public golf course was first raised in 1977 when the developer proposed a list of recreational activities to replace it. The decision to delete the golf course was certainly not a sudden one made by him alone. The discussion about the golf course had been going on for a number of years since the developer first raised it and both the pros and cons had been considered. Thus, there was the statement that the R&CD was in favour of the deletion and the substitution by other recreational facilities. There was also the objection raised by the Highways Department representative, but that was a lone voice. The others fell in with the R&CD and so did he.

130. The **Director of Lands** supplemented that:

- the Lands D informed the Committee in the letter of 8 January 2005 that there were no documents showing why the then R&CD welcomed the proposal. In fact, there was a document stating that the Commissioner for Recreation and Culture welcomed the proposal that other recreational facilities would be provided in place of the public golf course. But the document did not explain why he welcomed the proposal; and

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- the Lands D had tried its best to look for the records of inter-departmental discussions relating to the deletion of the golf course prior to the approval of MLP 5.0 and no records were found. But the failure to find the records did not mean that there were no such discussions before the decision was made.

131. The Committee noted that Sir David Akers-Jones had stressed that he had all along relied on professional advice when making decisions. However, according to paragraphs 3.5 to 3.7 of the Audit Report, the PGLA had said that the public golf course was one of the main reasons for the Government to have approved the land grant and such a requirement was particularly referred to in a special lease condition. Despite the PGLA's comments, the SCNTA approved the deletion of the public golf course. The Committee asked Sir David why he went against the PGLA's advice and whether that was because of his personal preference.

132. **Sir David Akers-Jones** responded that:

- the PGLA had raised a valid point and it was his duty to raise it. But there had been a consensus in the Government that it would be better to have other recreational facilities than the public golf course; and
- the ExCo had not requested that changes to the lease conditions be reported back to it. Instead, he was authorised to make changes and there were systems and procedure in place as to how he would make changes, not autocratically, but in consultation with the officers of the department and those outside the department. That was what he did.

133. On the question of land premium on approval of changes made in MLP 4.0 in 1977, the Committee noted Sir David Akers-Jones' written response that whether or not premium was payable would have been given full consideration not by one official acting on his own but together with his colleagues and superiors. It seemed that no premium was charged after this proper consideration, no doubt taking into account the drastic slump in the property market.

134. The Committee asked whether there were records showing that it was a collective decision that no premium was necessary and that the main reason was the drastic slump in the property market.

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135. **Sir David Akers-Jones** responded that:

- he would not have been involved in deciding about premium. Valuation for premium was the job of a professional team of estate surveyors headed by the PGLA. While there were few MLPs processed at that time, the question of premium on a change of MLP was always actively considered. The estate surveyors would have considered the question of premium very seriously before making the decision that this particular modification at that time did not attract a premium; and
- he did not think that there were records of the discussions among the estate surveyors. Both the Secretary and the Director had not been able to produce them.

136. In response to the Committee's enquiry as to whether there was a drastic slump in the property market in the period around 1977, the **Director of Audit**, in his letter of 10 January 2005, in *Appendix 52*, advised that according to the "Estimates of Revenue and Expenditure for the year ending 31st March 1979", it was mentioned that there was an economic recession in 1975-76 and continuing recovery during 1976-77.

137. The Committee referred to paragraph 5.15 of the Audit Report which mentioned that Developer A had said that the extension of the area for the fourth and fifth holes of the DB golf course had been agreed to at prior meetings with the SNT. According to Sir David Akers-Jones' written response, the developer might have been referring to meetings with the headquarters staff of the New Territories Administration which might not have involved meetings with him. The Committee asked Sir David:

- whether, according to his recollection, the developer had really discussed the matter with him and, if so, why he had not instructed his subordinates to consider charging a premium for the government land occupied by the developer; and
- why the officials concerned had omitted the question of premium until recently.

138. **Sir David Akers-Jones** responded that:

- the developer might have talked to him. As the land concerned was a very rough hillside area, one did not know where the boundaries were and it was very easy to go outside the boundaries;

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- the question of premium was entirely a matter for the PGLA and his staff. It seemed that the decision taken at the time was that the problem of encroachment could be sorted out when there were proper boundaries. The encroachment problem had been sorted out subsequently by the granting of an STT and the developer had paid a substantial penalty for having encroached on the land. Thus, the officials had discharged their duty; and
- he had a clear recollection of the officials concerned at that time. Their approach to work was not casual and their integrity was not in question. They would have certainly done a professional job on such a small question of encroachment on a rough area.

139. It was mentioned in Sir David Akers-Jones' written response that he was invited to become a non-executive director of The Mingly Corporation Limited (Mingly) in 2000, 13 years after his retirement as the CS. The Committee asked Sir David whether, given that the development of DB was still in progress today, his acceptance of the invitation from Mingly, an associate of Developer A, to be its director would give rise to concerns that he had made decisions alone in dealing with Developer A in order to pave the way for his post-retirement life.

140. **Sir David Akers-Jones** said that Mingly had nothing to do with Hong Kong Resort Company, i.e. Developer A. It was an entirely separate company engaging in financial investment.

141. The Committee asked the Secretary for Housing, Planning and Lands, after hearing Sir David Akers-Jones' reasons for deciding that the developments in DB needed not be reported back to the ExCo, whether he still maintained his earlier view that the case should have been brought back to the ExCo.

142. The **Secretary for Housing, Planning and Lands** responded that the critical consideration was whether there had been change to the original resort concept. Sir David had explained that the resort concept had been maintained. If this was agreed, it was not necessary to report to the ExCo. However, he held a different opinion. After hearing Sir David's explanation, he still maintained the view that the original concept of the DB development had changed and such change should have been brought back to the ExCo.

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143. **Conclusions and recommendations** The Committee:

Change in concept of the Discovery Bay development

- acknowledges that the development of the Discovery Bay (DB) began in the 1970s and 1980s and took place against the particular background that existed at those times;
- expresses alarm and strong resentment that:
 - (a) the lease conditions of the DB site failed to specify the requirements for achieving the development concept; and
 - (b) the original resort concept of the DB development, as reflected in the Governor-in-Council's decision of 6 July 1976, had changed from a holiday resort and residential/commercial development to that of a first-home community, and the Administration had failed to obtain the Executive Council (ExCo)'s endorsement of that change;
- acknowledges that the Secretary for Housing, Planning and Lands:
 - (a) considers that there had been change to the original resort concept of the DB development and such change should have been brought back to the ExCo for endorsement; and
 - (b) has undertaken to seek the ExCo's endorsement of the development concept of DB;
- urges the Secretary for Housing, Planning and Lands to expeditiously seek the ExCo's endorsement of the change of concept;
- notes that the Director of Lands will implement the audit recommendations mentioned in paragraph 2.25 of the Director of Audit's Report (the Audit Report);

Provision of facilities in the Discovery Bay development

- expresses astonishment and serious dismay that:
 - (a) the approval of Master Layout Plan (MLP) 5.0 had in effect deleted the requirement to provide a public golf course, notwithstanding its specification in the lease conditions; and

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- (b) the Lands Department (Lands D) had failed to assess the implications, financial or otherwise, of the deletion of the facilities in the DB development;
- notes that the Director of Lands will implement the audit recommendation mentioned in paragraph 3.21 of the Audit Report;

Changes in Master Layout Plans and premium implications

- expresses astonishment and finds it inexcusable that the Lands D failed to:
 - (a) maintain a record of the public recreational facilities actually provided in the DB development;
 - (b) verify the specific as-built facilities in the DB development with those agreed with the developer to ensure that they had in fact been built; and
 - (c) document the reasons for not assessing and/or charging premium for the changes in those MLPs;
- condemns the then land authorities for having failed to assess whether premium should be charged for the changes made in the MLPs after the land grant and prior to 7 June 1994 (including the deletion of the public golf course in MLP 5.0 and the cable car system in MLP 5.1);
- notes that the Director of Lands has implemented the audit recommendations mentioned in paragraph 4.23 of the Audit Report;

Site boundaries of Discovery Bay and Yi Long Wan developments

- expresses grave dismay that:
 - (a) despite a lapse of 28 years after the land grant of the DB site, the Lands D had not yet set out the boundaries of the site;
 - (b) some 41,200 square metres of government land adjoining the DB site had been occupied without authorisation for over 20 years, but the Lands D did not take timely actions to rectify the encroachments;
 - (c) although certain buildings of the Yi Long Wan development were found outside the boundaries of the land grant, the Lands D had not taken any follow-up action to resolve the encroachment problem;

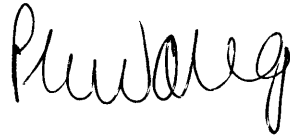
Grant of land at Discovery Bay and Yi Long Wan

- (d) there was a lack of co-ordination between the then District Office/Islands and the then Registrar General's Department, before the latter gave its pre-sale consent of the Yi Long Wan development; and
 - (e) without seeking legal advice, the Certificate of Compliance for the Yi Long Wan site had been issued before rectification of the site boundary problem;
- notes that the Director of Lands will implement the audit recommendations mentioned in paragraphs 5.12, 5.34 and 5.49 of the Audit Report; and

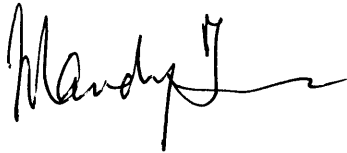
Follow-up actions

- wishes to be kept informed of the progress in:
 - (a) seeking the ExCo's endorsement of the development concept of DB; and
 - (b) implementing the various recommendations made by the Audit Commission and other improvement measures.

**SIGNATURES OF THE CHAIRMAN,
DEPUTY CHAIRMAN AND MEMBERS OF THE COMMITTEE**



Philip WONG Yu-hong
(Chairman)



TAM Heung-man
(Deputy Chairman)



LAU Kong-wah




Andrew CHENG Kar-foo



Abraham SHEK Lai-him



Jeffrey LAM Kin-fung



Albert Jinghan CHENG

3 February 2005

**CHAPTERS IN THE DIRECTOR OF AUDIT'S REPORT NO. 43
DEALT WITH IN THE PUBLIC ACCOUNTS COMMITTEE'S REPORT**

**Director of
Audit's Report
No. 43**

**P.A.C.
Report No. 43**

<u>Chapter</u>	<u>Subject</u>	<u>Chapter</u>
1	Control and monitoring of District Council expenses and related activities	1
3	Government subsidies to the English Schools Foundation	2
4	Corporate governance and Headquarters administration of the English Schools Foundation	3
5	School administration of the English Schools Foundation	4
6	Grant of land at Discovery Bay and Yi Long Wan	5

**RULES OF PROCEDURE OF
THE LEGISLATIVE COUNCIL OF
THE HONG KONG SPECIAL ADMINISTRATIVE REGION**

72. Public Accounts Committee

(1) There shall be a standing committee, to be called the Public Accounts Committee, to consider reports of the Director of Audit –

- (a) on the accounts of the Government;
- (b) on such other accounts required to be laid before the Council as the committee may think fit; and
- (c) on any matter incidental to the performance of his duties or the exercise of his powers as the committee may think fit.

(2) The committee shall also consider any report of the Director of Audit laid on the Table of the Council which deals with examinations (value for money audit) carried out by the Director relating to the economy, efficiency and effectiveness of any Government department or public body or any organization to which his functions as Director of Audit extend by virtue of any Ordinance or which receives public moneys by way of subvention.

(3) The committee shall consist of a chairman, deputy chairman and 5 members who shall be Members appointed by the President in accordance with an election procedure determined by the House Committee. In the event of the temporary absence of the chairman and deputy chairman, the committee may elect a chairman to act during such absence. The chairman and 2 other members shall constitute a quorum.

(4) A report mentioned in subrules (1) and (2) shall be deemed to have been referred by the Council to the committee when it is laid on the Table of the Council.

(5) Unless the chairman otherwise orders, members of the press and of the public shall be admitted as spectators at meetings of the committee attended by any person invited by the committee under subrule (8).

(6) The committee shall meet at the time and the place determined by the chairman. Written notice of every meeting shall be given to the members and to any person invited to attend a meeting at least 5 clear days before the day of the meeting but shorter notice may be given in any case where the chairman so directs.

(7) All matters before the committee shall be decided by a majority of the members voting. Neither the chairman nor any other member presiding shall vote, unless the votes of the other members are equally divided, in which case he shall have a casting vote.

(8) The chairman or the committee may invite any public officer, or, in the case of a report on the accounts of or relating to a non-government body or organization, any member or employee of that body or organization, to give information or any explanation or to produce any records or documents which the committee may require in the performance of its duties; and the committee may also invite any other person to assist the committee in relation to any such information, explanation, records or documents.

(9) The committee shall make their report upon the report of the Director of Audit on the accounts of the Government within 3 months (or such longer period as may be determined under section 12 of the Audit Ordinance (Cap. 122)) of the date on which the Director's report is laid on the Table of the Council.

(10) The committee shall make their report upon the report of the Director of Audit mentioned in subrule (2) within 3 months (or such longer period as may be determined by the Council) of the date on which the Director's report is laid on the Table of the Council.

(11) Subject to these Rules of Procedure, the practice and procedure of the committee shall be determined by the committee.

**Paper presented to the Provisional Legislative Council
by the Chairman of the Public Accounts Committee
at the meeting on 11 February 1998 on
Scope of Government Audit in the
Hong Kong Special Administrative Region -
'Value for Money Audits'**

SCOPE OF WORK

1. The Director of Audit may carry out examinations into the economy, efficiency and effectiveness with which any bureau, department, agency, other public body, public office, or audited organisation has discharged its functions.

2. The term "audited organisation" shall include -

- (i) any person, body corporate or other body whose accounts the Director of Audit is empowered under any Ordinance to audit;
- (ii) any organisation which receives more than half its income from public moneys (this should not preclude the Director from carrying out similar examinations in any organisation which receives less than half its income from public moneys by virtue of an agreement made as a condition of subvention); and
- (iii) any organisation the accounts and records of which the Director is authorised in writing by the Chief Executive to audit in the public interest under section 15 of the Audit Ordinance (Cap. 122).

3. This definition of scope of work shall not be construed as entitling the Director of Audit to question the merits of the policy objectives of any bureau, department, agency, other public body, public office, or audited organisation in respect of which an examination is being carried out or, subject to the following Guidelines, the methods by which such policy objectives have been sought, but he may question the economy, efficiency and effectiveness of the means used to achieve them.

GUIDELINES

4. The Director of Audit should have great freedom in presenting his reports to the Legislative Council. He may draw attention to any circumstance which comes to his knowledge in the course of audit, and point out its financial implications. Subject to these Guidelines, he will not comment on policy decisions of the Executive Council and the Legislative Council, save from the point of view of their effect on the public purse.

5. In the event that the Director of Audit, during the course of carrying out an examination into the implementation of policy objectives, reasonably believes that at the time policy objectives were set and decisions made there may have been a lack of sufficient, relevant and reliable financial and other data available upon which to set such policy objectives or to make such decisions, and that critical underlying assumptions may not have been made explicit, he may carry out an investigation as to whether that belief is well founded. If it appears to be so, he should bring the matter to the attention of the Legislative Council with a view to further inquiry by the Public Accounts Committee. As such an investigation may involve consideration of the methods by which policy objectives have been sought, the Director should, in his report to the Legislative Council on the matter in question, not make any judgement on the issue, but rather present facts upon which the Public Accounts Committee may make inquiry.

6. The Director of Audit may also -

- (i) consider as to whether policy objectives have been determined, and policy decisions taken, with appropriate authority;
- (ii) consider whether there are satisfactory arrangements for considering alternative options in the implementation of policy, including the identification, selection and evaluation of such options;
- (iii) consider as to whether established policy aims and objectives have been clearly set out; whether subsequent decisions on the implementation of policy are consistent with the approved aims and objectives, and have been taken with proper authority at the appropriate level; and whether the resultant instructions to staff accord with the approved policy aims and decisions and are clearly understood by those concerned;

- (iv) consider as to whether there is conflict or potential conflict between different policy aims or objectives, or between the means chosen to implement them;
- (v) consider how far, and how effectively, policy aims and objectives have been translated into operational targets and measures of performance and whether the costs of alternative levels of service and other relevant factors have been considered, and are reviewed as costs change; and
- (vi) be entitled to exercise the powers given to him under section 9 of the Audit Ordinance (Cap. 122).

PROCEDURES

7. The Director of Audit shall report his findings on value for money audits in the Legislative Council twice each year. The first report shall be submitted to the President of the Legislative Council within seven months of the end of the financial year, or such longer period as the Chief Executive may determine. Within one month, or such longer period as the President may determine, copies shall be laid before the Legislative Council. The second report shall be submitted to the President of the Legislative Council by the 7th of April each year, or such date as the Chief Executive may determine. By the 30th April, or such date as the President may determine, copies shall be laid before the Legislative Council.

8. The Director's report shall be referred to the Public Accounts Committee for consideration when it is laid on the table of the Legislative Council. The Public Accounts Committee shall follow the rules governing the procedures of the Legislative Council in considering the Director's reports.

9. A Government minute commenting on the action Government proposes to take in respect of the Public Accounts Committee's report shall be laid on the table of the Legislative Council within three months of the laying of the report of the Committee to which it relates.

10. In this paper, reference to the Legislative Council shall, during the existence of the Provisional Legislative Council, be construed as the Provisional Legislative Council.



中華人民共和國香港特別行政區
Hong Kong Special Administrative Region of the People's Republic of China



立法會秘書處

LEGISLATIVE COUNCIL SECRETARIAT

來函編號 YOUR REF
 來函日期 OUR REF AM 12/03/03
 電話 TELEPHONE 2869 9203
 傳真傳真 FACSIMILE 2877 9600

26 November 2004

Dr Hon Philip Wong Yu-hong, GBS
 Chairman
 Public Accounts Committee
 Legislative Council
 Legislative Council Building
 8 Jackson Road
 Central
 Hong Kong

Dear Dr Wong

**Progress report on matters outstanding in
 Public Accounts Committee Report No. 40
 on
 “Subvention for staff emoluments
 of The Legislative Council Commission”**

I wish to report on the progress in relation to the Public Accounts Committee's recommendations in Chapter 2 of its Report No. 40 regarding Chapter 5 of the Director of Audit's Report No. 40 on “Subvention for staff emoluments of The Legislative Council Commission”.

Review of funding arrangements for The Legislative Council Commission (LCC)

In its response made in the Legislative Council on 15 October 2003, LCC stated that as its funding arrangements with the Administration had been formulated nine years ago when LCC was first established, it was opportune to have an overall review.

The Exchange of Letters (EoL) between the Administration and LCC, which sets out the general principles and guidelines governing the administrative arrangements for LCC and its working relationship with the Administration, as well as the existing funding arrangements for LCC, has been reviewed. It has been amended to reflect the updated funding arrangements since the last revision in 1997, such as the replacement of the baseline approach for funding by the Operating Expenditure Envelope approach. The revised EoL was signed by LCC and the Administration in November 2004.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Ricky C C Fung', written in a cursive style with a large loop at the beginning.

(Ricky C C Fung)
Secretary General

c.c. Chief Secretary for Administration (Attn: Ms Chang King-kiu)
Secretary for Financial Services and the Treasury (Attn: Ms Elizabeth Tse)

**Witnesses who appeared before the Committee
(in order of appearance)**

Mrs Pamela TAN KAM Mi-wah, JP	Director of Home Affairs
Mr Isaac CHOW, JP	Deputy Director of Home Affairs (2)
Mr Patrick LI, JP	Assistant Director of Home Affairs (2)
Mr TSE Man-shing	Assistant Director of Home Affairs (Administration)
Mrs Alice LAU MAK Yee-ming, JP	Commissioner of Inland Revenue
Mrs Deborah MA LAU Siu-mi	Chief Assessor, Inland Revenue Department
Hon Michael SUEN Ming-yeung, GBS, JP	Secretary for Housing, Planning and Lands
Miss Diane WONG	Principal Assistant Secretary for Housing, Planning and Lands (Planning and Lands) 1
Mr Patrick LAU Lai-chiu, JP	Director of Lands
Mr Graham Ross	Assistant Director (Hong Kong), Lands Department
Mr LAU Chi-ming	District Lands Officer/Islands, Lands Department
Prof Hon Arthur LI Kwok-cheung, GBS, JP	Secretary for Education and Manpower
Mrs Fanny LAW, GBS, JP	Permanent Secretary for Education and Manpower
Mrs Cherry TSE, JP	Deputy Secretary for Education and Manpower (2)
Prof Felice Lieh MAK, MD, CBE, JP	Chairman, English Schools Foundation

Mr John Bohan	Acting Secretary and Chief Executive, English Schools Foundation
Mrs Gloria NG WONG Yee-man, JP	Parents Representative, English Schools Foundation
Mr AU YEUNG Ping-kwong, JP	Deputy Director of Lands/Survey and Mapping, Lands Department
Dr Sarah Rigby	Chairwoman of Joint Council of Parent Teacher Associations, English Schools Foundation
Mr Alex CHIU	Parents Representative, English Schools Foundation
Hon Frederick MA Si-hang, JP	Secretary for Financial Services and the Treasury
Ms Bernadette LINN	Principal Assistant Secretary for Financial Services and the Treasury (Treasury)
Hon Sir David Akers-Jones, GBM, JP	Former Chief Secretary

**Introductory Remarks by
Chairman of the Public Accounts Committee,
Dr Hon Philip WONG Yu-hong, GBS,
at the First Public Hearing of the Committee
on Wednesday, 8 December 2004**

Good morning, ladies and gentlemen. Welcome to the Public Accounts Committee's first public hearing relating to Report No. 43 of the Director of Audit on the results of value for money audits, which was tabled in the Legislative Council on 24 November 2004.

The Public Accounts Committee is a standing committee of the Legislative Council. It plays the role of a watchdog over public expenditure through consideration of the reports of the Director of Audit laid before the Council on the Government's accounts and the results of value for money audits of the Government and those organisations which receive funding from the Government. The consideration by the Committee of the Director's reports involves gathering evidence relevant to the facts contained in the Director's reports, so that the Committee may draw conclusions and make recommendations in a constructive spirit and forward-looking manner. I also wish to stress that the objective of the whole exercise is such that the lessons learned from past experience and our comments on the performance of the public officers concerned will enable the Government to improve its control over the expenditure of public funds, with due regard to economy, efficiency and effectiveness.

The consideration of the Director's reports follows an established process of public hearings where necessary, internal deliberations and publication of the Committee's report. The Committee has an established procedure for ensuring that the parties concerned have a reasonable opportunity to be heard. After the Committee is satisfied that it has ascertained the relevant facts, it will proceed to form its views on those facts, followed by a process of formulating its conclusions and recommendations to be included in its report. In accordance with Rule 72 of the Rules of Procedure of the Legislative Council, the Committee is required to make its report on the Director's report to the Legislative Council within three months of the date at which the Director's report is laid on the Table of the Council. Before then, we will not, as a committee or individually, be making any public comment on our conclusions.

Following a preliminary study of the Director of Audit's Report No. 43, the Committee has decided, in respect of five chapters in the Report, to invite the relevant public officers and parties concerned to appear before the Committee and answer our questions. We have, apart from this morning's hearing, also set aside the morning of 10 December for the public hearings.

Finally, I would like to draw your attention to the fact that my colleagues, Hon TAM Heung-man, Hon Andrew CHENG and Hon LAU Kong-wah have declared interest in respect of Chapter 1 of Report No. 43 which concerns "Control and monitoring of District Council expenses and related activities". The issues examined in this chapter include tax deduction on 50% of the honorarium for District Council Members and the allowance and grant for District Council Members. Hon TAM Heung-man and Hon Andrew CHENG have declared that they are serving District Council Members. Hon LAU Kong-wah has declared that he was a former District Council Member. The Committee considers that it is proper for these three Members to make the declaration.

To avoid any conflict of interest on the part of the three Members and in order that the impartiality and integrity of the Committee may be maintained, the Committee has agreed that they do not take part in the examination of this chapter. They will not participate in the public hearing, nor in the discussion and compilation of the Committee's report on this chapter. Neither will they make any public comment on the issues relating to this chapter.

I now declare the Committee to be in session.

% Non-taxable Income / Total Income

Year	District Council Members				Legco Members					
	Income	Taxable (A)	Non-taxable (B)	Total (C)	% of Non-taxable Income B/C	Income	Taxable (D)	Non-taxable (E)	Total (F)	% of Non-taxable Income H/F
1982	Honarium	\$ 1,000	\$ 1,000	\$ 2,000	50	ROE	\$ 0	\$ 4,000	\$ 4,000	100
1984	Honarium	1,000	1,000	2,000	50	ROE	0	9,500	9,500	100
1985	Honarium	1,750	1,750	3,500	50	Stipend ROE	8,500	10,200	18,700	55
1991	Honarium	5,450	5,450	10,900	50	Stipend ROE	36,000	30,000	66,000	45
1996	Honarium ORA	7,900	7,900	20,300	61	Stipend ROE	53,380	98,730	152,110	65
2000	Honarium AA	9,095	9,095	28,190	68	Stipend ROE	62,590	115,750	178,340	65
2001	Honarium AA	8,975	8,975	35,950	75	Stipend ROE	58,210	132,644	190,854	69
2004	Honarium OEA	8,345	8,345	32,700	75	Stipend ROE	55,220	125,834	181,054	70

Note

ORA = Office Rental Allowance 辦事處租金津貼

AA = Accountable Allowance 實報實銷津貼

OEA = Operating Expenses Allowance 營運開支津貼

ROE = Reimbursement of Operating Expenses 發還工作開支

稅務局專員辦事處
香港灣仔告士打道 5 號
稅務大樓 36 樓



OFFICE OF THE
COMMISSIONER OF INLAND REVENUE
REVENUE TOWER, 36/F.,
5 GLOUCESTER ROAD, WAN CHAI,
HONG KONG.

電話 Tel. No.: 2877 0113
圖文傳真 Faxline No.: 2877 1082

Our Ref: HQ188/17C Pt. 14
Your Ref: CB(3)/PAC/R43

Clerk to the Public Accounts Committee
Legislative Council Building
8 Jackson Road, Central
Hong Kong
(Attn: Mr Colin CHUI)

28 December 2004

Dear Mr Chui,

Report No. 43 of the Director of Audit
Chapter 1 : Control and monitoring of District Council expenses
and related activities

I refer to your letter of 22 December 2004.

Subsequent to the Public Accounts Committee [PAC] meeting on 8 December 2004, the Inland Revenue Department [IRD] has contacted the Home Affairs Department [HAD] regarding whether there will be any change to the remuneration package to District Council Chairmen and Members as well as the control and monitoring measures to be exercised over the reimbursable and non-reimbursable expenses.

Subject to the response of the HAD and the comments from the PAC, the IRD will proceed to implement the removal of the said administrative measure. In any event, the IRD will, through the HAD, advise the District Council Chairmen and Members to keep documentary evidence of expenses incurred from 1 April 2005 in support of their tax deduction claims for the 2005-06 final and subsequent years of assessment.

Yours sincerely,

(Mrs LAU MAK Yee-ming, Alice)
Commissioner of Inland Revenue

cc Director of Home Affairs
Director of Audit

民政事務總署
香港灣仔軒尼詩道一百三十號
修頓中心二十九及三十樓



Home Affairs Department
29th and 30th Floors, Southorn Centre,
130 Hennessy Road,
Wan Chai,
Hong Kong.

本署檔號 Our Ref. HAD/GA/CON/1/131

來函檔號 Your Ref.

電話 Tel.: 2835 1378

傳真 Fax.: 2573 7139

31 December 2004

Public Accounts Committee
Legislative Council
Legislative Council Building
8 Jackson Road
Central
Hong Kong
(Attn: Mr Colin CHUI)

Dear Mr Chui,

**The Director of Audit's Report on the
results of value for money audits (Report No. 43)**

**Chapter 1: Control and monitoring of District Council
expenses and related activities**

Thank you for your letter dated 21 December 2004.

In response to the Audit findings in paragraph 3.7 of the Audit Report, we have conducted a thorough examination on the 354 cases of non-compliance with the Home Affairs Department (HAD) Guidelines on the reimbursement of the Operating Expenses Allowance (OEA) and the Information Technology and Other Support Grant (ITOSG) to District Council (DC) Members. A table shortlisting the follow-up/remedial actions to be taken has subsequently been drawn up in the Appendix. We will take the matter forward and request the DC members concerned to provide supplementary information in support of their claims and to recover the overpayment of allowance and grant, etc. as soon as possible. We aim to complete all follow-up action by March 2005.

As regards the implementation of the Audit recommendations in various parts of the Audit Report, the follow-up actions taken are summarized below –

Allowance and Grant for DC Members (Para 3.18)

- (a) In early December 2004, we appealed to all DC members for full compliance with the HAD guidelines in claiming reimbursement of OEA and ITOSG. In mid-December 2004, we also held a special briefing with all DC Chairmen and Vice-Chairmen to explain to them the major areas of non-compliance and the imminent introduction of additional control measures to step up the monitoring system.
- (b) At the district level, we have reminded all staff to process the reimbursement of OEA and ITOSG with meticulous care and ensure strict adherence to the HAD guidelines.
- (c) We are now in the process of reviewing our guidelines based on the audit recommendations in paragraph 3.18(b) of the Audit Report and will hold consultation with DC members in January 2005 to seek their comments on proposed revision of the guidelines.

Use of DC Funds for Minor Environmental Improvement Projects (Para 4.21)

- (a) We have requested/reminded all Districts to –
 - (i) draw up/update the list of Minor Environmental Improvement (MEI) projects for which they have maintenance responsibility; and
 - (ii) comply with the relevant HAD guidelines and government circulars in implementing MEI projects.
- (b) We have awarded term contracts for, amongst others, grass cutting in three districts in the New Territories. We plan to expand the term contract system to cover the remaining districts in April 2005.


- (c) We are now in the process of reviewing the following arrangements and will revise the relevant guidelines where necessary –
- (i) the need to conduct annual checks for projects requiring maintenance to a high standard; and
 - (ii) the granting of cash assistance to rural committees to undertake grass-cutting jobs.

Submission of Annual District Plans (Para 5.14)

We have drawn up a set of standard procedures for monitoring the submission of annual district plans (ADPs) by core departments. All Districts have been requested to adhere to the standard procedures with effect from 1 January 2005.

DC Homepages (Para.6.19)

- (a) We have advised the DCs to follow the Government Homepages Guidelines, stressing that they largely reflect the industry's best practices for homepage design, maintenance and content management.
- (b) We would assist DCs in drawing up short and long term improvement plans for their respective DC Homepages having regard to the current level of compliance with the relevant audit recommendations, individual district needs and characteristics.
- (c) As regards the use of DC funds for developing additional DC homepages, we have reviewed the issue and revised the existing arrangement so that DC funds can be used for one-off development and/or annual enhancement/maintenance of these homepages on a project-by-project basis.


(TSE Man-shing)
for Director of Home Affairs

c.c. D of Audit
CIR

Cases of Non-compliance with HAD Guidelines on the Reimbursement of the Operating Expenses Allowance (OEA) and the Information Technology and Other Support Grant (ITOSG) to District Council (DC) Members

(A) : Employment of assistants

Area of Non-compliance	Follow-up Action or Reason for Not Taking Follow-up Action
<p>(i) Non-submission of employment contracts [5 cases]</p> <p>Non-submission of written statements confirming that the assistants are not DC members' relatives [20 cases]</p>	<ul style="list-style-type: none"> • We will request members concerned to submit certified copies of the relevant employment contracts, or declarations if they are unable to provide the employment contracts. • We will request members concerned to submit written statements confirming that the assistants they employed are not their relatives.
<p>(ii) Monthly salaries paid to assistants different from those specified in the employment contracts [5 cases]</p>	<ul style="list-style-type: none"> • We will request members concerned to submit written statements confirming the change in salary.
<p>(iii) Assistants' salary receipts without identity card numbers [30 cases]</p>	<ul style="list-style-type: none"> • We will specify this requirement in the revised guidelines to DC members and ensure strict compliance with it.

(B) : Office accommodation

Area of Non-compliance	Follow-up Action or Reason for Not Taking Follow-up Action
<p>(i) Rental/management fee receipts without owner's name, identity card number or signature [19 cases]</p>	<ul style="list-style-type: none"> • We will specify this requirement in the revised guidelines to DC members and ensure strict compliance with it.
<p>(ii) Non-submission of agreements on joint offices [2 cases]</p>	<ul style="list-style-type: none"> • We will request members concerned to submit agreements on joint offices.

(C): Claims for non-reimbursable items

Area of Non-compliance	Follow-up Action or Reason for Not Taking Follow-up Action
<p>(i) Publicity items containing information other than those allowed in the HAD Guidelines [63 cases]</p>	<p><u>Name Cards containing photographs</u></p> <ul style="list-style-type: none">• We have all along been considering name cards as printed items, which are allowed to contain photographs. No follow-up action is required for these claims. <p><u>Publicity items containing photographs</u></p> <ul style="list-style-type: none">• When we revised the HAD Guidelines on 1 June 2002, the eligibility criteria for reimbursing publicity items were relaxed such that information essential for discharging members' DC duties became acceptable. Against this background, we consider that publicity items containing photographs are reimbursable. No follow-up action is required for claims for publicity items containing photographs that were purchased on or after 1 June 2002. <p><u>Other publicity items</u></p> <ul style="list-style-type: none">• We will request members concerned to refund the relevant amount to the Government.
<p>(ii) IDD, roaming, international calls charges and expenses for telephone lines not made known to the public [38 cases]</p>	<ul style="list-style-type: none">• We will request members concerned to refund the relevant amount to the Government.

<p>(iii) Non-publicity materials, purchase of battery, rental of photocopier and surcharge for late payment [44 cases]</p>	<p><u>Purchase of battery</u></p> <ul style="list-style-type: none"> We consider it reasonable for DC members to claim reimbursement of batteries, which are used to support the functioning of various equipments. No follow-up action is considered necessary. <p><u>Other items</u></p> <ul style="list-style-type: none"> We will request members concerned to refund the relevant amount to the Government.
<p>(iv) Reimbursable items introduced with effect from 1 June 2002 but paid before 1 June 2002 [2 cases]</p>	<ul style="list-style-type: none"> We will request members concerned to refund the relevant amount to the Government.

(D): Improper reimbursement

Area of Non-compliance	Follow-up Action or Reason for Not Taking Follow-up Action
<p>(i) Claims without proper receipts [11 cases]</p>	<ul style="list-style-type: none"> We will request members concerned to submit certified supporting documents, or declarations if they cannot provide the required documents.
<p>(ii) Double payment [3 cases]</p>	<ul style="list-style-type: none"> We will request members concerned to refund the relevant amount to the Government.
<p>(iii) Rebate, subsidy, compensation and refund not refunded to the Government [3 cases]</p>	<ul style="list-style-type: none"> We will request members concerned to refund the relevant amount to the Government.
<p>(iv) Employee insurance for two staff but only one assistant was registered with the DC secretariat [1 case]</p>	

(v) Expenses on rental of ward offices not reimbursed according to tenancy agreements [1 case]	<ul style="list-style-type: none"> We will request members concerned to refund the relevant amount to the Government.
--	--

(E): Purchase of equipment and furniture

Area of Non-compliance	Follow-up Action or Reason for Not Taking Follow-up Action
(i) Non-submission of photographs of equipment and furniture [29 DC members]	<ul style="list-style-type: none"> It is specified in the HAD Guidelines that "the DC secretariats should request DC members to produce photographs of the items procured <u>as far as practicable</u> when they submit claims for reimbursement". As this is only advisory, members who did not submit photographs of equipment and furniture should not be regarded as having violated the HAD guidelines. Therefore, no follow-up action is required. We will remind members to submit photographs as far as practicable.
(ii) Non-submission of inventory records by DC members [7 DOs]	<ul style="list-style-type: none"> The inventory records have in fact been prepared and kept by the District Council secretariats. No remedial action is required. We will remind staff of District Council secretariats to ensure full compliance with this requirement in future.

(F): Time limit for making reimbursement claims

Area of Non-compliance	Follow-up Action or Reason for Not Taking Follow-up Action
(i) Claims submitted two months after payment was made [41 DC members]	<ul style="list-style-type: none">• It is specified in the HAD guidelines that “DC members are advised to submit the claims for reimbursement of expenses incurred within the following month”.• As this is only advisory, members not adhering to this requirement cannot be seen as having violated the HAD guidelines. Hence, no follow-up action is required.• We will remind members to submit claims as soon as practicable.
(ii) Claims submitted two months after the end of the previous calendar year cycle [4 cases]	<ul style="list-style-type: none">• We will request members concerned to refund the relevant amount to the Government.
(iii) Payments straddling two calendar years not apportioned and charged to the provision of the respective calendar year [20 cases]	<ul style="list-style-type: none">• We will ensure full compliance with this requirement in future.

(G): Monthly statement for DC Members

Area of Non-compliance	Follow-up Action or Reason for not Taking Follow-up Action
(i) Monthly statements not provided to DC members [6 DOs]	<ul style="list-style-type: none">• It is stipulated in the HAD Guidelines that “the DC secretariats are <u>advised</u> to produce monthly statements showing the cumulative reimbursed amount and the unclaimed balance to individual DC members”.• As this is only advisory, DOs that did not provide monthly statements to DC members cannot be regarded as having breached the guidelines.• In fact, DC members can approach DOs anytime for up-to-date cumulative reimbursed position and unclaimed balance.

**Hearings of the Public Accounts Committee
Value-for-Money Audit on the English Schools Foundation**

Chapter Three: Government Subsidies to the ESF

Speaking Notes for the SEM

Thank you, Chairman.

2. First of all, we are happy to note that the Director of Audit has in paragraph 2.24 of Chapter Three of his Report indicated his overall comments on the subvention review –

- (a) There is a genuine preferential treatment of the ESF over other international schools as far as Government subvention is concerned.
- (b) The historical reason for the subvention has to be revisited in the present-day context, giving regard to the development of a vibrant international school sector outside the ESF system in Hong Kong.

3. We have been conscientiously pursuing this subvention review over the past few years through frequent discussions with the ESF and would, as suggested by the Director of Audit, expedite action to complete the review.

Principle: Students' Benefits as Top Priority

4. Instead of going into the details of how we wish to change the subvention policy, we would rather make one clear point here. Government attaches great importance to education. The well-being of the students is our first and foremost considerations in devising our policies. Irrespective of how the subvention arrangement would be in the future, the interest of our children is not to be undermined. I am glad that this very principle is shared by the ESF and many stakeholders including parents and teachers. Notwithstanding the principled approach adopted by EMB, we have been very modest in the efficiency savings demanded of ESF in the past few years. Civil service payout aside, the annual efficiency savings just amount to around 3%, which is not out of line with that generally applied to public sector organizations.

When translated into the entire ESF budget, this only means a 1% cut. Facts speak louder than words. EMB has exercised the utmost care in ensuring that efficiency savings would not unduly affect education for our children.

5. Certainly, there could be diverse views on what best serve the need of our children. But one thing is clear – wastefulness and imprudent use of funds will not serve our children, especially when there are competing priorities for limited funds. The arguments of fair play, cost-effectiveness, resource constraints and professional accountability all come into play. We could have extensive discussion or even debate in future.

Considerations

Subvention and Accountability

6. During the past PAC sessions, we have extensively deliberated on the governance reform of the ESF. We believe that there is no effective institution without effective governance. We shall repeat that the ESF requires rigorous reform to achieve the level of transparency and accountability required for a leading education institution. We see this an overriding priority, preceding over the subvention issue.

7. Other than the governance structure within the ESF, accountability is also required for every dollar the ESF now receives from Government and the parents. We never micro-manage. But when it comes to the time when clarification needs to be sought, the community deserves to have somebody in the ESF answerable, and may I stress, in a disinterested manner. To this, this audit exercise has been useful in exposing many interesting information which would not otherwise be available to the public, to EMB and I think, to a lot of Foundation and ExCom members.

8. The same accountability should apply to parents who indeed remain the biggest contributor to the ESF budget. At present, a parent representative sits on the ESF Executive Committee and many more on the ESF Foundation. Irrespective of how their views would be channeled after the governance reform, the ESF should ensure that parents are fully informed of what actually happens in the classroom and in the management office.

The ESF's Role

9. We note that the ESF has refused to be classified as an international school system. It has strongly defended its position as a local school by saying that its curriculum is adapted to the Hong Kong context and has enrolled a significant percentage of permanent resident children. But it is not something unique as most, if not all, other international schools also operate in the same way. A step further to the ESF, quite a few international schools outside the ESF system have developed a strong curriculum for learning of Chinese language, history and culture. Individual schools even have a student body with almost 90% of its children having at least one parent being ethnic Chinese. Hence what the ESF could state as justifications and what sets the ESF apart, as quoted in paragraph 2.22 in Chapter Three, is indeed an anomalous historical legacy.

Implications

10. In pursuing changes to the existing policy, we wish to highlight that no one is above the law in Hong Kong. That we must abide by the law is clearly stipulated in the Basic Law. On the ESF's concern about Article 144 of the Basic Law, we have obtained clear legal advice that "the proposal to withdraw recurrent subsidies from the ESF by adopting a phased approach was justifiable as a development and improvement of education under Article 136 of the Basic Law and was consistent with Article 144 read in the light of Article 136 of the Basic Law".

11. I shall emphasize the point of a "phased approach". This is not only a matter of law. Echoing the fundamental principle which I highlighted in the outset, our review and any changes arising from it must be consistent with students' best interest. This not only applies to students in Hong Kong generally, but also to those who have already been admitted to ESF schools.

12. We notice that concerns on fee increase have been widely raised among ESF parents. Some in the ESF have been quoted to have repeatedly suggested that withdrawal of Government subsidies would automatically mean a 40% hike in the current fee level. This is grossly misleading. Such a causal relationship between subvention and fee level can only be made if all of the following happen. First, the ESF intends to charge parents for every dollar of subsidies foregone. Secondly, the ESF feels that there is absolutely no room for efficiency savings despite economy of scale. Thirdly, the ESF does not intend to undertake any

improvement measures pursuant to the Director or Audit's observations. I hope none of the above is true. I also hope that the reference to 40% hike in school fee is just media misreporting. The facts are before us in the Audit reports – the cost effectiveness of the ESF, rather than Government subvention, has a greater impact on the level of ESF tuition fees.

Timetable and Way Forward

13. On the way forward, we have to repeat our first and foremost principle that benefits of the students should be given top priority. We therefore adopt an open mind. We would certainly appreciate views and comments from Members and the community. And I hope that, as elected representatives of the people, Honourable Members would deliberate on the Audit reports in a disinterested manner, setting aside their personal or other links with the ESF, and seeing the ESF not in isolation, but in the context of the entire education landscape. The community has a legitimate expectation that their elected representatives sitting on the Public Accounts Committee will not tolerate wastefulness and will demand nothing less than the prudent use of public funds in an accountable manner.

14. Thank you.

Opening Statement (Chapter 3)

The ESF appreciates the work of the Audit Commission and the EMB, in particular Prof. Arthur Li, in highlighting the need for reform of governance of the ESF. This has served to strengthen our resolve and increased the momentum for the needed changes to take place.

With regard to the subvention, there are both historic factors, and benefits for the future of Hong Kong that should be recognized.

The ESF was established by Ordinance in 1967. This was based on the recommendations of the 1965 Education Policy White Paper. The reasons stated in the White Paper (page 6 of the Audit Report) are as applicable today as they were in 1965. The only changes being paragraph (e). The majority of students in the ESF schools are now permanent residents rather than British expatriates. The fact remains that despite the change in sovereignty the need for good quality English medium education continues to exist and indeed grow. This is evidenced by the increasing number of schools opened by the ESF at the behest of the Government, and the growth in the number of students in our schools from about 10,000 in 1997 to about 12,500 in 2005. The long waiting lists in many of our schools also attest to the robust demand for an ESF education.

The parity of subsidy principle was clearly stated in the White Paper and it was on this basis that the ESF was established by Ordinance. In 1979 six government schools entered the ESF on the understanding that parity of subsidy would be maintained. As late as 1995 when the basis for ESF funding was amended, it was done so in order to “better reflect” the principle of parity of subsidy. Discussions between ESF officers and EMB in 1999-2000, on the future of the subvention, were never concluded. No proposal on changing the basis of ESF funding was ever put before the Foundation, the supreme governing body. The ESF’s position on the principle of parity of subsidy remains unchanged. ESF regards itself as an integral part of the local education system, as entitled to government funding as other schools in the aided sector.

In 1995 the government reviewed subsidies to international schools. ESF was not consulted during this exercise. The EMB Working Group defined international schools as schools which follow a non-local curriculum and whose students do not sit for local examinations. But the type of education provided by the ESF schools as defined in the Ordinance is “... a modern liberal education through the medium of the English language to boys and girls who are able to benefit from such an education.” There is no mention of any international curriculum. This aside, there is the question as to whether the definition used by the Working Group still applies in the face of changes in the curriculum of some aided schools who now offer a non- Hong Kong curriculum. Furthermore ESF schools have been modifying their curriculum; in the context of the change to the IB the phrase “the British curriculum” no longer applies. Even if ESF students do not sit for the local examination the local tertiary institutions are increasingly willing to take in students from the ESF through the non-JUPAS route.

Article 144 of the Basic Law guarantees that policies on subvention prior to 1997 shall be “maintained”. ESF sees no contradiction between this Article and Article 136 as the latter makes clear that policies on education should be “on the basis of the previous educational system”. ESF is a part of the previous educational system and should not unilaterally be excluded from the government aided sector. Given the historic links between the EMB and the ESF, those in the community who elect to send their children to ESF do have a reasonable expectation that ESF will continue to be part of that sector.

ESF will continue to serve a distinct need as part of Hong Kong’s educational service. No longer do most ESF families return to other countries. 81% of present students are Hong Kong people: permanent residents. ESF schools not only assist Hong Kong in attracting talent and investment by provision of affordable, high quality education, to incoming expatriates, but now serve a significant sector of local Hong Kong people. Among these are returning Chinese who hold foreign passports and for whom English may be the first language, people from other Asian countries who are long term residents, Eurasians, as well as local families whose requirements are best met through ESF schools. It is a myth to assume that these groups are necessarily those who could afford a fully private education. ESF does not claim a special advantage over international schools but believes that it provides EMB with a group of schools that serve a particular need for an inclusive, open access education (including for those with special educational needs) with an international dimension as befits an international city.

ESF serves the Hong Kong economy and society. In the absence of an affordable ESF, the EMB and Hong Kong generally would incur costs. ESF assists Hong Kong in its positioning as an international city by attracting and retaining investment and talent to Hong Kong, and providing an international dimension to the EMB’s educational service. Former ESF students now work in all aspects of professional life in Hong Kong, contributing to the local economy the language and other skills acquired at ESF schools, while remaining part of a wider network of international connections. ESF would welcome then an evaluation by EMB of the contribution of ESF and international Schools to Hong Kong society and economy, and the needs of the mother tongue English community.

ESF believes that there should be no alteration of the parity of subsidy principle until the value of ESF to Hong Kong, and the needs of those who require mother tongue English education, have been formally evaluated.



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Your Ref: CB(3)PAC/R43

Ms Dora Wai
Public Accounts Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

28 December 2004
(By Fax 2537 1204 and Post)

Dear Ms. Wai,

Re Chapter 3: Government Subsidies to the English Schools Foundation

Thank you for your fax/letter of December 21st requesting ESF to clarify its position within the education sector with regard to whether ESF considers itself part of the local system or the international one.

Hong Kong is an international city with ambitions to become Asia's World City. Among those living and working in Hong Kong are people from around the world, including ethnic Chinese who hold passports of other countries, people of other Asian ethnicities (e.g. from the Indian Subcontinent), Eurasians, as well as those who would traditionally have been categorized as 'expatriate'. These groups have permanent residence rights in Hong Kong; they contribute to the local economy, pay taxes and consider themselves to be 'Hong Kongers'.

ESF serves people in those categories as well as an increasing number of local Chinese families. With regard to our student population we do not regard a distinction between 'local' and 'international' as a meaningful one. In Hong Kong many international schools serve local families. In ESF schools only 18% of children are now 'Caucasian' with over 60% ethnically Chinese or Eurasian, and nearly 80% Asian. 81% of students are permanent residents. The most commonly spoken first language is English, one of Hong Kong's official languages.

ESF schools, like international schools, teach to a non-local curriculum; some local subvented schools teach to an international curriculum. ESF's curriculum, especially in the primary sector, is in fact a localized version of the British National Curriculum. Hong Kong's universities accept local students with 'overseas' examination qualifications. Again, the boundary between what is 'local' and 'international' is becoming blurred.



With regard to employment of teachers, it is true that ESF schools recruit most of their staff from the English speaking world as would be expected of a first language English school system committed to high standards of teaching in that medium.

ESF regards itself as an integral part of the local education system, providing the system with an international dimension, as befits an international city. Our mission statement commits us to serve Hong Kong and the region. ESF schools meet a need in the community for a high quality, affordable education in the medium of English. Most ESF families cannot access the local system given the competitive nature of entry into many EMI Band One schools, and the necessity in most of them for children to prove a high competency in Chinese language. While some families send their children to ESF schools by choice, because of their international flavour, high standards of English and liberal teaching methods, many families have a limited choice or no choice at all. ESF provides an affordable alternative for those for whom the mainstream system is inaccessible or inappropriate, and the purely private which is often unaffordable.

It is true that before 1997 ESF served a mainly expatriate clientele. With the growing global economy, the old distinctions between 'local' and 'expatriate' are blurred. Gone are the days when professionals from other countries necessarily enjoy generous packages that include subsidized education in ESF or international schools. ESF now serves a different 'expatriate' market, many of whom are employed on terms no different to those employed locally. Many of these families have qualified for permanent residence rights. ESF believes that it makes an important contribution to the education system, in providing this valued part of the community with an affordable, high quality education service.

As to whether ESF should be considered to be part of the international school system, we acknowledge that there are areas of comparability. Where we can claim a measure of distinctiveness is in our more inclusive philosophy. ESF schools are non-selective (except for the English admissions test) and we include in our number about 10% who are in receipt of some form of special needs support.

ESF's positioning as an integral part of the local system is underpinned by the Ordinance that established the Foundation in 1967, and which subsequently embraced 16 schools. This embeds ESF in the local system. We are grateful for the funding that accompanies this. We also gratefully accept the responsibilities that come with being part of the local system. ESF are partners of the EMB, working with them on a number of initiatives: the opening of PIS schools, work on continuous professional development, school evaluation and so on. When the Canadian Overseas International College went bankrupt, it was to the ESF that the EMB turned to launch the rescue operation that resulted in the opening of the Phoenix International School in 2002. ESF also accepts, as the recent Audit process shows, the accountability that comes from being part of the local system and in receipt of public funds.



英基學校協會
ENGLISH SCHOOLS FOUNDATION

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In summary ESF does regard itself as an integral part of the local education system but also acknowledges that other institutions, now nominally 'international', could also make this claim. We make no claim to exclusivity and would favour an evaluation of the contribution to the economy and society of Hong Kong of all schools offering an international dimension, with a particular review of the education available to English speaking children in Hong Kong.

The English Schools Foundation considers itself to be a Hong Kong institution, committed not to any other country, denomination or international movement, but to Hong Kong's future as an international city, catering to those who make Hong Kong their home and who contribute to this city's livelihood.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive

PS Please be advised that a soft copy of this letter has been emailed to cwywong@lcgeo.gov.hk while the Chinese version will be submitted to you at a later date.

cc Secretary for Education and Manpower
Secretary for Financial Services and the Treasury (Attn : Mr Manfred WONG)
Director of Audit
Chairman, English Schools Foundation

建立優良教育 承擔香港未來
COMMITTED TO HONG KONG'S FUTURE AND
TO EXCELLENCE IN EDUCATION

**Extract from the minutes of ESF Foundation meeting
held on 14 December 2000**

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Present:

EXECUTIVE COMMITTEE

Mr J Shroff	Chairman
Mr J Shanahan	Vice-Chairman
Mr G Macnaughton	Treasurer
Ms J Wisker	Secretary
Mr T Hoffman	Chairman, Management Committee
Mrs I Rushworth	Chairman, JCPTA
Mr D Cotton	Chairman, Academic Committee
Mr D Reeves	Chairman, Staff Council

GOVERNMENT AND COMMUNITY REPRESENTATIVES

A. Marden	Marden Foundation
Gordon Lamb	China Light and Power Company
M.A. Shah	City University of Hong Kong
The Hon. T.W.H. Ha	The Bishop of Victoria

PARENTS

Aman Shah	Sha Tin College
B. Yiu	Island School
G. Garder	Glenealy School
J. Parkinson	Bradbury School
M. Bayliss	Bradbury School
M. Haynes	West Island School
N. Bilcliffe	Kennedy School
N. Sallnow-Smith	Peak School
P. Hodson	Peak School
Richard St. Paul	Kowloon Junior School

TEACHERS

A. Richardson	JCSRS
C. Robertshaw	Peak School
D. May	Kowloon Junior School
J. Choules	Sha Tin Junior School
M. Anderson	Kennedy School
M. McNally	Glenealy School
D. Boyle	West Island School
K. Quayle	Bradbury School
M. Foakes	West Island School
R. Abraham	Island School

R. Carthy
R. James
Richard St. Paul

Kennedy School
Sha Tin Junior School
KGV School

PRINCIPALS

Anne Wilkinson
B. Gordon Lewis
David James
Denis Cocks
Mike Doherty
Perry Tunesi
Robert Lyden

Principal, Bradbury School
Principal, Sha Tin Junior School
Principal, Island School
Principal, KGV School
Head, JCSRS
Principal, Peak School
Principal, Beacon Hill School

SCHOOL COUNCIL CHAIRMEN

E. Tai
G. McBride
J. Shanahan
K. Forestier
S. Ka
S. Nanda
T. Hoffman

Chairman, West Island School
Chair, Quarry Bay School
Chairman, KGV School
Chair, Glenealy School
Chair, Peak School
Chairman, Kennedy School
Chairman, Island School

NON-TEACHING STAFF

Amy Lai
Sheila Foster

IN ATTENDANCE

John Tustin
John Bohan
David Coles
David West
Michael Wood
Cynthia Brown
Jeni Fieldhouse
Chris Forse

Human Resources Director
Financial Controller
Education Officer
Education Officer
Educational Psychologist
Personal Assistant to Jennifer Wisker
Principal, Sheung Wan Kindergarten
Deputy Principal, Island School

Apologies

A. Williams
C. Rowlands
C.K. Tang *Tang*
Chris Smith
D. Arnold
David Harrison
Dr. V. Lau
Eirene Yeung
G. Caldicott
Gareth Davies
Hon. Jasper Tsang Yak-Shing
Hon. Ronald Arculli
J. Csete
L. Coghlan
L.C. Lam

Cathay Pacific Airways
Sha Tin College
Education Department
Head, JCSRC
Sha Tin College
Principal, Quarry Bay School
Senior Non-Expatriate Officers' Association
General Chamber of Commerce
General Chamber of Commerce
Principal, Kowloon Junior School
Legislative Council
Legislative Council
Sha Tin Junior School
Quarry Bay School
Manager, Building Management Department

Liz Muscroft
 J. Ainsworth
 J. Brewster
 J. Sommerau
 K. Chan
 Lo Kong Kai
 M. Bowles
 M. Brown
 M. Dowie
 M. Hill
 M. Tanner
 M. Watts
 M.Y. Cheng
 Matthew Cheung
 Minnie Li
 N. Chan
 N. Martell
 N. Straughen
 P. Chillingworth
 P. Hamblin
 P. Johnston
 P. Leung
 P.W. Liu
 Peter Falvey
 R. Dyer
 R. Gardener
 R. Memnoni
 Rev. B. Prior
 S. Cannell
 S. Tait
 S.P. Balani
 Vanessa Bingham
 W. Arnold

Education Officer
 Kennedy School
 Peak School
 South Island School
 JCSRS
 The Roman Catholic Bishop
 John Swire and Sons
 Clearwater Bay School
 KGV School
 Clearwater Bay School
 Island School
 Quarry Bay School
 Education Department
 Director of Education
 Hong Kong Electric Company
 Jardine Matheson and Company
 Sha Tin Junior School
 Glenealy School
 Island School
 South Island School
 Sha Tin College
 Education Department
 Chinese University of Hong Kong
 University of Hong Kong
 West Island School
 South Island School
 KGV School
 Union and Methodist Churches
 Quarry Bay School
 Hongkong and Shanghai Bank
 General Chamber of Commerce
 Principal, Kennedy School
 Sha Tin Junior School

SECRETARY'S REPORT:

ESF SUBVENTION

Last year I spoke of the issue of the ESF grant which has supported ESF since 1967 and in the case of the Government's English schools long before that.

As a result of lengthy negotiation, the grant has been capped at its current level apart from growth in student numbers. So effectively, the principle of parity has been conceded. It was unrealistic with the Government spending so much on its own programme of reform that we should also benefit thereby depriving the local sector of much-needed resources. However, we shall reserve the right to go back to Government should inflation bite and threaten our viability.

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16 March 2000

Joseph W.O. Wong, J.P.
Secretary for Education and Manpower
Education and Manpower Bureau
9th Floor, CGO (West Wing)
Ice House Street
Central, Hong Kong

Dear Joseph,

First of all, congratulations on your next career move. It seems that you have only been at the Education and Manpower Bureau for a short while and yet you have made a significant impact.

Before you leave, I thought it would be helpful if I summarised the main points the Chairman, John Bohan and I took away with us from our meeting with you, the Director of Education and other colleagues on the 22nd February.

We were very heartened by your introductory remarks that you would ensure that the removal of the ESF subsidy would be very gradual and not affect our viability and that you wished to demonstrate the Government's continuous support for our organisation as an essential part of the infrastructure of Hong Kong as an international city. In particular, we were encouraged by your statements that ESF schools are in an entirely different category from international schools and play an important role in providing parents with choice and diversity.

Basically, we understand that you are intending at some future date to cap our grant: that you consider that any new classes should be funded by ESF in their entirety. You are proposing a phasing programme with the subsidy gradually reducing over a period of time with a start date yet to be agreed.

Recognising the important role we play in Hong Kong, (the historic nature of our subsidy going back to 1902 in respect of some former government schools), you are prepared to be as flexible as possible in considering the future use of land which ESF currently occupies, both our school and apartment sites so that ESF can generate income to compensate for the removal of the subsidy and also to provide for much-needed expansion.

In response our Chairman was concerned to define "flexibility". He stressed again the fact that 80% of our students are Chinese returnees to Hong Kong; most paid their own fees and therefore there should not to be an undue burden placed on the fee payer. He emphasised that the period of phasing out of the subsidy should stretch over thirteen years, i.e. the full programme of ESF education, so that current fee payers would not be affected and notice could be given to the parents of new students that at an agreed date their fees will be increased.

We understood from you that any change of usage of our sites would need to be within a broadly educational non-profit making context, yet you recognised that some commercial developments were necessary within that framework if the required increase in our income is to equate with the loss of grant over time.



Joseph W.O. Wang, J.P.
Secretary for Education and Manpower
16th March 2000
Page 2

We agreed that as a first step we would approach our advisors, Brooke International Associates. They will be able to provide us with an up to date assessment of our sites by the end of April.

Meanwhile, as you will appreciate to stop speculation, I have had to advise our Executive Committee on developments and will give you their formal response once they have had the opportunity to examine, in greater detail, the implications of a frozen subsidy on both fees and staff conditions, together with an assumption of income arising from entrepreneurial activities within an educational framework. That scenario looked at most optimistically should mean a minimum increase in fees and reduction in the current conditions of employment of our staff.

The Chairman has therefore convened the Executive Committee together with additional principal, parent and teacher representatives, to consider these issues. Each constituent member of the Board will consult with their specific constituency, i.e. parents, teachers, community, to receive ideas which we shall feed into our planning.

I hope you will agree that I have given a fair summary of our discussions.

With best wishes.

Yours sincerely,

Jennifer Wisker
Chief Executive
The English Schools Foundation

c.c : Mrs. Fanny Law, Director of Education
Mr. Jal Shroff, ESF Chairman
Mr. John Bohan, ESF Financial Controller

JW/cb

教育統籌局



EDUCATION AND MANPOWER BUREAU

本局檔號 Our Ref.: (30) in EMBCR 15/2041/99
來函檔號 Your Ref.:

電子郵件 E-mail: embinfo@emb.gcu.gov.hk
電話 Telephone: 2810 2018
傳真 Faxline: 2530 3780

13 April 2000

Jennifer Wiker
Chief Executive
The English Schools Foundation
43B Stubbs Road
Hong Kong

Dear Jennifer,

**Funding Arrangements for
English Schools Foundation (ESF) Schools**

Thank you for your letter of 16 March which gives a fair summary of the main points discussed at the meeting on 22 February 2000. However, I would like to take this opportunity to elaborate on a number of points.

First, I would like to put down a marker in relation to the Foundation's proposal to modify the land lease conditions of some ESF schools. I understand that one idea which the Foundation has in mind is to re-provision Island School at Borret Road to another site, and to redevelop the existing site for other purposes. As I explained to you over the telephone earlier, Government will have great difficulties agreeing to ESF redeveloping the Borret Road site if it is no longer required for educational purposes. Instead, we would expect the site to be returned to Government. We are prepared, however, to consider providing a replacement site to the Foundation for the redevelopment or expansion of Island School, or re-provisioning Island School at an existing ESF school site.

Secondly, we have taken up your suggestion that, in order to allow time for ESF to establish alternative income sources, as an interim measure, Government will only freeze the ESF per class subsidy at the prevailing level (i.e. the 1999/2000 school year level) without inflation adjustment with effect

from the coming school year (i.e. the 2000/01 school year). However, the number of eligible ESF classes will not be capped. I understand that this interim arrangement is acceptable to the Foundation and will not have any significant impact on fees. I now write to seek your formal agreement to this staged approach.

Thirdly, I understand that the ESF will submit proposals regarding redevelopment of existing school sites and possible expansion of ESF's activities to Government. However, I must emphasize that the approval of the Foundation's application for a private independent school (PIS) is independent of the proposal to phase out Government's subsidies. Indeed, as you know, applications for running PIS are being considered by a School Allocation Committee comprising government and non-government representatives and all applications will be considered on the merits of the applications.

Separately, I note that the Executive Committee of the Foundation has been advised of the latest development, and that in turn the Executive Committee will be consulting principal, parent and teacher representatives. While we have no objection to this, I trust that the deliberation will be conducted on a strictly confidential basis, as agreed at our meeting on 22 February. I also trust that Government's continual support for ESF should be emphasized.

I look forward to receiving an early formal response from the Foundation on the various points raised at the 22 February meeting, and arriving at a mutually acceptable agreement on the arrangement for phasing out Government's subsidies.

Yours sincerely,



(Joseph W P Wong)
Secretary for Education and Manpower

cc Director of Education (Attn: Mrs Fanny Law)



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15 January 2001

Mr. Joseph Y.T. Lai
Education and Manpower Bureau
9th Floor
CGO (West Wing)
Ice House Street
Central, Hong Kong

Dear Mr. Lai,

Re : Funding Arrangement for English Schools Foundation Schools

Thank you for your letter dated 5th January 2001 concerning progress towards achieving long-term funding arrangements for ESF schools.

Since I last wrote to you, the Executive Committee of the Foundation has considered a report on its property assets prepared by Brooke International. The detailed recommendations of this report are under consideration by a small group of Executive Committee members.

I would emphasise however, that unless a radical scheme was envisaged that involves commercial use of our leading school sites, it is highly unlikely that sufficient revenue could be raised to replace the third of our costs currently covered by the subvention. It is, in our opinion, not the time to embark on such a scheme in view of political sensitivity in its widest sense and also the current level of the property market.

In addition, the Foundation has conducted a fundamental review of benefits paid to teaching staff not only for the purpose of recruitment and retention to maintain quality, but also as part of our strategy towards reducing our cost base. As a result, the package of benefits which will now be on offer is considerably less than that currently offered through overseas terms and more recently, rental supplement, (known as salary supplement). Basically, staff currently employed on local terms who do not get benefits from any other source, and those whom we appoint from 1st September 2001 onwards will qualify for this much-reduced package. No further overseas packages for teaching staff will be offered. It is anticipated that a saving of around H.K.\$20 million will eventually be accrued (after a period of six years as these new measures come into effect). It is likely this sum will increase over time as post-holders currently on overseas terms / salary supplements leave and are replaced by staff holding the new benefit package.

I would add that both the Chairman and I were much heartened by our recent discussions at the end of the last year with Matthew Cheung, Director of Education, and were delighted to show



Mr. Joseph Y.T. Lai
Education and Manpower Bureau
15th January 2001
Page 2

him some aspects of an ESF education. We were pleased that he confirmed your view of us, basically that the ESF is a permanent fixture in Hong Kong. The Chairman and I made it clear to Mr. Cheung, as we have to you, that we have made a substantial sacrifice in foregoing the principle of parity. What this means is that effectively the subvention is frozen at current levels thus reducing Government expenditure on ESF under the Codes of Aid. This development has not been popular with ESF parents as we advised Mr. Cheung.

We shall be seeking ways to increase revenue as inevitably with the grant capped, the amount we shall eventually be required to finance ourselves will grow as inflation returns. If, however, inflation increases to the extent that our viability is threatened, we shall make representations to you to have the principle of parity restored. We cannot reduce staff benefits further without comprising the quality of our education provided: a substantial rise in fees would not be acceptable to our parents.

As you will appreciate, we are doing what we can to reduce our dependence on government funding but we do need the long time scale if our stability is to be maintained.

With best wishes for the New Year 2001.

Yours sincerely,

Jennifer Wisker
Chief Executive
English Schools Foundation

c.c : Mr. Matthew Cheung, Director of Education
Mr. Jal Shroff, ESF, Chairman
Mr. John Bohan, ESF, Financial Controller

JW/cb

**Reply of 17 January 2005 from
Mr Jal Shroff, former Chairman of the English Schools Foundation**

I refer to your letter CB(3)/PAC/R43 dated 14 January 2005.

Chapter 3: Government subsidies to the ESF

Your question "a" i.e. "whether I had agreed with Government that the parity of subsidy principle be forgone and that the government subsidy to ESF be phased out over 13 years".

To the best of my knowledge there was NO FIRM AGREEMENT with Government that the parity of subsidy principle be forgone and that the parity of subsidy principle be phased out over thirteen years.

If there had been such an agreement the matter would have been resolved and we would not be facing the situation we are today.

My understanding is that I had in discussion with a representative of the EMB suggested that one way to resolve the issue was for EMB to phase out the subsidy over a period of thirteen years PLUS modification of ALL our land lease conditions so that we had the option to redevelop some of the school sites commercially to generate additional income to make up the loss of revenue from the subsidy.

It was my belief that that there was a reasonable chance for the Executive Committee and the Foundation to accept this as a "fair" solution. The EMB was not in a position to agree to the modification of land lease conditions and again as far as I can remember the discussion did not continue.

Chapter 4: Corporate Governance & Headquarters administration of the ESF

Your question "b" i.e. "whether I had discussions with relevant government officials relating to corporate governance of the ESF; if so, contents of the discussion and the officials with whom I discussed and the occasion when the discussions were held; if not, why not"

With all due respect I must point out that I was Chairman for over nine years and during that time I obviously met with many government officials and no doubt discussed all aspects relating to obtaining new sites for additional ESF schools, finances, lack of places within our system to cater for children of new arrivals, the problem associated with the make up of the body of the Foundation and no doubt corporate governance. It is impossible for me to give you a detailed and accurate response.

Let me once again draw your attention that the Executive Committee of the ESF has on it a representative of the EMB who is "privy" to all. On most occasions this representative is present during any discussions with members of the Education Department or EMB.

Your question "c" i.e. "you require details of my discussion with other ESF Executive Committee/Foundation members and/or ESF senior management on the arrangements in regard to the extra payments made to the three senior staff (Staff A, B & C) leaving ESF, and the justification for offering such payments to them."

In any "monetary" settlement made with senior ESF staff our criteria has always been to keep a balance between the "cost" and the interest of the students and the reputation of the ESF.

In every case where dismissal is involved, extensive consultation is carried out not only with members of the Executive Committee but where appropriate with the respective School Council members. In many cases legal advice is taken to ensure that the interest of the ESF is protected and non-disclosure agreements are signed.

Let me briefly comment on each of the three cases raised in the Audit Report (I would request that you respect confidentiality and non-disclosure agreements signed by the ESF and not expose us to any possible legal implications).

Staff "A" This involved a head-office staff and dismissal negotiations were finalized by the Secretary, approved by the Executive Committee and minuted.

Staff "B" This involved a head teacher who resigned in the middle of an external inspection of the school and the Secretary of the Foundation after due consultation decided that it was in the interest of the children that he should NOT continue as principal. In view of his 20 plus years of service in the ESF a special case was made for him to go on paid leave up to his final date of resignation (31st August 2003).

The Secretary was wrong not to have this minuted at one of the Executive Committee meetings.

Staff "C" I note that Mrs. Cherry Tse has on 11th January 2005 forwarded you a complete copy of the documents related to this case including the minutes of the Executive Committee meeting (encl. K) which authorised me as Chairman to negotiate "as would be necessary to effect termination". The Chairman of the Management Committee accompanied me in my discussions to finalize details of the termination with Staff "C". I have nothing further to add but would once again urge you to respect confidentiality.

Your question "d" i.e. "The reason why the sale of ESF surplus quarters without prior approval has occurred as mentioned in 5.28 of the Audit Report".

To the best of my knowledge, the Executive Committee had discussed the possibility of selling off certain "old" properties, at an appropriate time, as these properties involved high maintenance and were becoming uneconomical to hold on to, the Secretary, Chairman, Treasurer and Vice Chairman were given authority to make the final decision.

The ESF also employed the services of one or more property companies to advise us on all property transactions.

KPMG audit our accounts annually and I understand that all contracts dealing with the sale or purchase of property have been properly executed as per the ESF Ordinance requirements in section 12(4).

Jal Shroff
17 January 2005



中華人民共和國香港特別行政區政府總部教育統籌局
Education and Manpower Bureau
Government Secretariat, Government of the Hong Kong Special Administrative Region
The People's Republic of China

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24 January 2005

Ms Miranda Hon
Clerk to Committee
Public Accounts Committee
Legislative Council Secretariat
8 Jackson Road, Central
Hong Kong

Dear Ms Hon,

**The Director of Audit's Report on the
Results of Value for Money Audits (Report No. 43)**

Thank you for copying to us the email message of Mr Jal Shroff, the former Chairman of the English Schools Foundation ("ESF"), dated 17 January 2005. I would like to elaborate on the context within which the development covered in response to "Question (a)" took place.

Agreement on the Withdrawal of Subsidies

As we have explained to the Public Accounts Committee ("PAC"), the ESF has clearly acknowledged that the parity principle has foregone following the freeze of the subvention rate with effect from the 2000/01 school year. This has been documented in internal records within the ESF and formal correspondences with Government. The only trigger for revisiting the issue is when inflation threatens the ESF's viability. Irrespective of how one looks at it, logically, this trigger does not justify disowning the agreement to forego the parity principle especially when, after years of deflation, the prevailing price level remains significantly lower than that in 2000.

On the 13-year withdrawal programme, it is important to note that it is not dependent on the proposed land lease modification. As clearly illustrated by exchanges in 2000-2001, Government shares the

ESF's view that the subvention withdrawal should be properly managed with a reasonable transitional arrangement, which should comprise a basket of measures, with land lease modifications being one of the several possibilities mooted. Of note is the fact that, the then ESF Chief Executive's letter dated 15 January 2001 indicating clear concession on the parity principle took place after the communication by the then SEM on 13 April 2000 in respect of Government's reservation about land lease modification. In other words, the explicit agreement to forego the parity principle was given AFTER clear knowledge of the non-feasible nature of lease modification. In addition, other avenues for generating income and cutting costs were also touched upon in the course of the discussion. It was against this backdrop that the ESF applied for the allocation of sites for running two Private Independent Schools. The ESF has also indicated at an early stage of the negotiation that it would reduce its staff cost (cf. the then ESF Chief Executive's letter of 17 June 1999), though visible progress was only seen after a lapse of five years.

Indeed, to look at the question more fundamentally, the focus of the discussion was not on "whether" recurrent Government subsidies should be withdrawn, but rather on "how" the withdrawal should be phased. Government has been pursuing the review with goodwill, taking into account the possible impact on the ESF and its stakeholders. And that is also why, despite our principled approach, the reduction in subvention to the ESF has been rather mild notwithstanding the fiscal deficit.

Others

We also wish to take this opportunity to supplement our verbal advice with a written response on the following issues which have been covered in the hearing session on 10 January –

- (a) "Approval" of Annual Estimates of the ESF: There is no requirement under the Education Ordinance (Cap 279) or the English Schools Foundation Ordinance (Cap 1117) for the ESF to submit its annual estimates for "approval" by Government. Although it has been the ESF's understanding that its past submissions were intended for our approval, we only examine such estimates in considering the school fee level of the schools, calculating grants or in contexts for similar requirements. This generally applies to all categories of schools including aided schools. It is the

primary obligation for individual schools to exercise proper financial control and maintain their financial viability.

- (b) Overdraft Problem in the ESF: A Member raised concern about the overdraft problem of the ESF as evidenced in its audited accounts. As we responded on 10 January, we are aware of the problem. We wish to elaborate that in receiving the routine estimates from the ESF, we have indicated a need to maintain a smooth cashflow at least from the late 1990s.

In more recent years, we also noted that due to some non-recurrent reasons (e.g. lower income arising from the SARS outbreak and the commissioning of capital upgrading works in some ESF schools), the negative cashflow in the ESF at its financial year end (i.e. August) has increased. This is an issue that we look into in the context of our examination of the ESF estimates and audited accounts. We have also, during our informal exchanges with the ESF leadership, referred to the scope for evening out the cashflow of the ESF, especially given the rather stable and predictable spending patterns of educational establishments.

Yours sincerely,



(Mrs Cherry Tse)
for Secretary for Education and Manpower

c.c. Chairman, English Schools Foundation
Acting Secretary and Chief Executive, English Schools Foundation
Secretary for Financial Services and the Treasury
Director of Audit
Mr Jal Shroff



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**ENGLISH SCHOOLS FOUNDATION
SUBMISSION TO
THE PUBLIC ACCOUNTS COMMITTEE OF LEGCO**

**PAC HEARING ON
CHAPTERS 3, 4 AND 5 OF
REPORT NO. 43 OF THE DIRECTOR OF AUDIT**

10 DECEMBER 2004



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2. Membership of Executive Committee (As of 1 November 2004)

Chairman: Professor Felice Lieh Mak

Professor Felice Lieh Mak was elected Chairman of the English Schools Foundation (ESF) in March 2004. She is also Director, Medical Education Unit, Faculty of Medicine, The University of Hong Kong and Chairman, Medical Council of Hong Kong. She has served on the Education Commission, the Task Force on Language Benchmarking for School Teachers, and the Advisory Committee on Teacher Education and Qualifications.

Vice Chairman: Mr Christopher Erving

Mr Christopher Erving was elected Vice Chairman of the ESF in March 2004. Mr Erving is a solicitor and senior partner in a legal practice in Hong Kong.

Treasurer: Mr Samuel Yiu-kin Poon

Mr Samuel Yiu-kin Poon was appointed Treasurer of the ESF in November 2004. Mr Poon is a member of the Advisory Committee of The Securities and Futures Commission of Hong Kong and the Joint Committee on Student Finance under the Education and Manpower Bureau.

EMB Representative: Ms Maisie Chan

Ms Maisie Chan is Principal Assistant Secretary (Infrastructure and Research Support) at the Education and Manpower Bureau of the HKSAR. Ms Chan has represented the Government on the ESF Executive Committee since September 2004.

Acting Secretary and Chief Executive: Mr John Bohan

Mr Bohan has served as Acting Secretary and Chief Executive of the ESF since June 2003. He is also its Financial Controller.

Chairman, Management Committee: Mr Bill Sharp

Mr Bill Sharp has represented the ESF's Management Committee as its Chairman on the Executive Committee since March 2004. The Management Committee is comprised of the heads of the Councils of all ESF schools.

Chairperson, Joint Council of Parent Teacher Associations: Dr. Sarah Rigby

Dr. Sarah Rigby has represented the Joint Council of Parent Teacher Associations (JCPTA) of the ESF on the Executive Committee since February 2004. She is a parent of Quarry Bay School.

Chairman, Academic Committee: Mr Brian Driver

Mr Brian Driver is the principal of West Island School. He has represented the principals of all ESF schools, known as the Academic Committee, on the ESF Executive Committee since September 2004.

Chairman, Staff Council: Mr David Reeves

Mr. David Reeves has represented the Staff Council on the ESF Executive Committee since 1997. The Staff Council is comprised of representatives of teachers from all ESF schools. Mr Reeves is a teacher at Island school.



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3. ESF: Serving Hong Kong

ESF is an integral part of the local education system, created by Ordinance in 1967. From two schools in 1967, the ESF has grown to 16 schools in 2004. In 1979 the ESF subsumed six government English language schools. Bauhinia School opened in 2002, at the request of the Hong Kong government to cope with the increasing demand for places.

ESF provides a unique contribution to the EMB's portfolio of schools offering variety and choice. ESF provides the local system with an international dimension, as befits an international city. Its pedagogy encourages creative thinking, and investigative learning. Its graduating students enter top universities world-wide.

The ESF's mission is "to serve Hong Kong and the Region". It no longer serves mainly expatriate families. 81% of its families are permanent residents and the majority are ethnically Chinese. Thousands of its graduates are building their careers in Hong Kong.

ESF schools provide a world class education and its examination results bear comparison to the most selective and elite schools in the UK and globally. 98% of its graduating students passed the GCE Advanced Level examination, with 42% achieving grade A. 43% of our graduates attend UK universities, 20% go to the USA, and 30% to other countries. About 7% attend local universities and this number is growing.

ESF combines high quality education with affordability for Hong Kong families. **Parents and students express great satisfaction with the ESF schools,** valuing their ethos, teaching methodologies, high level English medium teaching, their success in examinations and university entrance and the schools' multi-cultural dimensions. There are long waiting lists for places in many of the schools.

The schools are open access with regard to ability, and the only qualification is that children can be educated in the English medium. About 10% are in receipt of special needs support, including those with severe or multiple learning difficulties.

ESF schools are staffed with over 90% Native English Teachers, and high-level English is the medium of learning. ESF schools teach to an **international curriculum adapted to local circumstances.** All students have an entitlement to study Putonghua. The schools are not beholden to an exclusive foreign culture or faith. Like international schools, ESF schools' multicultural profiles allow local students to develop a global perspective that enhances their value to an international city.

ESF takes pride in partnership with the EMB, and accepts responsibility for assisting the local system in such areas as school evaluation and continuous professional development. ESF has already entered dialogue with EMB with the aim to assist in the 3+3+4 reforms. Our experience in liberal studies and teaching methodologies can be invaluable in this.



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ESF has assisted in developing new schools for Hong Kong, most notably in the Private Independent School initiative where ESF is building two schools at the request of the government. ESF also agreed to take over the failed Canadian Overseas International College in 2001, reopening it as the Phoenix International School.

ESF is accountable to government. A member of the EMB sits on the ESF Executive Committee and its accounts are audited annually.

ESF benefits Hong Kong

The ESF receives a subvention that permits it to provide high quality, affordable education. 100% of the subvention goes into school classes not into the management system. The average subvention per child is currently about 12% lower than for students in local and DSS schools. ESF is grateful to the government for its support but also believes that **Hong Kong reaps a rich reward from its investment in the ESF system.**

- In high quality English medium education for Hong Kong people;
- In attracting talent and investment to Hong Kong's business community;
- In the 'multiplier' effects of attracting such talent and investment, enhancing the livelihood of the local people;
- In retaining talent in Hong Kong by provision of affordable education locally.
- In providing special education to students who would otherwise be a burden on the local system;
- In educating Hong Kong's leaders of tomorrow with a liberal education that develops critical thinking, creativity and decision-making skills particularly valued by the business community.

ESF serves sections of the community for whom alternative schools are inappropriate and/or unaffordable. This group (which includes some who fail to gain admission to local schools): 'returnees', those of other East and South Asian ethnicities, Eurasians, and expatriates all make a valuable contribution to Hong Kong society and economy. *Without an affordable system lying between the purely local and international/private, Hong Kong would incur social and economic costs that could outweigh the benefits to taxpayers of reducing the subvention.*

ESF does not claim a monopoly in quality education nor an exclusive right to subvention. **ESF believes that government support for international standard education should be expanded,** not weakened, allowing Hong Kong to become a centre for educational excellence in the region. ESF notes that cities in the mainland are encouraging foreign schools and systems to set up in China, enhancing English. Hong Kong will be the poorer should the unique partnership of ESF and EMB be placed in jeopardy.

ESF is a valuable asset for Hong Kong. ESF commits itself to offering value for money, and an enhanced partnership with EMB in its mission to makes Hong Kong a centre for educational excellence in Asia's 'World City'.



4. The Views of Parents on an ESF Education

The views of ESF parents as demonstrated by a recent survey and through comments made via an email hotline in response to the Audit Report, reveal the following thoughts on the applicability of the continuation of government funding of ESF schools.

Parents send their children to ESF schools for the following reasons:

Parents value the high quality of education provided by a highly qualified and experienced teaching staff, as illustrated by their excellent examination results. Parents believe that a stable teaching force makes an important contribution to this quality. *(Appendix 1, chart 1)*

ESF develops excellent English language skills taught by native English teachers. *(Appendix 1, chart 2)*

Many parents have no alternative to ESF schools for their children. Parents of Eurasian, Indian, and East Asian children who are often long term residents of Hong Kong require an English education taught by native speakers. Additionally, families returning to Hong Kong from abroad often require the type of education provided by ESF schools. These families are entitled to an affordable education. *(Appendix 1, charts 3a and 3b)*

ESF schools are affordable. Among ESF's customers are many who could not afford a more expensive education in Hong Kong or abroad. *(Appendix 1, chart 4)*

ESF parents value the choice that ESF offers, to a quality education in the medium of English with an international dimension as befits an international city. ESF provides variety and an alternative choice to the Hong Kong educational system. *(Appendix 1, chart 5)*

ESF schools offer good value with affordable schools achieving standards comparable to the best in the world. ESF schools offer not only good teaching but a wide and rich extra-curricular programme that develops the whole child. *(Appendix 1, chart 6)*

ESF schools are inclusive. They do not limit access only to the most able. They provide help to large numbers of students requiring special needs support.

ESF is an established system of 37 years which parents place trust in. *(Appendix 1, chart 7)*



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Parents are concerned about the possibility of withdrawal of government funding for ESF schools because:

- Many children would not fit into the local system because of their lack of Chinese medium competency.
- Some families could not retain residency in Hong Kong without affordable education: these include both Chinese returning families and expatriates.
- Families fear that the quality of the schools would be compromised.
- The unavailability of affordable ESF education could seriously affect the educational prospects of Hong Kong's children, with a negative effect on the quality of life in the SAR for future generations
- It is currently more expensive to the government to educate children in local and DSS schools than it is in ESF schools
- Any immediate loss of subvention would seriously disrupt the education of children now in ESF schools.

In summary parents wonder why the government is considering withdrawing support to an excellent system of schools that serves the residents and economy of Hong Kong so well. ESF education costs less for the government than education in local or DSS schools. Parents are aware that in other cities in China and the region that government is supportive of English language education, and are concerned that Hong Kong will begin to lag behind, losing its allure as an international city. Parents believe that government should be supporting more schools of the ESF type rather than withdrawing that support. They believe that no move should be made to reduce subvention until government fully evaluates the importance of English medium education to Hong Kong, English being one of Hong Kong's official languages and the global language of business.

Parents agree with the Audit Report's recommendations to ensure that the ESF provides good value for money, but believe that the issue of subvention is a distinct and separate issue, affecting the quality of life for many people and impacting on the Hong Kong economy.

Parents appeal to government not to make children, the present and future generations of ESF and Hong Kong citizens, suffer because of failings of governance and administration, for they are the innocents.



5. Responses to Specific Analyses in Chapters 3, 4 and 5 of Audit's Value for Money Study of ESF

ESF believes that it needs to provide supplementary data to provide a fuller and more balanced picture of certain of the conclusions and figures presented in Audit.

Chapter 4

Budgetary Control

The ESF wishes to demonstrate its track record in controlling income and expenditure relative to approved budgets. To this end your attention is drawn to the table on the following page.

The ESF's income has to be forecast based on likely enrolments. It is important that this is done realistically to ensure that a shortfall does not occur which could disrupt planned spending. This objective has been met over the 14 years as shown in the table.

It is necessary to exercise good control over expenditure, even if income is better than budget, to ensure that a disciplined approach is maintained. In 8 of the last 14 years, expenditure has been to within 1% of budget, and sometimes much closer. In 3 years Executive Committee (with advice) had approved additional maintenance expenditure early in the year, without which expenditure would have been very close to budget (this is marked with an asterisk).

A point to note is that most years' budgets projected only a small surplus. These small budgeted surpluses left only a small contingency for the unexpected. However, The Foundation has always sought to manage carefully without increasing fees to provide for high levels of contingencies.



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The English Schools Foundation
Statement of Accounts for the Years 1990/91 - 2003/04

SCHOOL YEAR	INCOME			EXPENDITURE			SURPLUS / (DEFICIT)		
	Budget HK\$M	Actual HK\$M	Variance Favorable / (Unfavorable) HK\$M % of Budget	Budget HK\$M	Actual HK\$M	Variance Favorable / (Unfavorable) HK\$M % of Budget	Budget HK\$M	Actual HK\$M	Variance Favorable / (Unfavorable) HK\$M
90-91	330.7	345.0	14.3 4.3%	327.7	327.7	0.0 0.0%	3.0	17.3	14.3
91-92	384.9	403.1	18.2 4.7%	383.2	392.4	(9.2)* (2.4%)*	1.7	10.7	9.0
92-93	455.1	468.6	13.5 3.0%	451.3	460.7	(9.4)* (2.1%)*	3.8	7.9	4.1
93-94	522.8	546.7	23.9 4.6%	522.8	522.8	0.0 0.0%	0.0	23.9	23.9
94-95	611.6	623.4	11.8 1.9%	608.9	608.5	0.4 0.1%	2.7	14.9	12.2
95-96	698.4	702.4	4.0 0.6%	693.1	692.1	1.0 0.1%	5.3	10.3	5.0
96-97	749.6	762.5	12.9 1.7%	741.4	744.5	(3.1) (0.4%)*	8.2	18.0	9.8
97-98	815.5	813.4	(2.1)** (0.3%)**	811.2	815.0	(3.8) (0.5%)*	4.3	(1.6)	(5.9)
98-99	868.7	878.4	9.7 1.1%	868.4	860.6	7.8 0.9%	0.3	17.8	17.5
99-00	887.4	917.4	30.0 3.4%	878.2	853.6	24.6 2.8%	9.2	63.7	54.5
00-01	924.3	968.9	44.6 4.8%	909.4	929.0	(19.6)** (2.2%)*	14.9	39.9	25.0
01-02	1,017.0	1,027.9	10.9 1.1%	1,007.6	982.3	25.3 2.5%	9.4	45.6	36.2
02-03	1,053.7	1,051.0	(2.7)** (0.3%)**	1,044.0	1,033.1	10.9 1.0%	9.7	17.9	8.2
03-04	1,056.8	1,059.5	2.7 0.3%	1,056.7	1,034.7	22.0 2.1%	0.1	24.8	24.7
TOTAL	10,376.5	10,568.1	191.6 1.8%	10,303.9	10,257.0	46.9 0.5%	72.6	311.1	238.5

NOTE: * Planned Expenditure: additional expenses on schools' building maintenance were approved by Executive Committee early in the financial year.

** Major Events: 1997-98 - Asian financial crisis; 2002-03 - SARS



Paragraphs 3.3 – 3.11: Ratio of current liabilities to current assets

Audit observes that ESF has a high ratio of current liabilities to current assets.

The ESF submits that its net current assets position should not be considered in isolation. The value of the Foundation's property portfolio is not reflected fully in the Balance Sheet. The net book value was only HK\$4.4M as at 31 August 2004. However, their market value was far higher – at the last valuation in 2001 the portfolio was valued at HK\$755m. This confers considerable financial stability, well in excess of all liabilities.

As noted in ESF's response to the Audit Report, the current liabilities are similar from year to year. Because major items such as staff gratuities are paid on a two-year cycle, the effect is to roll over the liabilities from year to year. There is a very low risk of large liabilities crystallising in any one year.

Paragraphs 3.12 – 3.16: Bank Overdraft

Audit has observed that ESF maintains high levels of bank overdrafts.

The ESF utilises its overdraft facility in the summer months. This is during the period when fee income is low and expenses are high (payment of staff gratuities, building development, renovations, etc., which need to be completed over the summer holidays). As soon as fee and government income flow into the ESF starting September, this overdraft is paid off. The level of overdraft varies from year to year depending on the level of development and renovation work undertaken during the year.

The duration of the overdraft is relatively short as can be seen in the table below.

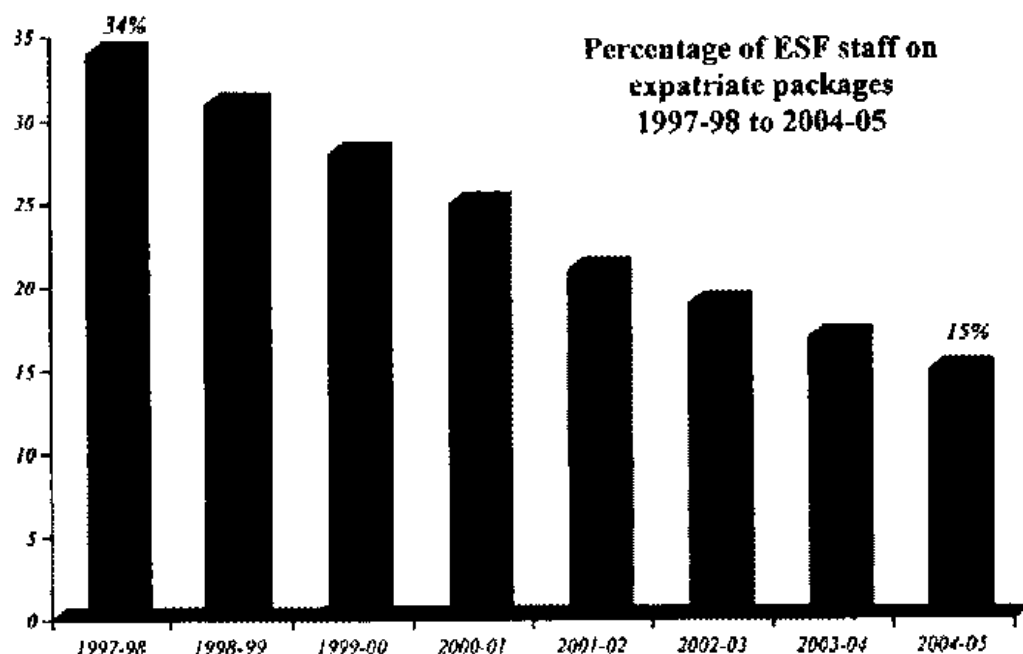
Year	No. of Days having overdraft	Average Overdrawn Balance HK\$	Amount of Overdrawn Interest paid HK\$
2004	56	49M	362,936
2003	59	48M	389,816
2002	6	8M	6,493
2001	-	-	-
2000	3	19M	14,633
1999	27	11M	67,280

Paragraphs 4.1 – 4.39: Staff recruitment and remuneration

The ESF has, since 1997, sought to introduce measures intended to align remuneration levels of ESF teachers with the prevailing circumstances in Hong Kong and elsewhere.



The chart below shows the declining percentage of ESF staff on expatriate contracts which include housing. By gradually phasing out these contracts since 1997 we estimate that the ESF is spending approximately HK\$ 18 million less on remuneration per annum (based on a snapshot comparison of 1997-98 and 2004-05.)



In addition the ESF has introduced a salary reduction of 4.42% this year, which will be completely implemented by 2005. The following table shows a detailed breakdown of average salary levels of ESF staff:

	Audit Commission (as of 1 Apr 04)	Old "Overseas" Contracts	New Contracts ALL	New Contracts without Resp. Allow.
Salary (HK\$)	56,047	61,124	52,440	47,865
Benefits (HK\$)*	22,903	38,657	18,943	18,063
Total / month (HK\$)	78,950	99,781	71,382	65,928
Total / year (HK\$)	947,400	1,197,374	856,586	791,140

* Benefits include gratuity, medical, dental and housing benefits



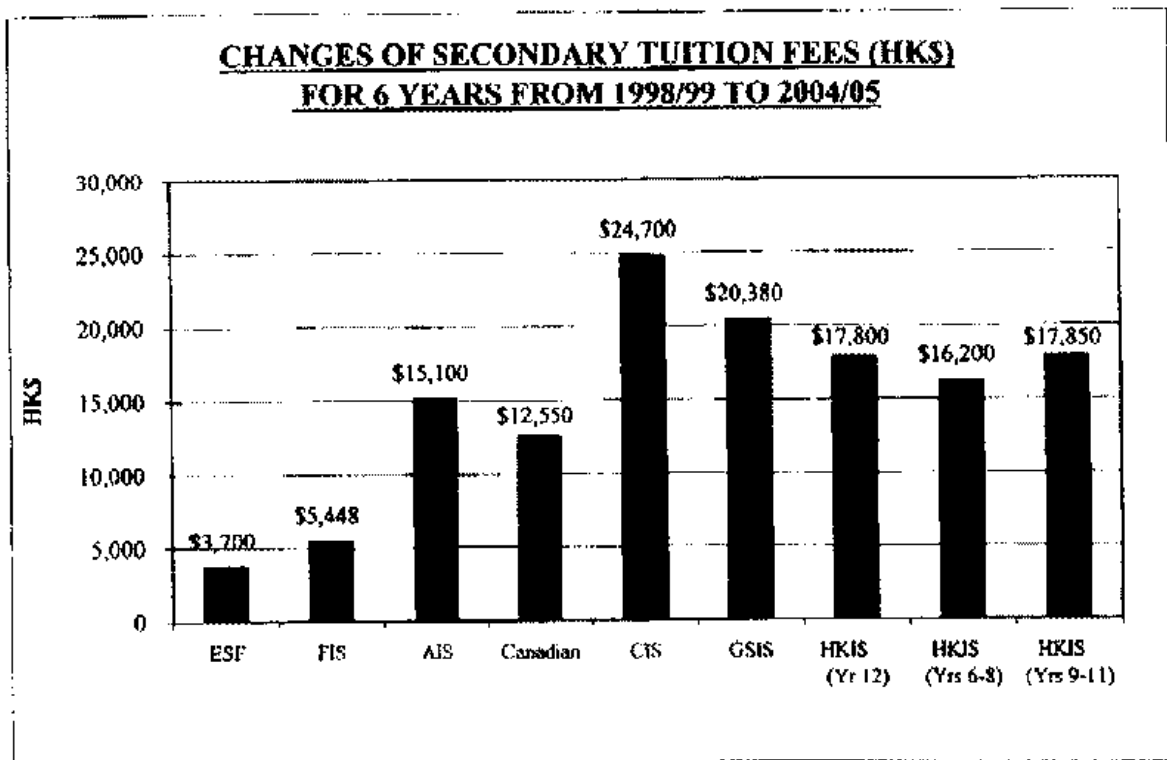
Chapter 3

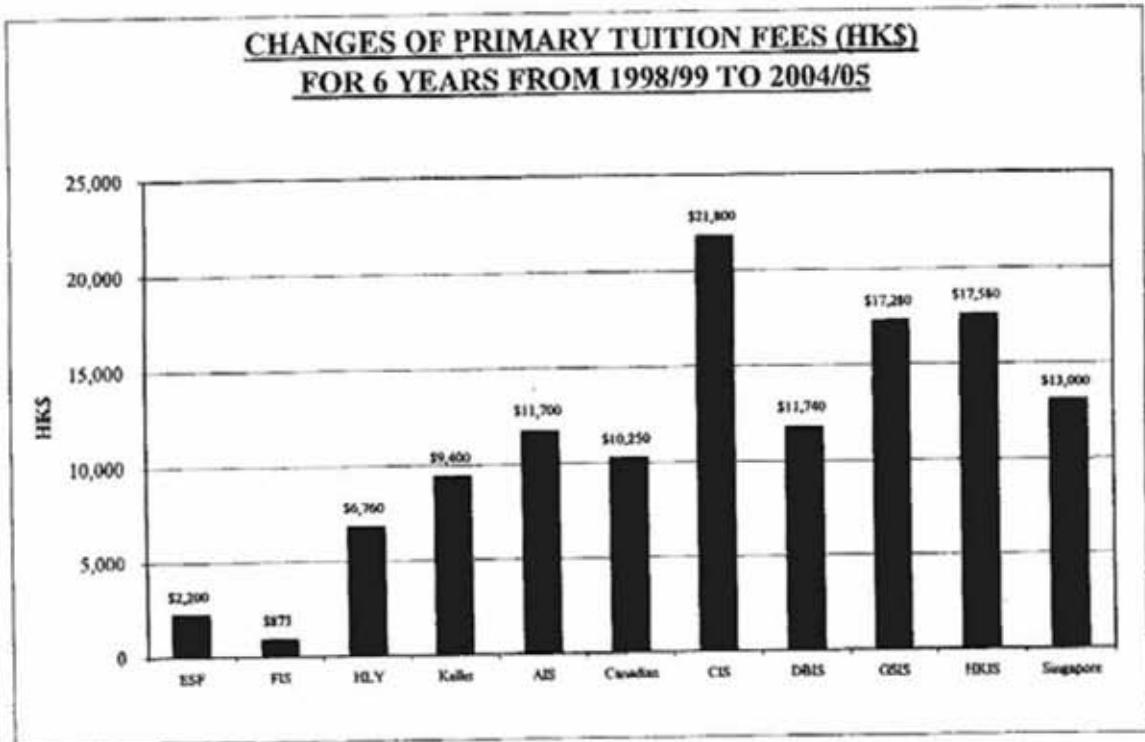
Paragraph 2.20 – 2.27: Fees

The Foundation instituted a formal fee policy in 1994. The Executive Committee has agreed to a revision of the current policy. Our commitment has been to keep the fees as affordable as possible. The attached charts show the Foundation's fee increases compared with other fee paying institutions over the last six years.

The increases are displayed below by \$ amount for both primary and secondary schools. The data analysed by percentages presents a very similar picture.

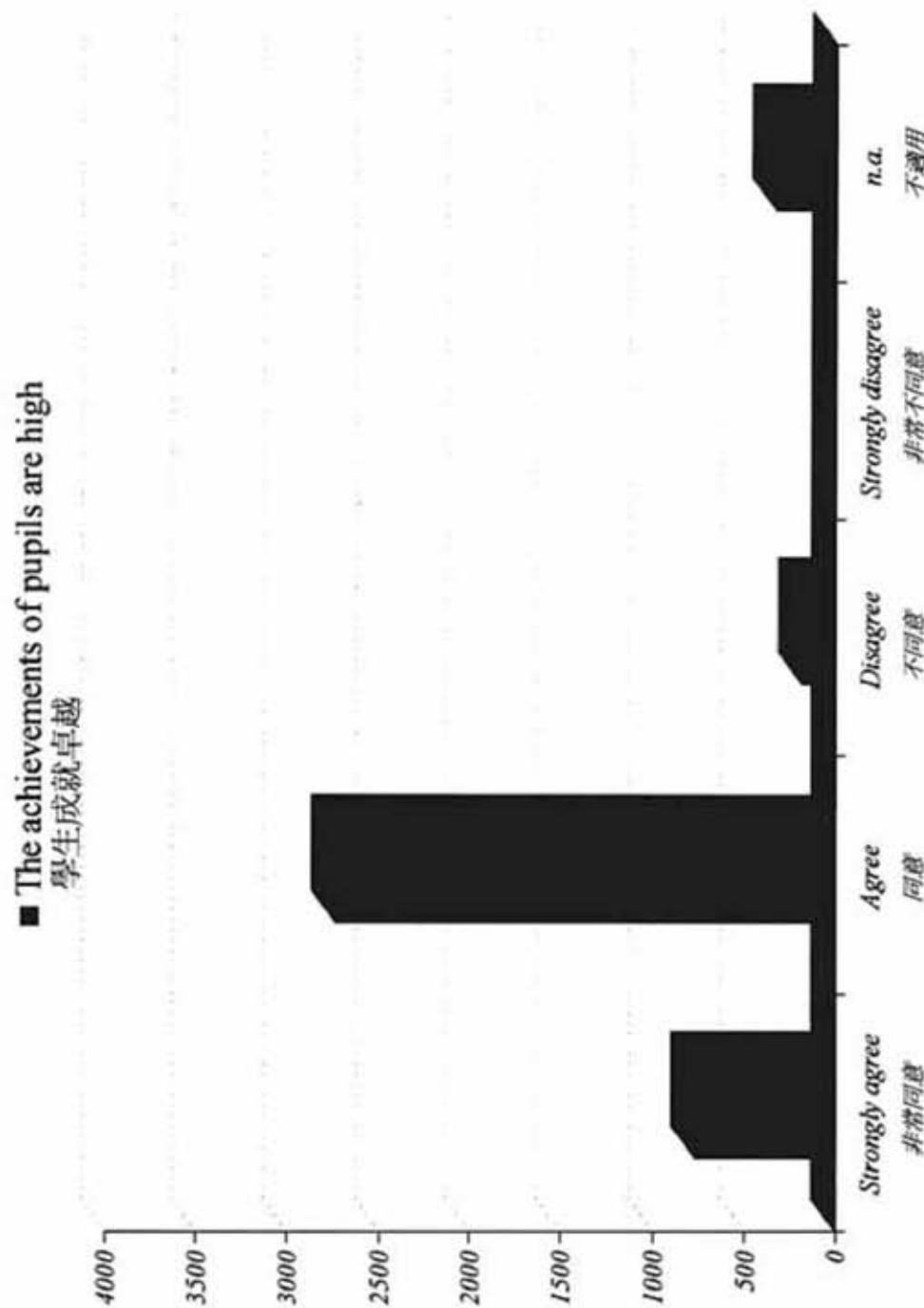
N.B. It should be noted that the relatively low fee increases displayed are during a period when the per capita subvention from Government was falling (see Chapter 3 paragraph 2.3. – page 7).





Based solely on tuition fees. All other factors such as debenture and capital levies have been excluded from this analysis.

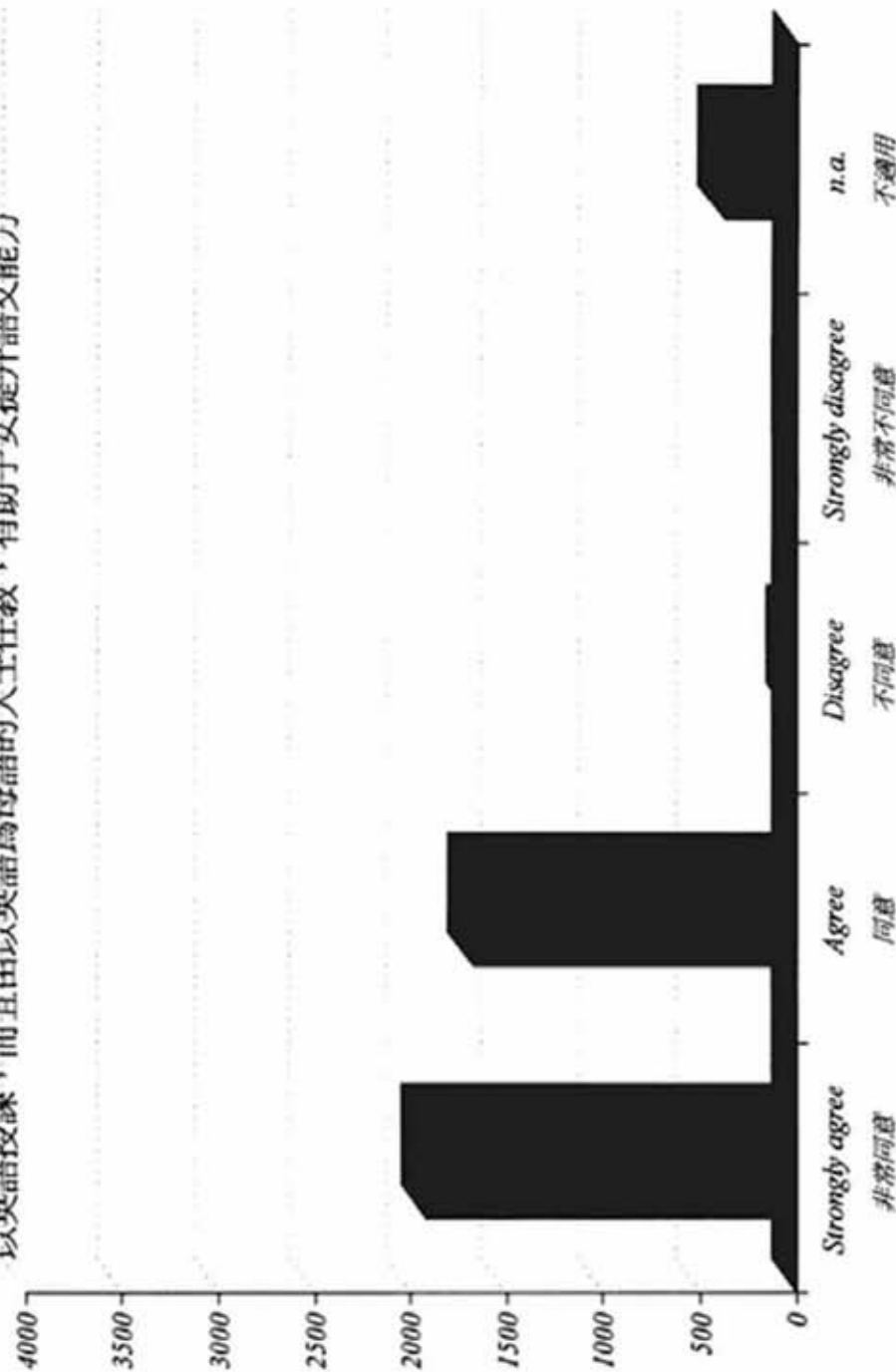
Chart 1: Why parents choose ESF 家長選擇英基的原因
Academic achievement 學術成就



Based on representative sample of 4046 data points - Study ongoing 根據 4046 份具代表性的資料數據計算 - 研究尚在進行中

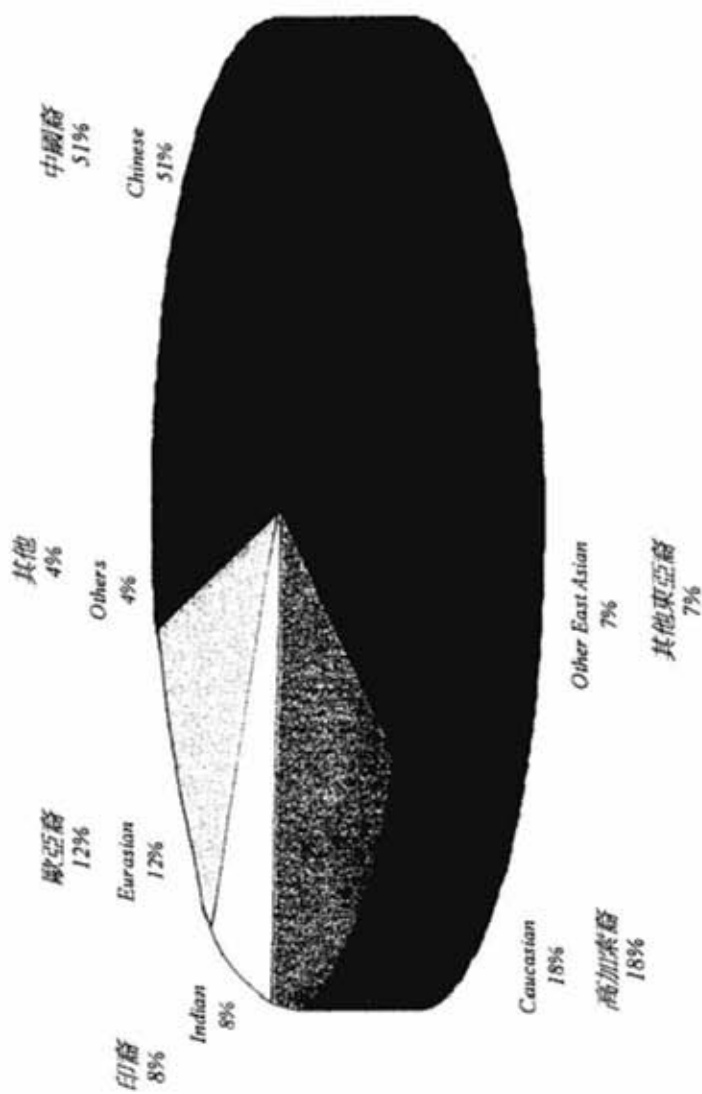
Chart 2: Why parents choose ESF 家長選擇英基的原因 Nature and quality of the experience 教學特點和質素

- English medium teaching by native speakers will help my child's language development
以英語授課，而且由以英語為母語的人士任教，有助子女提升語文能力



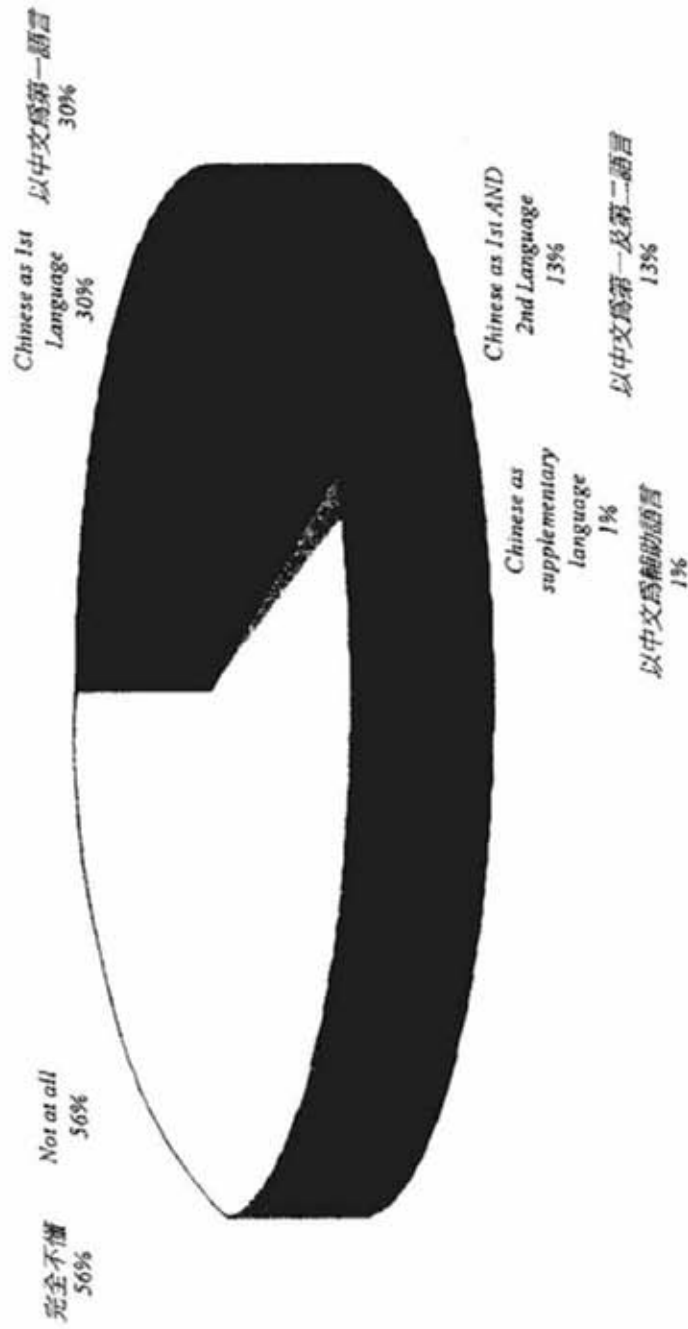
Based on representative sample of 4046 data points – Study ongoing 根據 4046 份具代表性的資料數據計算 – 研究尚在進行中

Chart 3a: Ethnicity data among ESF families Oct 2004
英基家庭的族裔數據 (2004年10月)



Based on representative sample of 4046 data points – Study ongoing

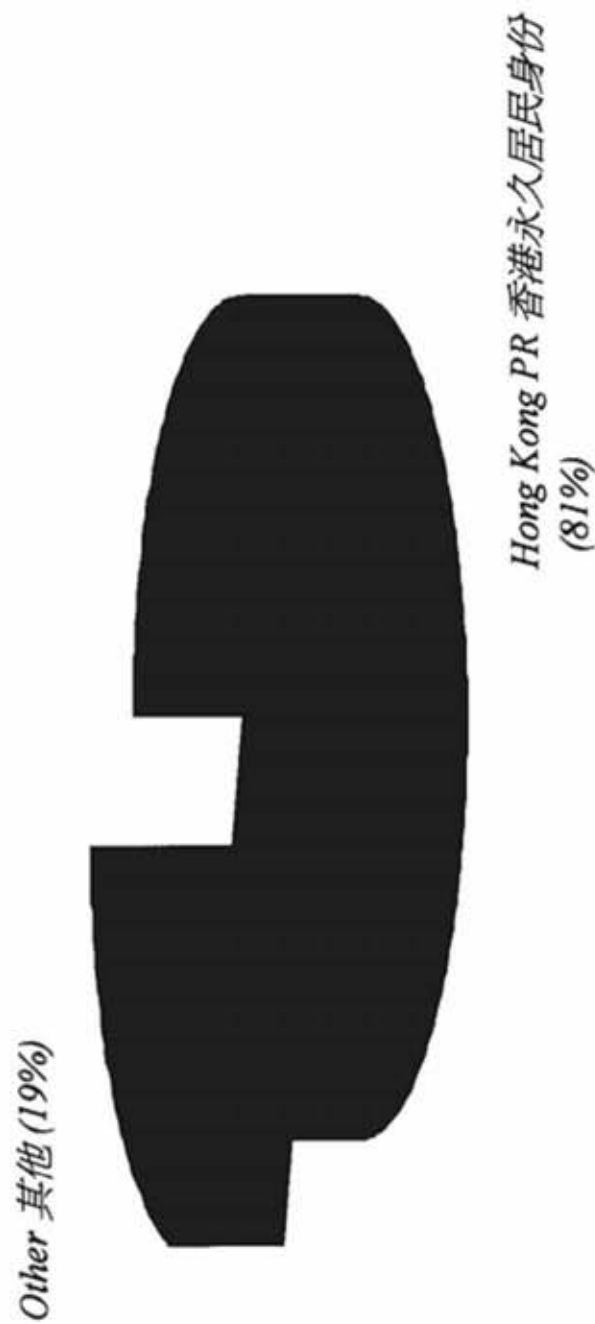
Chart 3b: Mother tongue data among ESF families Oct 2004
 英基家庭中以廣東話為母語之數據 (2004年10月)



Based on representative sample of 4046 data points – Study ongoing

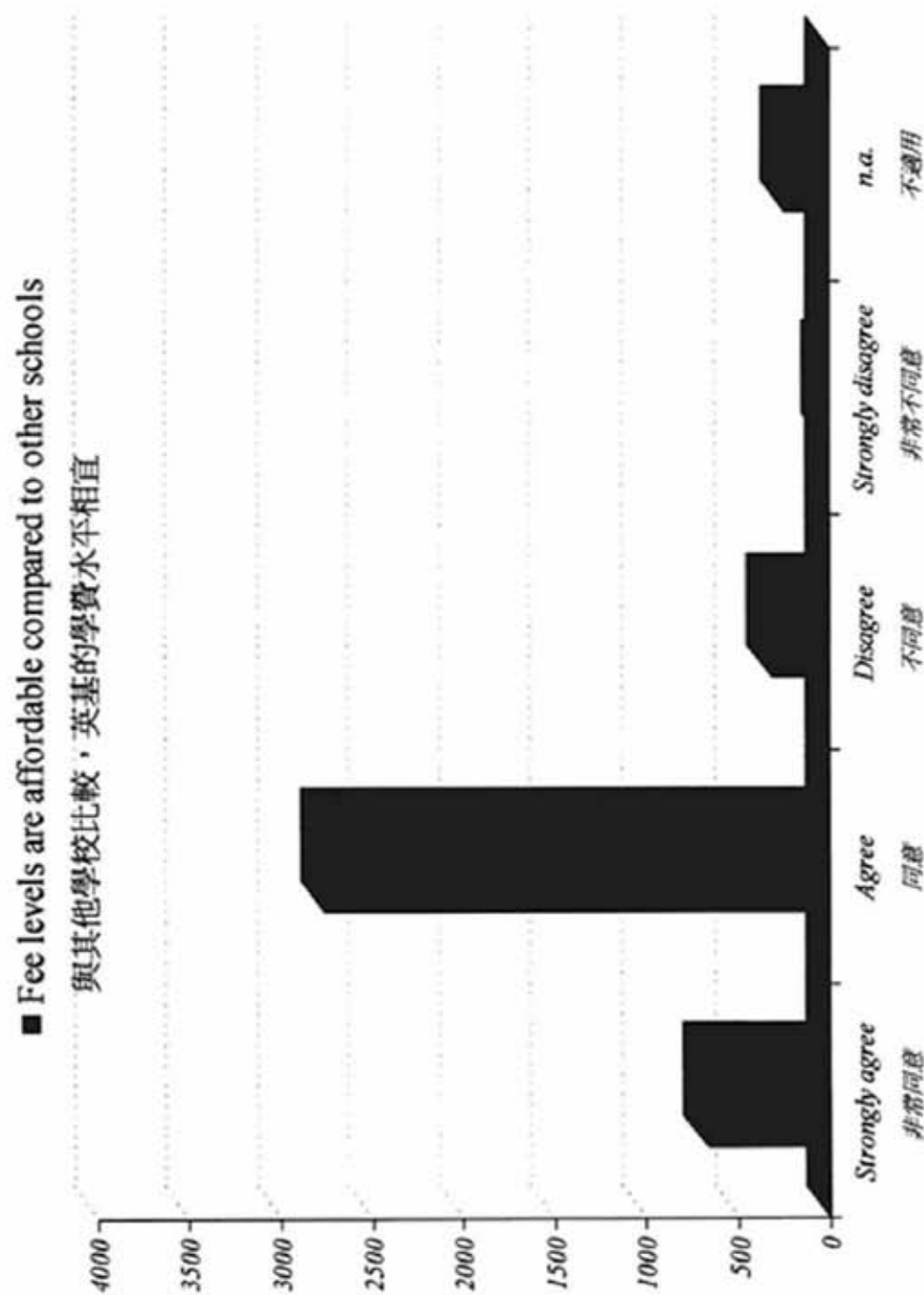
Chart 3c: % of ESF Students with either parent holding Hong Kong PR Status (Oct 2004)

雙親擁有香港永久居民身份的英基學生比例（2004年10月）



Based on representative sample of 4046 data points – Study ongoing 根據 4046 份具代表性的資料數據計算 – 研究尚在進行中

Chart 4: Why parents choose ESF 家長選擇英基的原因 Finance 財政因素

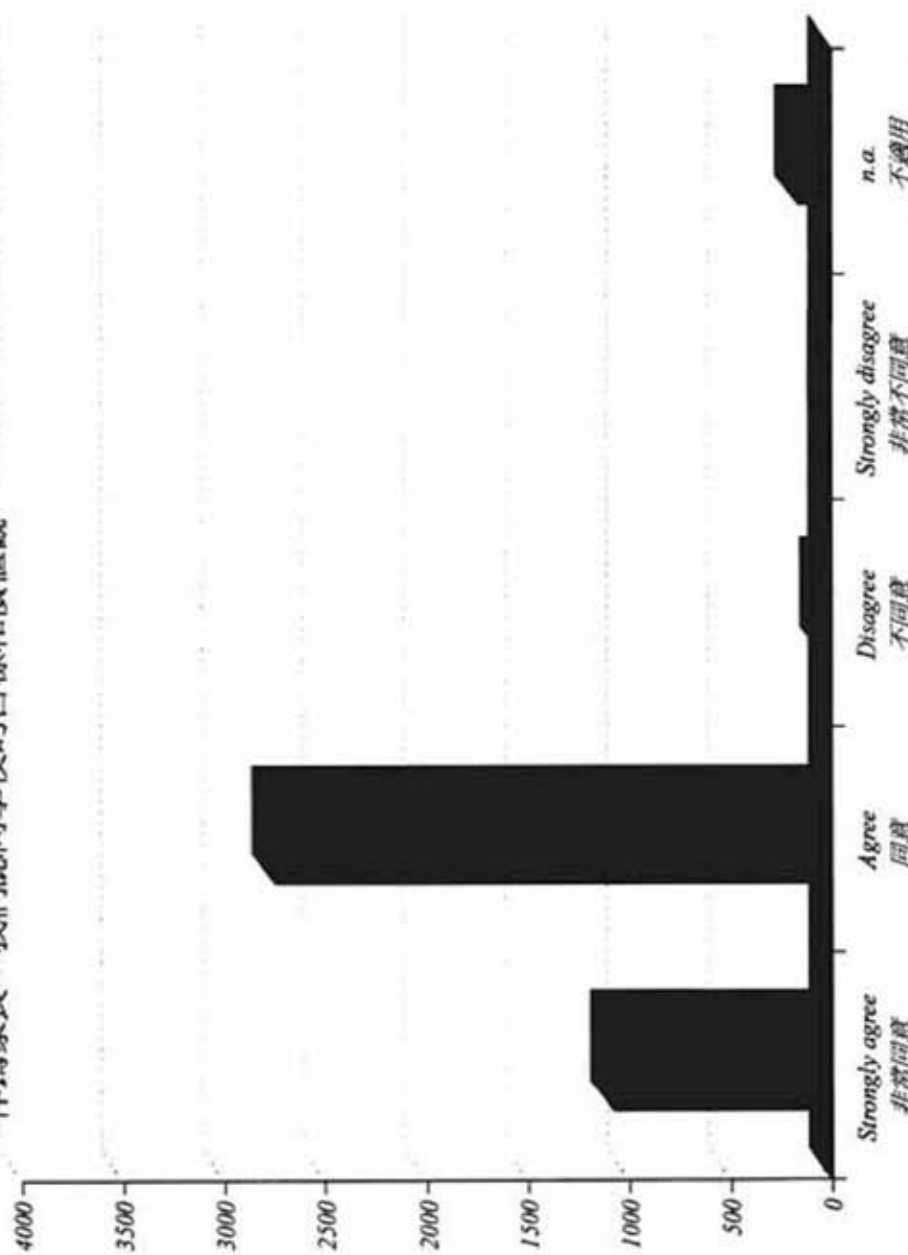


Based on representative sample of 4046 data points – Study ongoing 根據 4046 份具代表性的資料數據計算 – 研究尚在進行中

Chart 5: Why parents choose ESF 家長選擇英基的原因 Aims and values 目標和價值觀

■ The aims and values of the schools accord with our views as parents

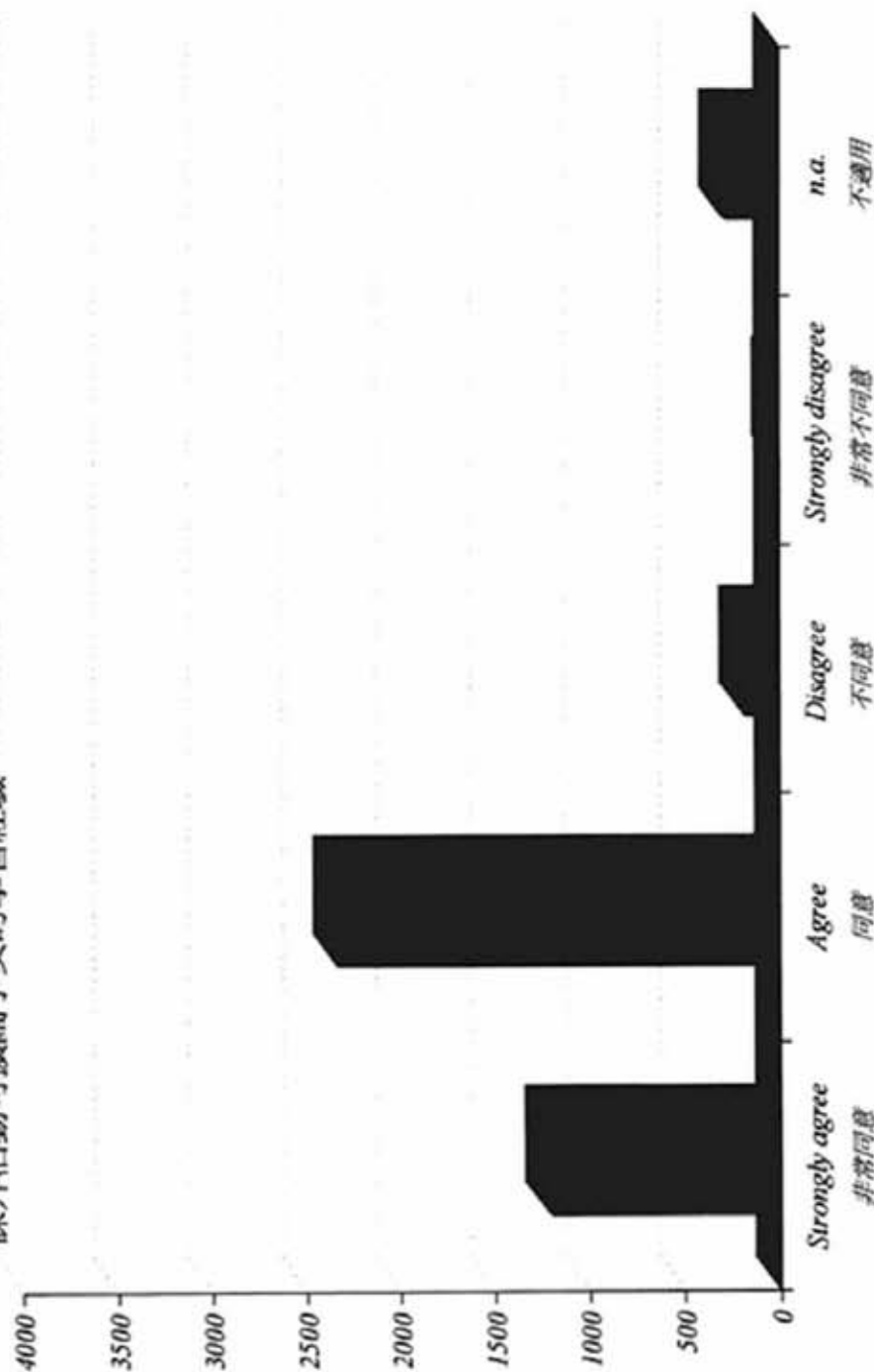
作為家長，我們認同學校的目標和價值觀



Based on representative sample of 4046 data points – Study ongoing 根據 4046 份具代表性的資料數據計算 – 研究尚在進行中

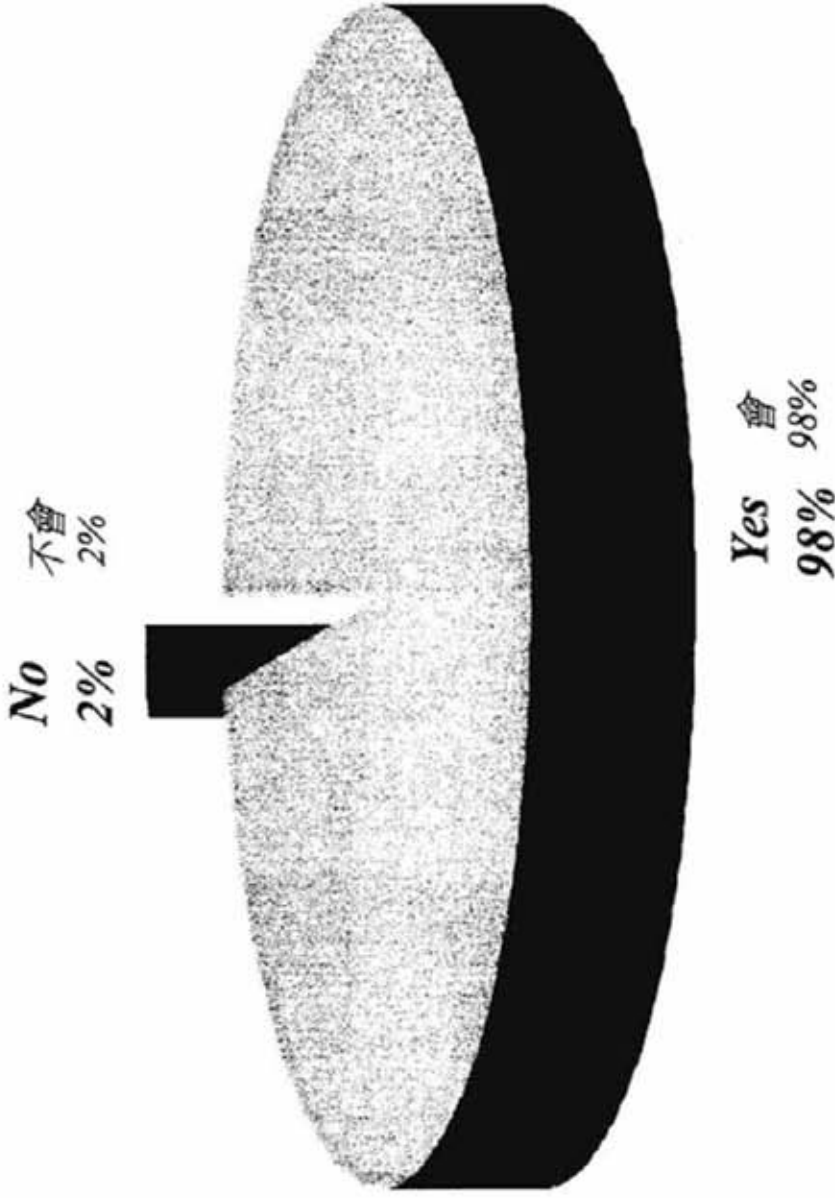
Chart 6: Why parents choose ESF 家長選擇英基的原因 Nature and quality of the experience 教學特點和質素

- The extra curricular activities give my child enriching experiences
課外活動可擴闊子女的學習經驗



Based on representative sample of 4046 data points – Study ongoing 根據 4046 份具代表性的資料數據計算 – 研究尚在進行中

Chart 7: Proportion of parents who would recommend ESF to another parent
樂於向其他家長推薦英基學校的家長人數比例



Based on representative sample of 3712 data points. Out of the 4046 entries received 334 respondents did not answer this question. – Study ongoing

**Hearings of the Public Accounts Committee
Value-for-Money Audit on the English Schools Foundation**

**Chapter Four: Corporate Governance and
Headquarters Administration of the ESF**

Speaking Notes for the SEM

Thank you Chairman.

2. This Chapter of the Audit Report covers corporate governance and Headquarters administration. Both are core issues pertaining to the sustained well-being of the English Schools Foundation ("ESF") as a strong education institution. We generally agree with the Audit observations and recommendations. We hope to see early implementation of necessary improvement measures within the ESF to bring about a more transparent and accountable organization, which operates on sound cost-effectiveness performance.

Governance Reform within the ESF

3. Yesterday, the ESF held its annual Foundation meeting. Among other businesses, there has been an extensive discussion on a set of draft guidelines prepared by the ESF Chairman for the restructuring of the ESF governance and management. This attempt strongly demonstrates the Chairman's commitment in sustaining the ESF as a quality education centre, which we deeply appreciate.

4. We see the ESF Foundation's endorsement of the guidelines a good first step towards the right direction of modernizing the governance structure of the ESF. We note that the principles and approach are sensible ones but as always, devil is in the detail, which would be worked out by a task force. At this point of time, this task force has yet to come into being. A clear way forward is pending. Whether the intended results of the guidelines could be delivered would hinge on the shape of the finalized product to be available next year. We sincerely hope that the entire ESF community could render its continuous support to the upcoming task force and the ESF Executive Committee in order to bring this important task to fruition in a timely manner. Without prejudice to Government's overall policy of not micro-managing any subvented body, we would be happy to contribute our knowledge and experience in school administration should the ESF considers our advice useful and relevant to

the review work in the next step.

5. Back to the Audit Report, we believe that the final outcome of the governance reform could address these problems identified during the audit exercise or at our fact-finding work –

- (a) The existing mammoth-sized governance body is less than effective and must be slimmed up. The proposed size of 25 as contained in the Chairman’s guidelines seems consistent with the Audit observations.
- (b) Composition of the ESF governance body should reflect a proper balance of views from various sectors.
- (c) Proper procedures should be put in place to avoid any possible conflicts of interest which might undermine the quality of management. Essentially, stringent declarations of interest requirements should apply as they do within Government and in the private sector.
- (d) Actions should be done to ensure that as a fundamental practice, decision making in a fully informed and evidence-based approach should be practiced at all level of management within the ESF. Proper records should be maintained on the decisions made and on the considerations underpinning such decisions.

As stated in the Audit Report, we would also review our long term role on the ESF Foundation and the ESF ExCom, giving regard to our usual practice of not involving in the management of individual schools or their school sponsors.

Cost Effectiveness of the ESF

6. Meanwhile, pending outcome of the ESF governance reform, we would continue to expect the ESF to enhance its cost-effectiveness to safeguard prudent use of public funds and parents’ tuition fees. This is important in that further to the “oyster lunch”, which brought uneasiness to many ESF stakeholders when it was known to the public earlier this year, the Audit Report reveals departure from market practices in various aspects of the ESF operation.

7. We are glad that the ESF has so far been positive in its response

to the Audit findings. While we should offer a reasonable period of time for it to adjust, the ESF must take prompt action and seize every opportunity to seek remedial measures early. Members of the public would be interested in hearing from the ESF justifications in support of its policies touched upon in the Audit Report. For example –

- (a) **Remuneration:** Why is it necessary to offer a remuneration package much more favourable than that offered by other local international schools whose standard of operation is comparable to that of ESF? How is it value-for-money? What is unique about the ESF? And in what ways are ESF teachers distinctive from their local counterparts that deserve a much enhanced package?
- (b) **Housing Benefits:** ESF staff are privileged to have quarters built in prime sites. Why is it necessary for the ESF to offer rental allowance up to 50% of monthly salary (as high as 90% back in early 1990s)? On what basis did the ESF draw up such a rate? Has the rate been the outcome of vigorous market research? Were the rates adopted only after a decision by ExCom in an informed manner with justification and financial implications to the ESF thoroughly set out in a paper to ExCom?
- (c) **Overdraft:** Cashflow of schools with a long history should be quite stable and predictable. What special circumstances that keep recurring every year that have barred ESF from better managing its income and expenditure pattern to smoothen its cash flow? While the ESF has been able to run on surplus towards year end, where does the money go when ESF parents pay their fees during the year?
- (d) **Golden Handshake:** In what circumstances would the ESF offer payments to departing staff to an extent more than that stated in the employment contract? Any rule on how to assess the amount of enhancement? Who could make such decisions? Were these decisions properly documented? Why was the ExCom not consulted and not even informed in some of the cases?

8. With the above general remarks, we welcome Members' questions on Government's views in relation to Chapter Four of the Audit Report.

**Hearings of the Public Accounts Committee
Value-for-Money Audit on the English Schools Foundation**

**Chapter Four: Corporate Governance and
Headquarters Administration of the ESF**

(Continued Session)

Speaking Notes for the SEM

Chairman,

Thank you for allowing me to speak again before this Committee resumes its hearings on Chapter Four of the Audit Report.

2. During the hearings on 10 December, some Members blamed the Administration for not monitoring the English Schools Foundation (“ESF”). Such criticisms are unfounded and I feel obliged to make a response to put things in perspective, for the purpose of a fair and informed discussion.

The ESF’s Obligation and the Administration’s Role

3. The ESF is established by law and enjoys the powers and privileges bestowed by the English Schools Foundation Ordinance (Cap 1117). The ESF Foundation is the supreme governing body within the ESF establishment. Its membership comprises representatives from a wide cross-section of the community, including government officials, whose role was intended to be advisory, to allow the ESF the benefit of the views of different community sectors. Had it been envisaged that the Government should play a watchdog role, the Ordinance would not have been introduced by a private Member, and the Government would have been given the necessary statutory powers to direct and monitor the operation of the ESF.

4. For historical reasons, EMB has one representative on the ESF Executive Committee. This is a unique arrangement, not repeated in other school sponsoring bodies receiving government subvention. The purpose is for liaison and advice. Indeed, it is an established and widely-accepted policy that the Administration should refrain from micro-management.

5. This notwithstanding, since late 2002 when we suspected significant cost effectiveness problems within the ESF, we have stepped up

our attention to ESF operation, both inside and outside the ESF Executive Committee. One example is the fact-finding exercise which we initiated in early 2003. Members should all have been provided with the draft report of this exercise and I shall not explain the depth and breadth of our work. We could proudly say that we have done our part diligently. Understandably, without the same legal right to access ESF archives, we are unable to unearth the mismanagement to the same extent as the Director of Audit. But gratifying to note is that most if not all observations we made have been generally shared by the findings of the Director of Audit.

The Responsibilities of the ESF Executives

6. Years of impartial and conscientious examinations of public accounts have earned the Public Accounts Committee much community respect. For this respect to continue, a fair evaluation of the ESF Executives' role in ensuring ESF's cost effectiveness must not be missed. To be fair to my colleagues, and more importantly, to be fair to all ExCom and Foundation members, I must elaborate on what should have been the reasonable expectations of the ESF Executives and part-time ExCom and Foundation members serving on an honorary basis.

ESF Headquarters Administration

7. I am quoting one of the most glaring mismanagement examples in this Audit Report, i.e. the three golden handshake packages recently offered by the ESF to its senior staff. We have carefully reviewed the minutes of the meetings when the ExCom was apprised of the departure of the three senior staff. We confirm that *only in one case*, that of Staff A, was the ExCom consulted on the extra payment made. At that time, the ExCom was told that the resignation was accepted "in accordance with the Conditions of Service" and I stress, "in accordance with the Conditions of Service". In other words, the ExCom was not informed that it should indeed be the resigned officer who should have paid the compensation to the ESF for the short notice given for his departure. In respect of Staff B and C, the ExCom was only informed of their resignation. No mention of payment was ever made. For Staff C, whose resignation took immediate effect, we did ask the ESF for details but in vain. We became aware of the golden handshake for him through an anonymous letter issued to the press several months afterwards. In respect of the payment to Staff B, if not for the report of the Director of Audit, I am afraid that EMB, and I presume other ExCom members, would still be kept in the dark. And frankly, we do not know whether similar cases exist.

8. To put it mildly, I was surprised at the last PAC hearing that some

Members attributed the ESF's wastefulness to be the responsibility of EMB. Members seemed to have mis-interpreted the problem and picked the wrong target of attack. We have been participating in the ESF ExCom on the basis of trust and cooperation. For an organization which has repeatedly emphasized the outstanding calibre of its staff, and with a successful business person in the chair, would Members consider it reasonable that we should, at each and every one of the monthly ExCom meetings, *take the initiative* to ask if for the last month, there had been any golden handshake proposals, any inappropriate payments of entertainment, medical and dental allowances or any claim for taxi fare that was not supported by receipts? How could the ESF ExCom function if it were pre-occupied with this kind of micro operational matters? And, more fundamentally, should the onus not be on the ESF Executives to bring up for the ExCom's approval cases which merit exceptional treatment not in line with established policies and financial management rules? Do they not have the duty to furnish all necessary background information to enable the ExCom to make an informed decision?

ESF School Administration

9. The same applies to school administration. At the last PAC hearing, some Members criticised EMB for not doing anything about the school whose council had not met for almost two years. Let me state the facts. Just as in the case of aided schools, EMB is *not* represented on any ESF school councils. How would EMB know if the problem was not even reported to the ExCom? But in accordance with the ESF Regulations, the Chief Executive of the ESF or his representative sits on *every* school council. Should we rather ask what has the ESF Headquarters done? What should be the role of the ESF management in the first place? Why has it kept the ExCom in the dark? We simply could not see any case for blaming the Administration.

10. If Members indeed consider it reasonable that EMB should micro-manage given the recurrent subsidies we pay to the ESF, then I must caution that the same, if not more stringent, level of control must apply to all aided schools, which are almost completely funded by the Government, as well as subvented organizations in general. This clearly goes against the existing policy of school-based management and represents a move from outcome monitoring to input control and micro-management of subvented organizations.

11. In EMB, there are only six officers, from Assistant Education Officer to Permanent Secretary, with varying degrees of involvement with the ESF, amongst their many other responsibilities, whereas the ESF

Headquarters has a staffing establishment of over 50 persons working full time. Here, I have not included the administrative staff working in ESF schools, again working full time.

Value-for-Money Measurement by Quality

12. Last but not least, ESF has deployed the quality argument, namely its academic achievements, to defend its costs. I must say, golden handshake, unsatisfactory school administration, inappropriate entertainment allowances are not necessary bedfellows of quality education. In other words, wastefulness does *not* necessarily come with quality education. To put the quality question in proper perspective, we should compare like with like. If Members are so interested, I would suggest that Members enquire about the public examination results and the teacher qualifications of the other local international schools to see if they fare significantly worse than the ESF.

13. We appreciate that ESF schools have taken on students having special education needs. Therefore, the provision for Sarah Roe School, the special school operated by ESF, has been consciously insulated from the review on subvention arrangement. For Members' information, local public sector schools are also shouldering their fair share in providing education to children with Special Education Needs. These children form an average of 14% of the student body within the aided sector.

14. Chairman, I must reiterate that we are not seeking to belittle ESF's contribution to Hong Kong's education. Overall, its students are doing fine, its schools are doing fine, and its teachers are doing fine. However, its management, and if I may say so, its senior executive management and its governance, are lagging behind public expectation of a modern organisation. We should focus on value for money and governance. There must be proper checks and balances in the ESF to ensure cost-effective use of resources, transparency of operation and accountability of outcome.

15. Before this Committee, Chairman, is a 37-year old historical legacy. ESF's governance and management problems did not start yesterday. I urge Members to tackle the root of the problem and place responsibility where it should lie. Only by doing so could this Committee uphold its credibility and maintain its objectivity. All along, the Government has had high regard for this Committee and would continue to play our modest part to contribute to an impartial hearing.

16. Thank you, Chairman.

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14/F, Wu Chung House
213 Queen's Road East
Wanchai, Hong Kong

08 January 2005

Clerk to the Committee
Public Accounts Committee
Legislative Council Secretariat
The Legislative Council
8 Jackson Road
Hong Kong

(Attn: Ms Dora Wai)

Dear Ms Wai

Public Accounts Committee
The Director of Audit's Report No. 43

Please refer to the response of the English Schools Foundation ("ESF") dated 4 January 2005, relating to participation of Government officers in the business of the ESF. We intend to submit the enclosed information note for reference of the Public Accounts Committee. The Chinese version would be forwarded to you at a later stage.

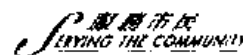
Yours sincerely,



(LAI Yiu-kei, Samson)
for Secretary for Education and Manpower

教育統籌局與教育署已於二零零三年一月一日合併為新的教育統籌局。為免浪費，我們繼續使用舊文具存貨。

We are the new Education and Manpower Bureau formed by the merger of the old Bureau and the Education Department. To minimize waste, we are using our old stationery while stock lasts.

 **服務市民**
SERVING THE COMMUNITY

Information Note for the Public Accounts Committee

Participation of Government Officers in the Business of the English Schools Foundation

INTRODUCTION

Upon instruction of the Public Accounts Committee, the Clerk to the Committee invited the English Schools Foundation ("ESF"), vide her letter of 22 December 2004, to provide information relating to the participation of Government officers in the business of the ESF. Such information includes the name of the Government representatives on the ESF Foundation and Executive Committee ("ExCom"), their attendance and their views or suggestions on the corporate governance and Headquarters administration of the ESF, etc.

2. To enable that the matter could be considered in a more informed manner, this information note seeks to set out other information not covered in the ESF's response of 4 January 2005.

GOVERNMENT REPRESENTATIVES ON THE ESF

The ESF Foundation

3. Under the English Schools Foundation Regulations, which are subsidiary legislation made by the ESF without the need of negative vetting or gazettal, the Chief Secretary for the Administration ("CS") and the Permanent Secretary for Education and Manpower ("PSEM") are members of the ESF Foundation. PSEM might also nominate up to two representatives as advisers to the ESF Foundation.

4. The CS had not attended any of the ESF Foundation meetings in the past. Government's role on ESF Foundation has all along been carried out by the Director of Education (now the Permanent Secretary for Education and Manpower) or her representative.

5. As stated in the Audit Report and in SEM's opening address at the PAC hearing on Chapter Four of the Audit Report, we would review our long term role on the ESF Foundation and the ESF ExCom, giving regard to our usual practice of not involving in the management of individual schools or their school sponsors. This would include the

position which is held by the CS in the ESF Foundation.

6. It is relevant to note that except for the two recent Foundation meetings, the remaining ones in the past five years were convened to consider reports of individual ESF principals, report of the ESF Secretary, annual accounts of the ESF and appointment of auditors. Indeed, from the angle of its day-to-day operation, our representation would make a bigger contribution to the ESF by offering advice to the ExCom than by receiving routine reports at the Foundation. The ExCom meets once a month while the Foundation, once a year only. When important issues were considered, we would step up our representation. For instance, when the Foundation elected its Chairman upon the resignation of the former Chairman, PSEM and her two designated advisers (also EMB officers) all attended the meeting. When the governance reform was raised for discussion at the most recent Foundation meeting held in December 2004, which has not been included in the ESF's response, both the subject Deputy Secretary and Principal Assistant Secretary attended.

The ESF ExCom

7. As regards the ESF ExCom, the membership includes PSEM, and she might appoint a representative to represent her at the meetings. It has been the long held practice that the representative is the Principal Assistance Secretary for Education and Manpower (or Assistant Director of Education before the merger) responsible for the ESF policy. Unless the circumstances require otherwise, this representative would attend meetings of the ESF ExCom on behalf of PSEM.

8. The information provided by the ESF shows that our representative has participated in most ESF ExCom meetings during the past five school years. Our involvement in the discussion of ESF matters should be consistent with Government's overall position vis-à-vis the ESF, i.e. to strike a sensible balance between oversight and avoidance of micro-management.

ACTIONS TAKEN BY THE ADMINISTRATION

9. For historical reasons, EMB has one representative on the ESF Executive Committee. This is a unique arrangement. The Administration does not sit on the management committee of any other aided schools or the executive committee of their sponsors. This suggests that our ExCom membership was intended to serve a liaison /

advisory function, ensuring that the interests of (British) civil servants whose children attended the ESF schools were well served and policy decisions were adequately communicated. From the way the English Schools Foundation Ordinance was couched, it was never intended that Government should micro-manage or monitor the ESF.

10. That said, we have expressed interest in some matters being study at Chapter 3 of the Audit Report. An example is the pay review process. Separately, we have kept informal exchanges with the ESF management on a wide spectrum of issues through channels outside the Foundation or ExCom context. Most of these meetings were informal and frank and were attended by the former ESF Chairman, but not the ESF Executives. For example, at a meeting with the then ESF Chairman on 11 July 2003, we asked about the details behind the sudden resignation of Staff C.

11. Other than meetings, we also maintain an exchange channel through electronic mail or formal letters of correspondence. The Government representative on the ESF ExCom has from time to time raised questions on issues to be discussed at future ExCom meetings, complaints or other areas of doubt in the operation of the ESF. For example, we have expressed interest in the background of the ESF Educational Services Ltd, which is a subsidiary of the ESF.

12. Separately, we have initiated the fact-finding exercise in early 2003, which is to examine the cost structure of the ESF operation. The Director of Audit, in his access to EMB records, has also drawn reference from the findings of this exercise. Indeed, as far as EMB is concerned, the conduct of this fact-finding exercise has provided valuable information on the probable reasons for the inertia within the ESF against changes. The problems we have encountered in the review process have been briefly set out in paragraph 3.16 of Chapter 3 of the Audit Report.

**Education and Manpower Bureau
January 2005**

**Reply of 7 January 2005 from
Mr Jal Shroff, former Chairman of the English Schools Foundation**

I refer to your letter CB(3)/PAC/R43 dated 6th January 2005 requesting me as the former Chairman of the English Schools Foundation (ESF) to comment on the Audit Commission's observations and recommendations on various aspects raised in the Audit Report in particular the part on "corporate governance" and also if during my tenure as Chairman of the ESF whether the Government representative on the Foundation had put forward any views or suggestions on various aspects covered in the Audit Report in particular issues relating to corporate governance.

My schooling was at KGV (today an ESF School) and I have been involved with the ESF since 1983 as a member of Parent Teacher Associations, School Councils, Management Committee, and for about nine years as the Chairman of the ESF.

I have just this morning (7th January 2005) received a copy of the report and would have appreciated if I had been given more time to digest and respond in detail to it, nevertheless I shall try my best to reply. I will restrict my response to the issue of Corporate Governance (Chapter 2) and your question concerning involvement of the Government representative on the Foundation who incidentally is a representative of the Director of Education (now representative of the EMB) and is one of the nine members of the Executive Committee of the Foundation.

Regulation 5 of the Regulations of the English Schools Foundation (1985 Revision) defines the Executive Committee of the Foundation as follows:

- 5.1 The Executive Committee shall administer all the affairs of the Foundation other than those vested by the Ordinance in some other authority of the Foundation or retained as a power of the Foundation itself.
- 5.2 The Executive Committee shall ensure that the provisions of the Education Ordinance & Regulations and of the Ordinance and these regulations are complied with.

Let me now comment on Part 2 CORPORATE GOVERNANCE.

- 2.8 I agree that the large membership size of the Foundation is not conducive to efficient decision making - having said that over the last many years the Foundation has seldom made any decisions of importance; the important decision making has been left in the hands of the nine members of the Executive Committee.

- 2.9 I agree that ESF needs to totally review its Regulations to ensure that they reflect the changes NOT so much in the development of the community (as stated in the Audit Report) but with regard to the multi cultural intake of its students and the latest Educational Developments, to ensure that ESF is in line with the best practices.
- 2.10 I do NOT believe it is necessary to establish an advisory body similar to those established by the UGC-funded institutions. The ESF presently has FOUR Standing Committees to advise the Executive Committee on (a) Management of Schools (b) Academic & Administrative matters (c) Professional & Educational matters (d) Views of Parents & Pupils within the schools.

I suggest that there is an acute need to establish an active Audit Committee (with representative from the EMB/Financial Services and the Treasury Bureau) whose job is to monitor and to advise the Executive Committee on all financial matters. The ESF has enough educationalist but is lacking in having someone in the head office with local commercial know-how. In my humble opinion the ESF is in the business of EDUCATION (turnover over a Billion HK\$)

- 2.13(b) Interesting idea but needs to be carefully thought through and at this point of time I am NOT prepared to comment.
- 2.15 The reality of the situation is that at most times external members once
2.16 & appointed do not have the time or frankly are NOT interested in
2.17 attending the meetings - with the best intentions I doubt if this situation can change unless we have a ratio of at least three outsiders to one insider.

In my humble opinion the FMB should play a much more active role to exercise their influence on decisions made at the Executive Committee meetings dealing with all financial matters. To the best of my knowledge the minutes of both the Executive Committee and the Foundation meetings will reflect that NO Government representative has over the last ten or more years brought up the question of Corporate Governance.

As Chairman I have had private discussions with Mrs Fanny Law on a number of occasions on the composition of the Foundation and the need at an appropriate time to make changes.

Incidentally every single draft budget prepared by the ESF over the last forty odd years has had to be approved by the Education Department (now EMB) before it is implemented. The budget reflects salaries, school fees and projected surpluses and or deficits.

Finally I do not entirely agree with 3.3 - any business leverages its Fixed Assets and I am surprised that the Audit does not reflect the value of ESF owned property - which I believe is substantial. If the ESF's finances are in such a bad state (as reflected in the Audit Report) surely it was irresponsible for the EMB to allocate ESF two additional sites to build two large private independent schools part of which will be financed by our parents?

In conclusion please keep in mind that since 1967 the fee paying parents of the ESF have paid their share in expanding from two schools to fifteen Schools; not to mention the numerous new buildings added to Schools - actually the Government has benefited considerably over the years both financially and from the quality of students that the ESF has turned out and it is a shame that they are now suggesting cutting the subsidy paid to the ESF.

Jal Shroff
7 January 2005



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4 January 2005

Ms. Dora Wai
Public Accounts Committee
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms. Wai,

**The Director of Audit's Report on the
Results of value for money audits (Report No. 43)**

**Chapter 4: Corporate governance and
Headquarters administration of the English Schools Foundation (ESF)**

Thank you for your letter of 22 December 2004. The responses to the various requests for information are set out in the appendices to this letter as follows.

- Appendix 1 Questions raised by Secretary for Education and Manpower
- Appendix 2 Attendance of government representatives at the Foundation meetings (your sub-paragraphs (a) and (b)).
- Appendix 3 Attendance of EMB representative of Executive Committee meetings (your sub-paragraphs (c) and (d)).

I trust that this response meets your requirements. The Chinese translation will follow shortly.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive

Encl.

- c.c. Secretary for Education and Manpower
Chairman, English Schools Foundation
Secretary for Financial Services and the Treasury
(Attn: Mr. Manfred Wong)
Director of Audit

Appendix 1

(a) Remuneration

The following answers to the questions should be read in conjunction with the ESF response summarised at paragraph 4.25 of Chapter 4 and also page 10 of the ESF submission to the Public Accounts Committee meeting of 10 December 2004. The latter shows that the percentage of staff on the old terms of service has reduced substantially in recent years due to previous management action and that the new contracts cost about 10% less than the average figure cited by the Audit Commission.

ESF did not and does not set out to offer remuneration packages above those offered by local international schools. ESF salaries were historically set by links to the Civil Service Master Pay Scale. Since 2002, remuneration levels are based on the need to recruit and retain teachers of the highest quality, following a decision in 2000 to end the overseas package. We cannot comment on the recruitment and retention capabilities of other schools in Hong Kong. Nor do we have data on the requirements of international schools such as job descriptions and person specifications; it cannot just be assumed that these are the same or similar to ESF's. We believe that our present remuneration level allows us to recruit new staff but it remains to be seen, given our recent increased staff turnover rates, whether we can retain the staff recruited since 2000.

There are no value for money indicators in the Audit Report. It is purely a cost study. There are no productivity indicators eg class sizes, hours worked, the needs and demands of our student population (which may be different to schools against which ESF was compared), and commitments to extra curricular activities. Neither are there quality indicators like examination results, value added data and satisfaction levels among parents. Without such information it is not possible to reach an informed view of the relative return obtained from employing teachers on ESF terms and conditions.

With regard to the question "what is unique about the ESF?", in the context of remuneration we make no claims to uniqueness and given the lack of data in the Report feel unable to comment on other schools in Hong Kong. The schools against which ESF is compared are, in any case, not named in the Audit Report.

We wish to make no comment on our distinctiveness other than to say that we recruit mainly native English speaking teachers, with appropriate qualifications and experience in the British or relevant international curriculum, and in liberal teaching methods. To secure and retain these teachers ESF has to compete in the international market, requiring us to offer internationally competitive terms and conditions. We cannot comment on other schools' terms and how far any particular set of terms are "deserved". In any case, the use of the verb "deserved" is inappropriate; the test is the ability to recruit and retain staff of the required calibre. Clearly, excessive staff turnover is detrimental to school effectiveness. It

also causes extra workload and expense to recruit replacements. As can be seen from Table 3 at paragraph 4.25 of the Report, the percentage of staff leaving has risen over the last 4 years from 7% to 11%.

(b) Housing benefits

It has been necessary to utilise rentals as the Foundation's own portfolio was previously 100% occupied and insufficient to provide the numbers of units required. The present arrangement was implemented in 1992/93 and its objective was to reduce costs. The basis was devised to provide for comparability in housing between staff of comparable status whether occupying the Foundation's own portfolio or in rented quarters. The then Treasurer opined that the rates were comparable to the Company he worked for. The scheme was implemented under the direction of the then Honorary Treasurer and Chairman, both Executive Committee members. The scheme took five months to implement because, as a cost-saving measure, it was bitterly opposed by a number of principals. It was only after meetings between the staff concerned and the then Chairman and Honorary Treasurer that the scheme was finally enforced.

The Executive Committee have agreed to review these housing benefits and it is expected this review will be completed by June 2005.

We have allocated ESF-owned quarters (previously occupied by teachers) to 4 newly appointed senior staff who took up post in September 2004. This decision was taken by the HR Director and myself, and candidates were shown the units concerned at the interview stage in April and May 2004.

(c) Overdraft

Day-to day income and expenditure (current account) is predictable from year to year. However, capital expenditure does not necessarily have a smooth pattern. ESF funded capital expenditure is investment in new and refurbished facilities that directly benefit students. This is over and above the amounts provided by Government for the provision of new facilities which the Foundation acknowledges with gratitude. The Foundation's position on this is set out in paragraph 3.5. of Chapter 4 of the Audit Commission Report. This is further exemplified at page 9 of the Foundation's submission to the meeting of the Public Accounts Committee of 10 December 2004. It would be possible for the Foundation to arrange its finances so that an overdraft was never incurred. This would be contrary to usual commercial practice. No commercial organisation would deny itself access to credit. In the absence of such an overdraft facility, projects which would benefit students would be needlessly delayed. This would not be value for money for stakeholders.

(d) Golden Handshakes

No formal policy has been set down relating to this. In the case of the three resignations cited in the Report, the staff concerned were, effectively, not required to work during their period of notice in the interests of the effective management of the Foundation and schools. In the two cases which did not go to the Executive Committee, these decisions were taken by Officers of the Foundation, (as per Section 9 of the Ordinance) who are Executive Committee members independent of any constituent interest groups. The Executive Committee has agreed that in future the approval of the full Executive Committee will be obtained before making extra payments to staff leaving the ESF and such approvals will be minuted.

Legco PAC's Enquiry of 22 December 2004a. Foundation Meetings (as per Minutes of Meetings)

1.	1 March 2004		
	Chief Secretary	The Hon Donald Tsang	Apology
	Education and Manpower Bureau	Mrs Fanny Law Mr David Wong Mrs Cherry Tse	Present Present Present
2.	11 December 2003		
	Chief Secretary	The Hon Donald Tsang	Apology
	Education and Manpower Bureau	Mrs Fanny Law Mr David Wong Mrs Cherry Tse	Apology Present Apology
3.	12 December 2002		
	Chief Secretary	The Hon Donald Tsang	Apology
	Education Department	Mr Hing-fai Lee Mr Andrew Poon	Apology Present
4.	14 December 2001		
	Chief Secretary	The Hon Donald Tsang	Absent
	Education Department	Ms Betty Ip	Apology
5.	14 December 2000		
	Chief Secretary	No record	No record
	Education Department	Mr M Y Cheng Mr C K Tam Mr Peter Leung	Apology Apology Apology

- b. The Chief Secretary did not attend any of the last five Foundation Meetings between 2000 - 2004.

Appendix 3

(c)

42 Executive Committee meetings were held for the past five years from 1999 to 2004.

<u>Period</u>	<u>No of Executive Committees Held During the Period</u>	<u>EMB Representative</u>	<u>Attendance No. of meetings attended</u>
3 March 1999	1	Ms. Kam Fung Lam	1
8 June 1999 – 30 November 1999	3	Mr. Joseph Wai	2
18 June 2000 – 22 May 2001	10	Mr. Peter Leung	8
16 October 2001 – 15 January 2002	3	Ms. Betty Ip	3
16 April 2002 – 26 November 2002	5	Mr. Andrew Poon	3
21 January 2003 – 10 June 2003	4	Mr. Patrick Li	4
27 June 2003	1	Mr. Tony Tang	1
23 September 2003 – 12 October 2004	14	Mr. David Wong	12
26 October 2004	1	Ms. Maisie Chan	1

(d)

After examination of the relevant meeting minutes, there has been no mention on the corporate governance and Headquarters administration of the ESF by the government representatives at any of the Foundation meetings and the Executive Committee meetings held in the past five years. It would be reasonable to offer an opportunity to EMB to comment directly to Public Accounts Committee in respect of (d) (ii).

Executive Committee Meeting held between 1999 - 2004

<u>Date of Meeting</u>	<u>EMB Representative</u>	<u>Attendance</u>
3 March 1999	Ms. Kam Fung <u>Lam</u>	Present
8 June 1999	Mr. Joseph Wai	Apology
12 October 1999	Mr. Joseph Wai	Present
30 November 1999	Mr. Joseph Wai	Present
18 January 2000	Mr. Peter Leung	Present
7 March 2000	Mr. Peter Leung	Present
5 April 2000	Mr. Peter Leung	Present
13 June 2000	Mr. Peter Leung	Present
17 October 2000	Mr. Peter Leung	Present
28 November 2000	Mr. Peter Leung	Apology
12 December 2000	Mr. Peter Leung	Present
16 January 2001	Mr. Peter Leung	Apology
6 March 2001	Mr. Peter Leung	Present
22 May 2001	Mr. Peter Leung	Present
16 October 2001	Ms. Betty Ip	Present
4 December 2001	Ms. Betty Ip	Present
15 January 2002	Ms. Betty Ip	Present
16 April 2002	Ms. Andrew Poon	Present
11 June 2002	Mr. Andrew Poon	Present
8 October 2002	Mr. Andrew Poon	Present
14 November 2002	Mr. Andrew Poon	Apology

26 November 2002	Mr. Andrew Poon	Apology
21 January 2003	Mr. Patrick Li	Present
18 March 2003	Mr. Patrick Li	Present
13 May 2003	Mr. Patrick Li	Present
10 June 2003	Mr. Patrick Li	Present
27 June 2003	Mr. Tony Tang	Present
23 September 2003	Mr. David Wong	Present
7 October 2003	Mr. David Wong	Present
25 November 2003	Mr. David Wong	Present
9 January 2004	Mr. David Wong	Present
10 February 2004	Mr. David Wong	Present
8 March 2004	Mr. David Wong	Present
23 March 2004	Mr. David Wong	Present
28 April 2004	Mr. David Wong	Present
17 May 2004	Mr. David Wong	Present
24 May 2004	Mr. David Wong	Present
15 June 2004	Mr. David Wong	Present
23 June 2004	Mr. David Wong	Present
28 September 2004	Mr. David Wong	Apology
12 October 2004	Mr. David Wong	Apology
26 October 2004	Ms. Maisie Chan	Present



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Urgent By Fax

來函編號 Your Ref CB(3)/PAC/R43

7 January 2005

Clerk, Public Accounts Committee
(Attn: Ms Dora WAI)
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

[Fax No. 2537 1204]

Dear Ms Wai,

**The Director of Audit's Report on the
results of value for money audits (Report No. 43)**

**Chapter 4: Corporate governance and
Headquarters administration of the English Schools Foundation**

Thank you for your letter of 6 January 2005. I append below the information and my comments requested in your letter.

***Audit Commission's examination of minutes of
Foundation meetings and Executive Committee meetings***

The Audit Commission (Audit's review of the minutes of meetings of the English Schools Foundation (ESF) covered the period September 2000 to April 2004. During this period, the Foundation and its Executive Committee held five and 27 meetings respectively. As part of the audit review, Audit staff have examined all the minutes of these 32 meetings. Accordingly, Audit staff have seen the minutes of the five Foundations meetings and 27 (covering the period September 2000 to April 2004) of the 42 Executive Committee meetings respectively referred to in Appendices 2 and 3 to the Acting Chief Executive of the ESF's letter of 4 January 2005.

***Attendance of the government representatives
at the five Foundation meetings***

As stated in paragraph 2.19 of Chapter 4 of the Director of Audit's Report No. 43, the failure of members to attend Foundation meetings reduces their opportunities to contribute to the ESF. According to the Regulations of the English Schools Foundation, there are four government representatives on the Foundation (see Appendix B to Chapter 4 of the Director of Audit's Report No. 43). According to the Foundation's meeting minutes:

- (a) at the two Foundation meetings in December 2000 and December 2001, all the four government representatives did not attend;
- (b) at each of the two Foundation meetings in December 2002 and December 2003, only one of the four government representatives attended; and
- (c) at the Foundation meeting in March 2004, three of the four government representatives attended.

Audit considers that the attendance rate of 25% (Note) of government representatives at the above-mentioned five Foundation meetings was unsatisfactory.

***Attendance of the government representative
at the 42 Executive Committee meetings***

As stated in Appendix 3 to the Acting Chief Executive of the ESF's letter of 4 January 2005, of the 42 Executive Committee meetings held between March 1999 and October 2004, the government representative attended 35 of them, representing an attendance rate of 83%. Audit considers this attendance rate acceptable.

Note: *Government representatives' attendance rate is calculated by:*

$$\frac{\text{Total number of government representatives' attendances at the 5 meetings}}{4 \text{ government representatives on the Foundation} \times 5 \text{ meetings}} \times 100\%$$

Government representatives' views on the corporate governance and Headquarters administration of the ESF at Foundation meetings and Executive Committee meetings

Regarding the statement in paragraph (d) in Appendix 3 to the Acting Chief Executive of the ESF's letter of 4 January 2005 that "there has been no mention on the corporate governance and Headquarters administration of the ESF by the government representatives at any of the Foundation meetings and the Executive Committee meetings held in the past five years", Audit examination of the minutes of the Foundation meetings and the Executive Committee meetings covering the period September 2000 to April 2004 revealed that:

- (a) there were no recorded views of the government representatives on the corporate governance of the ESF at either the Foundation meetings or the Executive Committee meetings;
- (b) there were no recorded views of the government representatives on the Headquarters administration of the ESF at the Foundation meetings; and
- (c) on some occasions, the government representative expressed views on the Headquarters administration of the ESF at some Executive Committee meetings. In the event that the Committee wishes to obtain information about these views, it may wish to request the ESF to provide it with the pertinent minutes of meetings.

Yours sincerely,



(Patrick LEUNG)
for Director of Audit

c.c. Secretary for Education and Manpower
Permanent Secretary for Education and Manpower
Chairman, English Schools Foundation
Acting Secretary and Chief Executive, English Schools Foundation
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred WONG)



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11 January 2005

Clerk to Committee
Public Accounts Committee
Legislative Council Secretariat
8 Jackson Road
Central
Hong Kong

(Attn: Ms Dora Wai)

Dear Ms Wai,

**The Director of Audit's Report on the
Results of Value for Money Audits (Report No. 43)**

**Chapter 4: Corporate Governance and Headquarters Administration
of the English Schools Foundation ("ESF")**

Thank you for your letter of 11 January 2005 seeking supplementary information in following up the hearing session held yesterday.

X X X X X X X X X

Attendance Record

Contrary to Mr Bohan's advice, EMB was represented at the ExCom meeting held on 28 September 2004 by Mr Samson Lai in his capacity as Acting Principal Assistant Secretary for Education and

Manpower (the incumbent Principal Assistant Secretary was on leave then). An extract from the minutes of that meeting is attached. For the 12 October 2004 meeting, it was our deliberate decision not to attend given that it was convened to consider the ESF's fundraising strategy which is squarely an internal matter of the ESF. In addition, against the backdrop of Government's discussion with the ESF on the future of the subvention arrangement, we considered our absence desirable to forestall any unnecessary speculation and accusation of conflict of interest.

A Member expressed concern as to whether the Government representative on the ESF ExCom contributed to discussion on important agenda items at the September meeting. We wish to point out that the ExCom minutes are not prepared in a verbatim format. Therefore, the absence of express reference to comments made by any one Member could not be used to deduce that that Member made no contribution to the deliberation. In addition, as explained at various PAC hearings, EMB's contribution to ESF deliberation was multi-channelled and took place also outside formal ExCom and Foundation meetings.

Yours sincerely,



(Mrs Cherry Tse)
for Secretary for Education and Manpower

c.c. Acting Secretary and Chief Executive, ESF]
 Chairman, ESF] w/o encl
 Secretary for Financial Services and the Treasury]
 Director of Audit

*Note by Clerk, PAC:

- (1) *The above only shows the item on "Attendance Record" in the Secretary's letter.*
- (2) *The extract from the minutes of the ExCom meeting on 28 September 2004 not attached.*



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APPENDIX 26

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10 December 2004

Ms Dora Wai
Public Accounts Committee
Legislative Council Building
8 Jackson Road
Central
Hong Kong

By Fax 2537 1204 and Post

Dear Ms Wai,

**The Director of Audit's Report on the
Results of Value for Money Audits (Report No. 43)**

**Chapter 4 : Corporate Governance and
Headquarters Administration of the English Schools Foundation**

Please find attached the Draft Guidelines for the Restructuring of the Governance and Management of the ESF which has been approved by members at the Foundation Meeting on 9 December 2004.

A Chinese translation of the paper will be provided in due course.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive
English Schools Foundation

Att

cc Secretary for Education and Manpower
Chairman, English Schools Foundation
Secretary for Financial Services and The Treasury (Attn : Mr Manfred Wong)
Director of Audit
Ms Gloria Ng

建立優良教育 承擔香港未來
COMMITTED TO HONG KONG'S FUTURE AND
TO EXCELLENCE IN EDUCATION

APPROVED BY MEMBERS
AT
THE ESF FOUNDATION MEETING ON 9 DECEMBER 2004

DRAFT GUIDELINES FOR THE RESTRUCTURING OF
THE GOVERNANCE AND MANAGEMENT OF THE ESF

Introduction

Initially, it was thought prudent to make changes in the margins and thus avoid the long and tedious process of seeking legislative amendments to the Ordinance. But after detailed considerations this was not a possible option given that quite fundamental and sweeping changes have to be made. Since we are to go through a legislative process at any rate it will be by far better to effect changes that are far ranging and in line with best practice.

The constitutional underpinning of the ESF is the special ordinance from the government of the HKSAR. This Ordinance covers the following:

- The name and registered office of the organisation
- Its mission and purpose
- The rights and duties of members
- The election and replacement of the governing body
- The functions and powers of the governing body
- The appointment and removal of officers
- The procedures for members' meetings, the preparation of accounts
- The management of its schools
- Form of contract
- The formation of committees

Anthony and Young had this observation to make of non-profit organisations:

Although the governing body supposedly represents the interests of the general, or in some cases, that part of the public that has provided major financial support, it frequently is insufficiently informed about major issues facing the organization and its decisions therefore are not always optimal...The absence of profit measures, the tendency to be service organizations and the differences in top management structure result in a tradition of inadequate management controls.

This observation is especially germane to the ESF in view of the debacle in the past year and the recommendations made in the Audit Report. These aside, changes in the political landscape, an increasingly competitive environment, the new approaches to education, the mounting demand for greater transparency, quality and accountability are additional factors that drive the need for a restructuring of its governance and management.

The most fundamental change to be effected is the separation of governance and management roles. This draft will therefore address these issues separately.

Guiding principles for the restructuring of governance

Governance processes and structures should:

1. Drive probity, efficiency and effectiveness
2. Ensure compliance with statutory and regulatory requirements
3. Provide proper stewardship for assets and resources
4. Ensure the proper and effective use of funds, both public and private
5. Follow a policy of openness and transparency in dissemination of decisions made
6. Focus on strategic planning rather than micromanaging
7. Make provisions for risk management and control
8. Demonstrate accountability
9. Require a proper code of conduct in the performance of public service

The governance structure and functions

A. The ESF Council

Role: The Council is the supreme governing body of the ESF.
It will replace the current Foundation.

Composition: No more than 25 members with a clear majority of lay members external to the ESF with a ratio of 2:1.

Guidelines for the membership:

1. Each of the members elected or nominated should serve on an ad personam basis. They should serve as trustees rather than the representative of any constituency.
2. The members will sign a code of conduct and undertake to abide by it.
3. There should be an appropriate mix of old and new members, staggered terms for 25% of members.
4. Each member apart from the ex-officio members should not serve more than two consecutive terms each lasting for three years.
5. The membership should have a range of expertise, knowledge and skills taking into account the needs of the ESF at a particular time. At the time of election or appointment the Council should provide a list of the members and their expertise to serve as a guide in this process.
6. There should be a register of members' interest.
7. The staff members elected should not concurrently hold office in staff associations.
8. The members of Council will elect a chairman, vice-chairman and treasurer from amongst its lay members.
9. The Council should review its effectiveness every six years and the results of the review be published in the ESF annual report.

B. The Nomination Committee

The Committee shall have no more than 20 members consisting of nominations from the Joint Council of Parent Teacher Association and the Management Committee. The members shall nominate the 3-5 lay members of Council.

C. Committee Structure

There shall be number of Standing Committees of Council this may include an Audit Committee, Management Committee, Academic Committee, Staff Council and the Joint Council of Parent and Teacher Associations. There should be a balance between the need for participation by various stakeholders and the size as well as the number of committees.

The Council may, as when necessary, appoint task forces, steering groups etc. to perform specific functions.

The management structure and functions

Senior Management Team

Role: To be responsible for the day to day running of the schools, to implement the strategies and policies approved by Council, to advise Council on matters relating to any aspects of the ESF. This will be headed by the Chief Executive.

The Chief Executive Advisory Group

Role: To advise the CE and the SMT on issues relating to management.

The School Management Structure

This will remain essentially unchanged apart from the administrative procedures that will need to be put in place on the recommendations of the ICAC and the Audit Report.

Incidentals

To reflect their roles more accurately the Secretary should be re-titled Chief Executive and the Financial Controller the Director of Finance.

Implementation process and timeline

Approval of the draft guidelines by ExCom – November 2004

Approval of the draft guidelines by the Foundation – December 2004

Appointment of a task force by ExCom, the task force will be charged with the task to work out the details of the restructuring in consultation with the CE designate – December 2004 to January 2005

Approval of the draft details by ExCom – February 2005

Open consultation of the draft – February to April 2005

Task Force to make the necessary amendments based on the results of the consultation – May 2005

Approval of the draft by ExCom – June 2005

Approval of the draft by the Foundation at an extraordinary meeting – July 2005

Drafting of the necessary amendments to the Ordinance and the Regulations -- ??

Seek legislative amendments to the Ordinance in the form of a private member's bill if appropriate -- ??

Implementation and the drafting of the Standing Orders --??

List of References

1. *A Guide for Effective Audit Committees*. Hong Kong Society of Accountants, 2002
2. *Corporate Governance for Public Bodies: A Basic Framework*. Hong Kong Society of Accountants, 2003
3. *Fit for Purpose: A review of governance and management structures at The University of Hong Kong*, 2003
4. *International Corporate Governance: Text, Readings and Cases* Robert Tricker, 1994
5. *Management Review of the University of Hong Kong*. University Grants Committee, 1999
6. *Non-statutory Guidelines on Directors' Duties*, Companies Registry, HKSAR Government
7. *OECD Principles of Corporate Governance 2004*
8. *Report of the Committee on the Financial Aspects of Corporate Governance (Cadbury Committee) 1992*



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18 January 2005

Ms. Dora Wai
Legislative Council Building
8 Jackson Road
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Dear Ms. Wai,

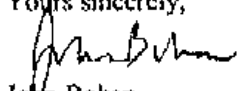
**The Director of Audit's Report on the
Results of value for money audits (Report No. 43)**

**Chapter 4: Corporate governance and
Headquarters administration of the English Schools Foundation (ESF)**

I refer to your letter of 13 January 2005. I have answered below the three points you raise in the same order as in your letter.

- (a) Having consulted the Chairman, it is proposed that EMB will be able to appoint one or two members to the new ESF Council. The precise role will be considered by ESF's task force which is about to start work on issues of governance, so it is not possible to report further at present. However, the recommendations of the task force will need to be discussed with EMB to ensure the proposals conform to EMB's own views on its role and relationship with ESF.
- (b) The percentage of quarters expenses for ESF Headquarters staff is 22%.
- (c) The PAC will be kept informed of the outcome of this exercise as you have requested.

Yours sincerely,


John Bohan
Acting Chief Executive

/mt

c.c. Secretary for Education and Manpower
Permanent Secretary for Education and Manpower
Chairman, English Schools Foundation
Secretary for Financial Services and the Treasury
(Attn: Mr. Manfred Wong)
Director of Audit
Human Resources Director, English Schools Foundation



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APPENDIX 28

10 January 2005

Ms. Dora Wai
Public Accounts Committee
Legislative Council
8 Jackson Road
Central
Hong Kong

Dear Ms. Wai,

Director of Audit's Report No. 43

- Chapter 3: Government subsidies to the English Schools Foundation**
Chapter 4: Corporate governance and Headquarters administration of the English Schools Foundation
Chapter 5: School administration of the English Schools Foundation

Please find attached ESF's summary of the Audit recommendations contained in Chapters 3, 4 and 5 and the action proposed in each case. I would be grateful if you could circulate these documents to the members of the Public Accounts Committee.

Thank you.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive

c.c. Secretary for Education and Manpower
Chairman, English Schools Foundation
Secretary for Financial Services and the Treasury
(Attn: Mr. Manfred Wong)
Director of Audit

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RECOMMENDATIONS ON AUDIT REPORT
Chapter 3 – Government Subsidies to the ESF

Audit Recommendations	Response from ESF	Action
<p><u>Part 2 : Reviews of Government Subsidies to ESF and International Schools</u> <u>(Page 24 – 2.26)</u> Audit has <i>recommended</i> that the Secretary for Education and Manpower should:</p> <p>(a) expedite action to complete the review of government subsidies to ESF schools; and</p> <p>(b) if the recurrent government subsidies to ESF schools are to be withdrawn, implement the withdrawal using a phased approach so that the ESF, its staff and management, its students and their parents can plan well ahead.</p>		
<p><u>Part 3 : Freezing Government Subsidies to ESF and</u> <u>Recent Fact-Finding Exercise</u> <u>(Page 32 – 3.18)</u> Audit has <i>recommended</i> that the Secretary for Education and Manpower should:</p> <p>(a) brief the Panel on Education of the Legislative Council on the interim measures of freezing the per-class subsidies to the ESF at the 1999-2000 school-year level, and the number of ESF classes eligible for recurrent government subsidies;</p> <p>(b) seek the authorisation of the Executive Council and the Legislative Council for the interim measures on providing recurrent government subsidies to the ESF if changes to ESF subsidy arrangements cannot be finalised in the</p>		

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<p>near future; and</p> <p>(c) seek the approval of the Executive Council and the Legislative Council for changes resulting from EMB review of government subsidies to the ESF.</p>		
<p>(Page 32 – Item 3.17) Audit considers that, if the fact-finding exercise leads to a reduction or an increase in government subsidies to the ESF, this may be at variance with the Government's parity of subsidy principle in subsidising the ESF. The EMB needs to seek the approval of the Executive Council and the Finance Committee for making a variation to the principle.</p> <p>(Page 32 – Item 3.18) Audit has recommended that the Secretary for Education and Manpower should seek the approval of the Executive Council and the Legislative Council for changes in the approach to providing recurrent government subsidies to the ESF.</p>		
	<p>(Page 32 – Item 3.20) The ESF has stated that, at the conclusion of the three audit reviews conducted by Audit and upon completion of the associated work, it will expedite completion of the fact-finding exercise.</p>	<p>Latest response : 3 November 2004</p> <p>Government reply : 7 December 2004</p> <p>Next ESF response : 11 January 2005</p>

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Audit Recommendations	Response from ESF	Action
<p>Part 2: Corporate Governance (Page 10 – Item 2.11) Audit has recommended that the ESF should:</p> <p>(a) conduct a review with a view to reducing the membership size of the Foundation, with reference to the best practices of similar educational institutions;</p> <p>(b) conduct a review of the Regulations of the English Schools Foundation with a view to reflecting the latest developments in the community; and</p> <p>(c) consider establishing an advisory body similar to those established by the UGC-funded institutions to provide a forum for representatives of different stakeholders to make contributions to its developments.</p>	<p>(Page 11 – Item 2.12) The Executive Committee of the Foundation accepts that the ESF's governance should be reviewed with a view to ensuring that it is in line with the best practices.</p>	<p>It was proposed by the Executive Committee and agreed in principle by the Foundation at the meeting held on 9 December 2004 to revise the governance of the Foundation. Details of the implementation process and timeline are contained in the paper approved by the Foundation Meeting, a copy of which is attached as Appendix A.</p>
<p>(Page 15 – Item 2.21) Audit has recommended that the ESF should:</p> <p>(a) conduct a review of the composition of Foundation members with a view to ensuring that external members will constitute a majority at Foundation meetings;</p> <p>(b) consider increasing the ratio of external members to internal members of the Foundation to, say 2 : 1;</p>	<p>(Page 15 – Item 2.22) The Executive Committee of the Foundation accepts that the ESF's governance should be reviewed with a view to ensuring that it is in line with the best practices.</p>	<p>As Item 2.11 above.</p>

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<p>(c) issue reminders to the related organisations if the attendance rates of their representatives at Foundation meetings are low; and</p> <p>(d) amend the Regulations of the English Schools Foundation to the effect that ESF staff members of the Executive Committee of the Foundation would abstain from voting on matters concerning ESF staff benefits at its meetings.</p>		
<p>(Page 17 – Item 2.27) Audit has recommended that the ESF should:</p> <p>(a) set up an audit committee under the Foundation comprising external members;</p> <p>(b) ensure that its internal audit office is staffed by well qualified and experienced personnel reporting directly to the audit committee; and</p> <p>(c) require its internal audit office to prepare annual audit programmes (to be approved by the audit committee) for conducting reviews covering major and high-audit-risk activities of the ESF, including the ESF Educational Services Limited.</p>	<p>(Page 17 – Item 2.28) The Executive Committee of the Foundation accepts that the ESF's governance should be reviewed with a view to ensuring that it is in line with the best practices.</p>	<p>Actioned – Audit Committee approved by Executive Committee at the meeting held on 23 November 2004. The first meeting of the Audit Committee was on 7 December 2004. It has since met KPMG, the external auditors, and had substantive discussions with management on 17 December 2004 and 7 January 2005.</p>

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<p>Part 3 : Financial Management (Page 21 – Item 3.9) Audit has recommended that the ESF should:</p> <p>(a) take action to reduce its net current liabilities; and</p> <p>(b) avoid preparing budgets based on a high level of bank overdraft at its financial year end.</p>	<p>(Page 22 – Item 3.10) The ESF has stated that:</p> <p>(a) the Executive Committee of the Foundation will continue to carefully:</p> <ul style="list-style-type: none"> (i) monitor ESF budgets and current liabilities; and (ii) determine prudent limits to borrowing; and <p>(b) no commercial organisation would deny itself access to credit which can help maximise value for shareholders.</p>	<p>The Executive Committee will review this recommendation when it reviews the First Stage Estimates 2005/06 at the meeting of 22 March 2005.</p>
<p>(Page 24 – Item 3.15) Audit has recommended that, in order to reduce its bank overdrafts at its financial year end, the ESF should adopt an arrangement under which:</p> <p>(a) its schools would transfer a part of their bank deposits for which they do not have immediate needs to the Foundation Office; and</p> <p>(b) the Foundation Office would refund to individual schools the money deposited with it when the need arises.</p>	<p>(Page 24 – Item 3.16) The Executive Committee of the Foundation accepts that it is necessary to make improvement on the arrangement for ESF schools to maintain bank balances. The ESF has stated that it will adopt:</p> <p>(a) either an arrangement under which ESF schools would transfer a part of their bank deposits (for which they do not have immediate needs) to the Foundation Office; or</p> <p>(b) a central cash management and payment system similar to those adopted by large commercial organisations, without the need for each ESF school to maintain its own bank account.</p>	<p><u>Actioned.</u> The Foundation will enter into an alternative arrangement with its bankers to offset credit balances on its accounts with any debit balances on other accounts. Target : 20 January 2005.</p>

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<p>Part 4 : Staff Remuneration and Recruitment (Page 28 – Item 4.10) Audit has recommended that the ESF should conduct a review of the remuneration packages of its senior staff with a view to ensuring that they are broadly in line with those of similar posts in other local educational organisations.</p>	<p>(Page 29 – Item 4.11) The ESF has stated that the remuneration packages of its senior staff: (a) have been reviewed by its Pay Review Body; and (b) will be within the purview of its Remuneration Study Group.</p>	<p>Actioned. Remuneration Study Group is due to report in June 2005.</p>
<p>(Page 35 – Item 4.26) Audit has recommended that the ESF should: (a) conduct a review of the remuneration packages of its teaching staff with a view to setting new packages, having regard to those of other major local international schools; (b) in doing so, take into consideration the need to pay competitive salaries to recruit and retain quality teaching staff from English-speaking countries; (c) implement the new remuneration packages on newly recruited teaching staff as soon as possible, and on existing teaching staff over a period of time, taking into account the effects of the new remuneration packages on their financial commitments; and (d) draw up central guidelines on the payment of responsibility allowances to teaching staff for compliance by its schools, with reference to the practices adopted by other local international schools.</p>	<p>(Page 36 – Item 4.27) The ESF agrees with the audit recommendations in paragraph 4.26. It has stated that: (a) it has established a Remuneration Study Group to conduct reviews of the remuneration packages of its teaching staff; (b) it must continue to be the employer of choice; (c) changes to contractual conditions of its teaching staff can only be implemented on renewal of their contracts or with their consent; and (d) principals and school councils require a degree of independence on payment of responsibility allowances to teaching staff to meet the unique circumstances of individual schools.</p>	<p>(a) to (c) Actioned. Remuneration Study Group is due to report in June 2005.</p> <p style="text-align: right;">Implementation – by 30 April 2005.</p>

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<p>(Page 38 – Item 4.32) Audit has recommended that the ESF should:</p> <p>(a) ensure that the approval of the Executive Committee of the Foundation is obtained before making extra payments to ESF senior staff upon their leaving the ESF; and</p> <p>(b) record such approvals in the meeting minutes of the Executive Committee of the Foundation.</p>	<p>(Page 38 – Item 4.33) The ESF agrees with the audit recommendations in paragraph 4.32. It has stated that:</p> <p>(a) in the past, the agreement of the Chief Executive of the ESF and the Chairman/Vice-chairman of the Foundation was sought before making extra payments to ESF senior staff upon their leaving the ESF for contractual or confidentiality reasons; and</p> <p>(b) it will record the approval of the Executive Committee of the Foundation in its meeting minutes regarding extra payments to ESF senior staff upon their leaving the ESF, if this does not infringe legally binding agreements.</p>	<p>Actioned – 17 December 2004.</p>
<p>(Page 41 – Item 4.38) Audit has recommended that the ESF should:</p> <p>(a) review its recruitment practices with a view to reducing recruitment costs; and</p> <p>(b) send the minimum number of its staff overseas to interview applicants when it is necessary to do so.</p>	<p>(Page 41 – Item 4.39) The ESF agrees with the audit recommendations in paragraph 4.38. It has stated that its Recruitment Working Party established in the 2003-04 ESF financial year endorsed the policy of:</p> <p>(a) reducing the number of its school principals travelling overseas to interview applicants; and</p> <p>(b) reducing the time spent overseas by its interview-team members by using more video-conference interviews.</p>	<p>Actioned. The arrangements being made for the forthcoming recruitment round implement these recommendations.</p>

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<p>Part 5 : Staff Housing Benefits (Page 48 – Item 5.14) Audit has recommended that the ESF should:</p> <p>(a) as far as possible accommodate eligible staff in the staff quarters it owns, instead of leasing quarters for them;</p>	<p>(Page 48 – Item 5.15) The ESF agrees with the audit recommendations in paragraph 5.14. It has stated that:</p> <p>(a) it has taken action in respect of the audit recommendations in paragraph 5.14(a), (b) and (c). In the 2004-05 ESF financial year, three newly-appointed principals, whose predecessors were previously accommodated in ESF-leased quarters, have been allocated with ESF-owned quarters;</p>	<p>(a) to (c) <u>Actioned.</u></p>
<p>(b) lease the vacant staff quarters to its staff and outsiders to generate rental income;</p>		
<p>(c) select those appropriate ESF-owned Teaching-staff Grade quarters for re-grading as Senior-staff Grade quarters for allocation to its senior staff;</p>		
<p>(d) consider converting two adjacent Teaching-staff Grade quarters into one Senior-staff Grade quarters for allocation to a senior staff member if it is justified to do so;</p>	<p>(b) it will examine the technical and structural feasibility of the audit recommendation in paragraph 5.14(d);</p>	<p>Previously <u>Actioned.</u> See Building Management Department paper dated 12 December 1998.</p>
<p>(e) seek and record the approval of the Executive Committee of the Foundation if there is a need for the ESF to lease a staff quarters for a senior staff member exceeding his rent entitlement;</p>	<p>(c) the Executive Committee of the Foundation will consider the audit recommendation in paragraph 5.14(e). In the past, the authority to approve leasing a staff quarters for a senior staff member exceeding his rent entitlement was delegated to the Chief Executive of the ESF; and</p>	<p><u>Implemented.</u></p>

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<p>(f) seek the approval of the Executive Committee of the Foundation for paying the rates and management fees of ESF-leased quarters for its senior staff, irrespective of their rent entitlements; and</p> <p>(g) conduct a review of the rental-value level of staff quarters for its senior staff with reference to the housing benefits provided by other local educational institutions.</p>	<p>(d) it will take action in respect of the audit recommendations in paragraph 5.14(f) and (g).</p>	<p>A paper will be submitted in respect of Items 5.14(f) and (g) to Executive Committee by 31 March 2005. In the long-term the Remuneration Study Group will need to recommend future policy.</p>
<p>(Page 54 – Item 5.31) Audit has recommended that the ESF should:</p> <p>(a) formulate a plan for disposing of its surplus staff quarters;</p> <p>(b) negotiate with the Government on removing the non-assignment clauses in the government leases of its staff quarters at the Braemar Heights and at the Beacon Hill School;</p> <p>(c) seek and document professional advice obtained on the market rental values of its staff quarters for letting to ineligible staff; and</p>	<p>(Page 55 – Item 5.32) The ESF has stated that:</p> <p>(a) the Executive Committee of the Foundation will review carefully the audit recommendation in paragraph 5.31(a), having regard to the long-term needs of the ESF and the financial security conferred by the ownership of such fixed assets;</p> <p>(b) it agrees with the audit recommendation in paragraph 5.31(b). The Government would need to cooperate on this recommendation. The Beacon Hill School flats need careful consideration because of security, health and safety issues;</p> <p>(c) regarding the audit recommendation in paragraph 5.31(c), it is ESF practice to seek professional advice when benchmarking market rental values of its staff quarters for letting to ineligible staff. It accepts that such advice should be in writing, filed and retained; and</p>	<p>A paper will be submitted in respect of Items 5.31(a) and (b) to Executive Committee by June 2005.</p> <p style="text-align: right;"><u>Actioned.</u></p>

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<p>(d) obtain the prior approval from the Executive Committee of the Foundation before selling its staff quarters.</p>	<p>(d) it agrees with the audit recommendation in paragraph 5.31(d). The sale of staff quarters had been sanctioned by the Executive Committee of the Foundation in 1994, following its endorsement of the report of a consultancy study on the issue. All sales of staff quarters will require the approval of the Executive Committee of the Foundation in future.</p>	<p><u>Actioned.</u></p>
<p>Part 6 : Staff Medical Benefits <u>Reimbursement of Medical Expenses Exceeding Entitlement</u> (Page 61 – Item 6.14) Audit has recommended that the ESF should:</p> <p>(a) engage a medical insurance company to provide a medical scheme for its non-teaching staff and their dependants, with reference to similar schemes of other local educational institutions;</p> <p>(b) set an annual maximum amount of reimbursable dental expenses for each member of ESF senior staff and teaching staff and each of their dependants;</p> <p>(c) engage a medical insurance company to provide a dental scheme for all ESF staff and their dependants, with reference to similar schemes of other local educational</p>	<p>(Page 61 – Item 6.15) The ESF has stated that:</p> <p>(a) in the 2003-04 ESF financial year, it took action in respect of the audit recommendation in paragraph 6.14(a). However, ESF staff did not favour the proposed scheme. It will reconsider the audit recommendation;</p> <p>(b) it accepts in principle the audit recommendation in paragraph 6.14(b). Presently, reimbursement of dental expenses only covers basic dental treatment. By setting a maximum amount of reimbursable dental expenses for each eligible person, ESF staff could be encouraged to claim the maximum amount of expenses;</p> <p>(c) the audit recommendation in paragraph 6.14(c) was reviewed when the medical scheme was outsourced in 2001. At that time, the level of cover provided by a</p>	<p><u>Actioned.</u> Proceeding to obtain proposals from insurers. Due to complete by 28 February 2005.</p> <p><u>Actioned.</u> Proceeding to obtain proposals from insurers (which would include limits). Due to complete by 28 February 2005.</p> <p><u>Actioned.</u> Proceeding to obtain proposals from insurers. Due to complete by 28 February 2005.</p>

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<p>institutions; and</p>	<p>medical insurance company, when compared with the insurance premium, was not considered to be value for money. It will re-examine the audit recommendation; and</p>	<p>Agreed. Will also seek delegated authority for Chief Executive/Human Resources Director to approve emergency treatment.</p>
<p>(d) seek and record the approval of the Executive Committee of the Foundation if the medical benefits received by an ESF staff member exceed his entitlement.</p>	<p>(d) it agrees in principle with the audit recommendation in paragraph 6.14(d). The event mentioned in paragraphs 6.12 and 6.13 was an isolated and unique case, with the agreement being given by the then Chief Executive of the ESF. The Executive Committee of the Foundation has stated that it would consider similar events on a case-by-case basis in future. Some cases involve emergency treatment and there may not be sufficient time for contacting all Executive Committee members before the treatment. Therefore, there needs to be some means of delegating authority for such cases.</p>	<p>Paper will be submitted to Executive Committee by 31 March 2005.</p>
<p><u>Part 7 : Entertainment Expenses</u> (Page 66 – Item 7.13) Audit has recommended that the ESF should:</p> <p>(a) abolish the existing arrangement for setting annual individual budgets for entertainment expenses for some ESF staff;</p>	<p>(Page 67 – Item 7.14) The ESF has stated that:</p> <p>(a) the Executive Committee of the Foundation will consider the audit recommendations in paragraph 7.13(a), (b) and (d) as part of a further review of entertainment expenses. The present ESF arrangement for setting annual individual budgets for entertainment expenses only applies to 22 ESF designated staff out of a total of 1,218 ESF staff;</p>	<p>Paper will be submitted to Executive Committee by 31 March 2005.</p>
<p>(b) set up a new system so that only designated staff of the ESF may submit claims for reimbursement of entertainment;</p>		<p>Paper will be submitted to Executive Committee by 31 March 2005.</p>

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<p>expenses on a need basis;</p> <p>(c) strictly enforce its revised policy on reimbursement of entertainment expenses which prohibits reimbursement of entertainment expenses relating to staff functions;</p>	<p>(b) it agrees with, and has implemented, the audit recommendations in paragraph 7.13(c) and (f); and</p>	<p><u>Actioned</u> as at 1 September 2004.</p>
<p>(d) set up a staff welfare fund to meet the expenses of staff functions;</p>	<p>(c) it agrees in principle with the audit recommendation in paragraph 7.13(e). The Executive Committee of the Foundation will consider the appropriate maximum limit on reimbursable entertainment expenses allowed for each participant in each function.</p>	<p>Paper will be submitted to Executive Committee by 31 March 2005.</p> <p>Paper will be submitted to Executive Committee by 31 March 2005.</p>
<p>(f) strictly enforce its revised policy on reimbursement of entertainment expenses which requires ESF staff submitting claims to clearly state:</p> <ul style="list-style-type: none"> (i) the name of each ESF participant and his capacity; (ii) for guests, their names and the organisations they represent; and (iii) the purpose of the function. 	<p>(d) it agrees with, and has implemented, the audit recommendations in paragraph 7.13(c) and (f).</p>	<p><u>Actioned</u> as at 1 September 2004.</p>

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Audit Recommendations	Response from ESF	Action
<p>Part 1: Introduction (Page 5 – Item 1.17) Audit has recommended that the ESF should:</p> <ul style="list-style-type: none"> (a) fulfil its responsibilities for providing its schools with: <ul style="list-style-type: none"> (i) proper guidelines to help them deal with various administrative matters; and (ii) adequate support in implementing the guidelines; and (b) carry out internal audits of them to ascertain whether the guidelines have been complied with. 	<p>(Page 5 – Item 1.18) The ESF agrees with the audit recommendations. It has stated that:</p> <ul style="list-style-type: none"> (a) the ESF does provide its schools with guidelines to deal with administrative matters but, as Audit has rightly pointed out, these need to be proper and well supported; (b) the revision of Schools' Circulars/Administrative Memoranda is now in place to help schools deal with various administrative matters. Its Human Resources Department will oversee the process. In fact, two school principals began work on the administrative procedures in July 2004; (c) it is accepted that seminars and school visits need to be more systematically programmed to provide adequate support to schools in implementing the guidelines; and (d) it is logical to extend the programme of internal audits to cover the audit recommendations. 	<p>Revision already underway. 30% completed by 1 September 2004, 60% by 1 January 2005, 100% by 31 August 2005.</p> <p>With the establishment of the new CPD Co-ordinator post, specific needs will be identified and appropriate training provided.</p> <p>The newly created ESF Audit Committee will oversee the programme of internal audits.</p>

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<p>Part 2: Corporate Governance of Schools (Page 10 – Item 2.9) Audit has recommended that ESF schools should consider inviting suitable alumni to join their councils.</p>	<p>(Page 10 – Item 2.10) The ESF has stated that:</p> <p>(a) it recognises the value of more alumni being represented on school councils;</p> <p>(b) work has begun in 2003-04 to develop a systematic approach to the use of such people. Although the outcomes are not yet evidenced, it wishes to increase the representation of alumni on school councils; and</p> <p>(c) more alumni may be invited once alumni lists are complete.</p>	<p>This will be considered as part of the review of governance – see the ESF response to Chapter 4, paragraph 2.11.</p>
<p>(Page 12 – Item 2.15) Audit has recommended that the ESF should request its school councils to:</p> <p>(a) clearly set out and document their decision-making powers (i.e. what matters and changes require their approval) and the delegation of such powers; and</p> <p>(b) review periodically the delegated decision-making powers.</p>	<p>(Page 12 – Item 2.16) The ESF agrees that the decision-making powers of school councils should be better articulated. The ESF has stated that:</p> <p>(a) each school council should itemise its powers of delegation;</p> <p>(b) training for council members may be required; and</p> <p>(c) a bi-annual agenda item will be initiated by ESF representative to review the delegated decision-making powers.</p>	<p>This recommendation will be implemented through the revision of the booklet "Guidance for School Councilors". After consultation with stakeholder groups, the revised guidance will be effective by 30 June 2005.</p> <p>The existing programme of School Councilors training will be extended beginning with the course on 22 January 2005.</p> <p>This will be actioned from the Chief Executive's Office.</p>

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<p>(Page 15 – Item 2.22) Audit has recommended that the ESF should encourage its school councils to:</p> <p>(a) participate actively in the management and implementation of significant school activities; and</p> <p>(b) consider setting up appropriate sub-committees to further their involvement in key decisions on significant school matters.</p>	<p>(Page 15 – Item 2.23) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) it will consider rewriting the roles of school council members;</p> <p>(b) it recognises that, by widening the role of school council members, it must meet their training needs; and</p> <p>(c) the setting up of sub-committees will be carried out using acknowledged best practice as a guide.</p>	<p>This recommendation will be implemented through the revision of the booklet "Guidance for School Councilors". After consultation with stakeholder groups, the revised guidance will be effective by 30 June 2005.</p> <p>The existing programme of School Councilors training will be extended beginning with the course on 22 January 2005.</p> <p>This recommendation will be implemented through the revision of the booklet "Guidance for School Councilors". After consultation with stakeholder groups, the revised guidance will be effective by 30 June 2005.</p>
<p>(Page 17 – Item 2.29) Audit has recommended that the ESF should:</p> <p>(a) remind its school councils that they have to hold at least three meetings a year so as to comply with the minimum requirement under Regulation 14 of the ESF; and</p> <p>(b) encourage the councils of all ESF schools to hold more meetings than the minimum requirement under Regulation 14 of the ESF if this will help them better fulfil their roles and responsibilities.</p>	<p>(Page 18 – Item 2.30) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) it will issue letters to school councils reminding them of the minimum requirement for meetings; and</p> <p>(b) it will encourage school councils to meet six times a year and to set up sub-committees to help fulfil their roles and responsibilities.</p>	<p>A letter will be sent by 31 January 2005 to School Councils/Councilors to request implementation of these recommendations.</p> <p>In addition, the recommendations will be incorporated in the revision of the booklet "Guidance for School Councilors". After consultation with stakeholder groups, the revised guidance will be effective by 30 June 2005.</p>
<p>(Page 19 – Item 2.33) Audit has recommended that the ESF should urge its schools to:</p>	<p>(Page 19 – Item 2.34) The ESF agrees with the audit recommendations. It has stated that declaration registers will be</p>	<p>Target : 20 January 2005.</p>

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<p>(a) establish proper procedures to require council members to declare any interest which might conflict with their roles; and</p> <p>(b) properly document (e.g. on a standard form or in the meeting minutes) the declarations of conflict of interest made by council members.</p>	<p>prepared to record the interests of school council members.</p>	
<p>Part 3 : Strategic Planning (Page 23 – Item 3.8) Audit has recommended that the ESF should require its schools which had not widely consulted their stakeholders in the school planning process to:</p> <p>(a) seek the participation of various stakeholders, especially their councils, in the development of their plans; and</p> <p>(b) share their development plans as widely as possible with the stakeholders with a view to gaining the stakeholders' support.</p>	<p>(Page 23 – Item 3.9) The ESF agrees with the audit recommendations. It has stated that guidance on school development planning will be produced by a working group to assist schools in the planning process.</p>	<p>Actioned : in draft Education Development Plan (issued 7 January 2005).</p>
<p>(Page 25 – Item 3.15) Audit has recommended that the ESF should:</p> <p>(a) require its schools to produce a longer-term development plan (covering say, three to five years) which incorporates detailed short-term action plans; and</p> <p>(b) consider adopting a uniform planning cycle for its development plan and those of its schools.</p>	<p>(Page 25 – Item 3.16) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) school development plans will be aligned with the ESF education development plan; and</p> <p>(b) the draft ESF education development plan has already, in its procedures, adopted a uniform planning cycle.</p>	<p>Actioned : in draft Education Development Plan (issued 7 January 2005). The Education Development Director will constitute a group to provide guidance by 30 June 2005.</p>

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<p>(Page 28 – Item 3.22) Audit has <i>recommended</i> that the ESF should issue good practice guides to its schools to help them ensure that all significant aspects of school activities are included in their development plans.</p>	<p>(Page 28 – Item 3.23) The ESF agrees with the audit recommendation.</p>	<p>The Education Development Director will contribute a group to provide guidance by 30 June 2005.</p>
<p>(Page 29 – Item 3.28) Audit has <i>recommended</i> that the ESF should require its schools which had not evaluated their programmes against their development plans to:</p> <p>(a) conduct evaluations so as to assess how well they have been performing; and</p> <p>(b) make use of the evaluation results to help plan future courses of action to further raise the standards achieved.</p>	<p>(Page 30 – Item 3.29) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) a revised evaluation strategy was drafted in August 2004. Since then, procedures for performing school reviews have been written to ensure that schools conduct evaluations of their programmes against their current development plans. These evaluations also examine the impact of school development plans on students' standards of achievement; and</p> <p>(b) it is ESF practice to draw up action plans through the process of school self-evaluations and school reviews. Examples of this can be found in three schools.</p>	<p>Actioned : in draft Education Development Plan (issued 7 January 2005).</p>
<p>(Page 32 – Item 3.33) Stakeholders' views help ensure continuous improvement of schools. For those schools which had not regularly sought the views of stakeholders regarding their needs and expectations, Audit has <i>recommended</i> that the ESF should request them:</p>	<p>(Page 32 – Item 3.34) The ESF agrees with the audit recommendations. It has stated that:</p>	<p>Actioned : in draft Education Development Plan (issued 7 January 2005).</p>

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<p>(a) to put in place such a system; and</p> <p>(b) to take appropriate action to further improve their performance, based on the feedback from their stakeholders.</p>	<p>(a) a revised self-evaluation strategy will be drafted to ensure that schools seek the views from stakeholders regarding their needs and expectations; and</p> <p>(b) with the revised self-evaluation strategy, schools will feed the views of the stakeholders into their school development plans. Much of this has already occurred, albeit without ESF-wide guidelines.</p>	
<p>Part 4: Budgeting and Cash Management (Page 36 – Item 4.7) Audit has recommended that the ESF should:</p> <p>(a) issue guidelines to assist its schools in developing formal procedures for budgetary planning and control; and</p> <p>(b) in preparing the guidelines, take into consideration the key procedures as outlined in the SAG.</p>	<p>(Page 36 – Item 4.8) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) although no uniform models may be possible because of the unique circumstances of each school, it will issue formal guidelines to assist schools in budgetary planning and control; and</p> <p>(b) all school councils will need a finance sub-committee to deal with budgetary matters.</p>	<p>The guidelines will be issued by 31 March 2003. In addition, the recommendations will be incorporated in the revision of the booklet “Guidance for School Councilors”.</p>
<p>(Page 38 – Item 4.12) Audit has recommended that the ESF should require its schools to:</p> <p>(a) project the financial resources required to implement individual programmes in their development plans; and</p> <p>(b) use the projections as a basis for compiling their annual budgets.</p>	<p>(Page 38 – Item 4.13) The ESF agrees with the audit recommendations. It has stated that all schools should be required to cost their development plans and use the cost projections in compiling annual budgets.</p>	<p>The guidelines will be issued by 31 March 2003. In addition, the recommendations will be incorporated in the revision of the booklet “Guidance for School Councilors”.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>(Page 40 – Item 4.18) Audit has recommended that the ESF should require its schools which do not have a bidding system for assessing the funding needs of their departments to adopt such a system for budget allocation purpose.</p>	<p>(Page 40 – Item 4.19) The ESF has stated that it will consider the audit recommendations, having regard to the fact that school councils and principals require a degree of independence to meet the unique circumstances of each school.</p>	<p>A letter will be sent by 31 January 2005 to School Councils/Councillors to request implementation of this recommendation.</p>
<p>(Page 41 – Items 4.23 and 4.24) Audit has recommended that the ESF should urge its schools to:</p> <p>(a) seek the approval of their councils for their annual school budgets (including subsequent major amendments); and</p> <p>(b) regularly submit to their councils financial reports showing the up-to-date position of variances between the approved budget and the expenditure commitments together with a forecast of the outturn to the end of the financial year.</p> <p>For those councils of its schools which have not played an active role in monitoring the use of school funds, Audit has recommended that the ESF should remind them to:</p> <p>(a) take the initiative to examine closely and approve their school annual budgets (including subsequent major amendments); and</p> <p>(b) monitor regularly the use of funds against the approved budgets and investigate significant variances.</p>	<p>(Page 41 – Item 4.25) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) the role of principals in school budgeting will be included in the revised guidance for school councils;</p> <p>(b) all schools will start to report regularly their financial performance to their councils in September 2005;</p> <p>(c) there is a need to revise the guidance to school councils on the approval of school budgets and ensure consistent implementation at schools;</p> <p>(d) monitoring the use of school funds against the approved budgets should be a regular agenda item in school council meetings; and</p> <p>(e) finance sub-committees may have to be set up in schools to help monitor the use of school funds.</p>	<p>A letter will be sent by 31 January 2005 to School Councils/Councillors to request implementation of these recommendations. In addition, the recommendations will be incorporated in the revision of the booklet "Guidance for School Councillors".</p>

RECOMMENDATIONS ON AUDIT REPORT
Chapter 5 – School Administration of the ESF

<p>(Page 44 – Item 4.32) Audit has recommended that the ESF should require:</p> <p>(a) its schools to record the commitments and actual expenditure in the relevant ledgers of the school accounting systems, so as to facilitate the school management and budget holders to better manage individual budgets;</p> <p>(b) budget holders of its schools to clearly specify, in budget requests, details of expenditure items and the amounts to be spent, so as to facilitate schools to monitor whether expenses have been incurred for the originally intended purposes; and</p>	<p>(Page 44 – Item 4.33) The ESF agrees with the audit recommendations stated in paragraph 4.32(a) and (b) and will remind schools of the best practice.</p>	<p>A letter will be sent by 31 January 2005 to School Councils/Councillors to request implementation of these recommendations.</p>
<p>(c) its schools to establish formal policies and control procedures on virements of funds between budgets including:</p> <p>(i) the circumstances under which virements are allowed; and</p> <p>(ii) agreeing with their councils on the limits of virement which, if exceeded, would require councils' approval.</p>	<p>As regards the audit recommendation in paragraph 4.32(c), the ESF has stated that:</p> <p>(a) it wishes school councils and principals to exercise control on virement issues, and to encourage such delegated leadership and authority to schools; and</p> <p>(b) principals have to report to school councils as a check and a balance.</p>	
<p>(Page 46 – Item 4.38) Audit has recommended that the ESF should:</p> <p>(a) require its schools to examine their need for retaining surplus funds;</p>	<p>(Page 46 – Item 4.39) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) it will discuss with schools the strategic use of any reserves. Schools will also have to report to councils their need for retaining surplus funds; and</p>	<p>Actioned : See Chapter 4, Item 3.16.</p>

RECOMMENDATIONS ON AUDIT REPORT
Chapter 5 – School Administration of the ESF

<p>(b) request its schools to consider placing their surplus funds with it to help reduce its overdraft, as an option of deploying the funds; and</p> <p>(c) agree with its school principals the arrangement for transferring surplus funds to the ESF.</p>	<p>(b) it accepts that improvement is necessary to reduce the high level of overdraft of the ESF. It will adopt either the audit recommendation of requesting its schools to place their surplus funds with the ESF, or another alternative arrangement under which there will be a central cash management and payment system similar to those used by large commercial organisations, thereby avoiding the need for a separate bank account for each school.</p>	<p>A letter will be sent by 31 January 2005 to School Councils/Councillors to request implementation of these recommendations. The need for training will be ascertained by 31 March 2005 and training provided by 30 June 2005. In addition, the recommendations will be incorporated in the revision of the booklet "Guidance for School Councillors".</p>
<p>(Page 48 – Item 4.44) Audit has recommended that the ESF should:</p> <p>(a) advise its schools to consider preparing and updating cash-flow projections to enable them to manage their cash more effectively;</p> <p>(b) help its schools prepare cash-flow projections, where necessary; and</p> <p>(c) ensure that its schools periodically compare the cash-flow projection with the actual cash flow with a view to identifying potential problems in financial operation.</p>	<p>(Page 48 – Item 4.45) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) training on cash-flow projections will be provided to school councils and administrative staff, where necessary; and</p> <p>(b) a finance sub-committee may have to be set up in each school to monitor the cash-flow position.</p>	<p>Annual update to be completed by 1 September 2005 and each subsequent September.</p>
<p>Part 5: Financial and Administrative Matters (Page 51 – Item 5.5) Audit has recommended that the ESF should:</p> <p>(a) regularly review its school circulars and administrative memoranda to ensure that the guidelines are kept up-to-date; and</p>	<p>(Page 51 – Item 5.6) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) all SCAM should be updated regularly. Its internal auditor is updating these circulars and memoranda; and</p>	<p>Annual update to be completed by 1 September 2005 and each subsequent September.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>(b) consider making use of the Internet for distributing the circulars and memoranda to schools.</p>	<p>(b) it will look to extending the use of the Internet to disseminate the guidelines and procedures.</p>	<p>All updated and new circulars/memoranda will be placed on the website as soon as they are approved.</p>
<p>(Page 54 – Item 5.14) Audit has recommended that the ESF should:</p> <p>(a) in conjunction with its schools, draw up proper internal control procedures, making reference to the SAG; and</p>	<p>(Page 54 – Item 5.15) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) the internal auditor has already started to update internal control procedures, with reference not only to the SAG but also to ESF practices and other sources. Besides working with schools, the internal auditor also works closely with the Headquarters management when drawing up such procedures; and</p>	<p>This is work-in-progress and procedures will be issued by 28 February 2005.</p>
<p>(b) regularly carry out internal audits of schools to ascertain whether the internal controls are operating effectively.</p>	<p>(b) the ESF plans to consider systematic auditing and to review the use of time in auditing.</p>	<p>This will be carried out under the supervision of the newly appointed Audit Committee.</p>
<p>(Page 59 – Item 5.25) Audit has recommended that the ESF should:</p> <p>(a) revise the structure of accounts of its schools so that all entertainment expenditure is charged to one single account to facilitate monitoring and control; and</p> <p>(b) consider the appropriateness of setting aside an annual sum to be spent by its schools on staff functions.</p>	<p>(Page 59 – Item 5.26) The ESF agrees with the audit recommendations. It has stated that it will consider the appropriateness of setting aside an annual sum to be spent on staff functions.</p>	<p>To be implemented by 1 April 2005.</p> <p>Executive Committee will consider a report on this subject in March 2005.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>(Page 61 – Item 5.31) Audit has recommended that the ESF should formulate a policy on the provision of staff welfare and benefits by its schools.</p>	<p>(Page 61 – Item 5.32) The ESF agrees with the audit recommendation.</p>	<p>Executive Committee will consider a report on this subject by 31 March 2005.</p>
<p>(Page 62 – Item 5.34) Audit has recommended that the ESF should require its schools to ensure that, in processing claims for reimbursement of travelling expenditure, the claimant submits receipts and details of journeys.</p>	<p>(Page 62 – Item 5.35) The ESF agrees with the audit recommendation and has stated that a policy is being implemented in this respect.</p>	<p>Actioned : letter issued on 7 January 2005.</p>
<p>(Page 64 – Item 5.38) Audit has recommended that the ESF should:</p> <p>(a) require its schools to critically review their spending patterns with a view to identifying expenditure areas which are not essential; and</p> <p>(b) require its schools, in the light of the review results, to economise on their expenditure.</p>	<p>(Page 64 – Item 5.39) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) it will review the spending patterns of schools; and</p> <p>(b) its schools will continue to carefully monitor their budgets.</p>	<p>These recommendations will be implemented through the revision of the booklet "Guidance for School Councilors". After consultation with stakeholder groups, the revised guidance will be effective by 30 June 2005.</p>
<p>(Page 68 – Item 5.46) Audit has recommended that the ESF should:</p> <p>(a) set a financial threshold for recording assets by its schools;</p> <p>(b) require its schools to promptly record assets with value above the set threshold in the asset registers upon acquisition; and</p>	<p>(Page 68 – Item 5.47) The ESF agrees with the audit recommendations and has stated that it will review the current policy.</p>	<p>Procedures already drafted and will be issued by 31 January 2005.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>(c) require its schools to have asset registers checked periodically by persons who are not involved in the custody of the assets.</p>		
<p>Part 6 : Procurement and Energy Management (Page 76 – Item 6.10) Audit has recommended that the ESF should:</p> <p>(a) draw up a set of clear and comprehensive procurement guidelines to help its schools procure goods and services at best prices, making reference to EMB guidelines to aided schools in Hong Kong;</p> <p>(b) periodically revise the procurement guidelines to ensure that they are up-to-date and complete;</p> <p>(c) require all its school staff involved in procurement (e.g. finance officers, bursars and department heads) to follow the procurement guidelines issued by the ESF unless it is impracticable to do so, and in such circumstances, record the reasons for not doing so; and</p> <p>(d) ask the internal auditor to monitor compliance with the procurement guidelines by its schools.</p>	<p>(Page 76 – Item 6.11) The ESF agrees with the audit recommendations and has stated that procurement guidelines based on those of the EMB have now been drafted.</p>	<p>Procedures already drafted and will be issued by 31 January 2005.</p>
<p>(Page 77 – Item 6.14) Audit has recommended that the ESF should require its schools to always properly document the quotations obtained so as to demonstrate that procurement has been made on a fair and</p>	<p>(Page 77 – Item 6.15) The ESF agrees with the audit recommendation and has stated that the requirement for its schools to properly document the quotations will be made mandatory.</p>	<p>This is included in the procedures referred to in response to Item 6.10 above.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>competitive basis.</p>		
<p>(Page 80 – Item 6.24) Audit has recommended that the ESF should:</p> <p>(a) identify items of goods and services which are cost-effective and practicable to acquire through bulk-purchase orders;</p> <p>(b) devise a mechanism to coordinate its schools' orders for goods and services in order to take advantage of bulk-purchase discounts; and</p> <p>(c) urge individual schools to always plan and coordinate the purchase requirements within the school and to take full advantage of bulk-purchase discounts for goods and services.</p>	<p>(Page 81 – Item 6.25) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) no central purchasing scheme is presently in place, but this practice is being implemented for purchase of high-value items, e.g. information and communication technology equipment;</p> <p>(b) the ESF will consider setting up a mechanism in the long run to coordinate the purchase of other goods and services of high volume and/or high value; and</p> <p>(c) it will urge individual schools to always plan and coordinate the purchasing requirements.</p>	<p>ESF will consult with stakeholders, particularly principals in order to determine possible changes in practice by 31 March 2005.</p>
<p>(Page 83 – Item 6.32) Audit has recommended that the ESF should require its schools to:</p> <p>(a) conduct cost-benefit analysis before entering into leasing agreements for or making outright purchases of school equipment; and</p> <p>(b) document the analysis to show how decisions for leasing or purchasing school equipment have been made.</p>	<p>(Page 83 – Item 6.33) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) the practice of conducting cost-benefit analysis is in existence; and</p> <p>(b) more guidance will be given on documenting the practice.</p>	<p>These recommendations will be implemented through the revision of the booklet "Guidance for School Councilors". After consultation with stakeholder groups, the revised guidance will be effective by 30 June 2005.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>(Page 88 – Item 6.47) Audit has recommended that the ESF should require its schools to:</p> <p>(a) select the most economical tariff available for their electricity accounts;</p> <p>(b) conduct an analysis to ascertain the kVA value of their electricity accounts so as to enable them to select the most economical tariff;</p> <p>(c) explore the possibility of combining the electricity accounts within schools to obtain a more economical tariff; and</p> <p>(d) regularly monitor the electricity consumption pattern to ensure that the most economical tariff is obtained.</p>	<p>(Page 88 – Item 6.48) The ESF agrees with the audit recommendations and has stated that Audit guidance on energy management is valuable.</p>	<p>(a) and (b). A desk study and discussions with the electricity companies has shown that the majority of schools would not benefit financially from transferring to a maximum demand tariff. Further analysis of one school is ongoing. It can only be completed in the summer term when the maximum kVA is registered during the hot season.</p> <p>(c). This has been examined previously and found to be uneconomical.</p> <p>(d). Actioned : Building Management Department are monitoring usage.</p>
<p>(Page 89 – Item 6.51) Audit has recommended that the ESF should:</p> <p>(a) disseminate the practices of energy saving measures implemented by some of its schools to other schools; and</p> <p>(b) regularly conduct reviews to identify new energy saving measures that can be adopted by its schools.</p>	<p>(Page 90 – Item 6.52) The ESF agrees with the audit recommendations.</p>	<p>Actioned. Three schools are being supported in the EMSD competition which runs from January to December 2005. Good practices identified from this work are being disseminated to the other schools from January to April 2005.</p> <p>Actioned : Building Management Department are monitoring energy savings.</p>
<p>Part 7. Human Resources Management (Page 93 – Item 7.9) Audit has recommended that the ESF should require its schools to document in an assessment form the assessment of an applicant showing his relative merits and the reasons for recommending or not recommending him for appointment.</p>	<p>(Page 93 – Item 7.10) The ESF agrees with the audit recommendation.</p>	<p>Actioned : Draft School Circular with detailed procedures has been prepared. This requires consultation with Academic Committee and is expected to be formally issued by 20 January 2005.</p>

RECOMMENDATIONS ON AUDIT REPORT
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<p>(Page 95 – Item 7.16) Audit has recommended that, before offering appointment to applicants for school posts, the ESF should require its schools to:</p> <p>(a) submit the assessment forms and other relevant records (e.g. résumé) of the applicants to their councils for review; and</p> <p>(b) request their councils to endorse the most suitable applicant for appointment.</p>	<p>(Page 95 – Item 7.17) The ESF generally agrees with the audit recommendations. It has stated that:</p> <p>(a) the tight time-frame for offering appointments sometimes makes it impossible to convene school council meetings. Therefore, authority is vested with the principals;</p> <p>(b) given the large number of applicants for many ESF posts, and the large number of posts which may be vacant in a large school, it is impractical to involve school councils in reviewing all applications in the necessary time-scale. However, it acknowledges the need for school councils' involvement in decisions on staff appointments; and</p> <p>(c) an option being considered is that an appointments sub-group of school council is established to ratify the appointments.</p>	<p>Actioned : Draft School Circular with detailed procedures has been prepared. This requires consultation with Academic Committee and is expected to be formally issued by 24 January 2005.</p>
<p>(Page 98 – Item 7.27) Audit has recommended that the ESF should:</p> <p>(a) set guidelines on the conduct of performance appraisal of different ranks of school staff; and</p> <p>(b) require its schools to:</p> <p>(i) set up a formal performance appraisal system based on the guidelines; and</p>	<p>(Page 99 – Item 7.28) The ESF agrees with the audit recommendations. It has stated that:</p> <p>(a) the guidelines on the conduct of performance appraisal will be established through the relevant committees of the Foundation; and</p> <p>(b) as regards the setting up of a formal performance appraisal system based on the guidelines and the conduct of regular performance appraisals of school staff, these are stated initiatives in the ESF's</p>	<p>Plans put into place to have comprehensive Performance Development Plans for all staff by September 2006.</p>

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<p>(ii) conduct regular performance appraisals of school staff.</p>	<p>Development Plan 2004-07 which will be processed through the relevant committees of the Foundation.</p>	<p>Implementation of this recommendation is dependent on the future introduction of the proposed Performance Development Plans for staff. (see Item 7.27).</p>
<p>(Page 99 – Item 7.32) Audit has recommended that the ESF should consider devising a mechanism for awarding salary increments to its staff.</p>	<p>(Page 99 – Item 7.33) The ESF agrees in principle with the audit recommendation and has stated that 74% of ESF staff are on the maximum incremental point.</p>	<p>To be reviewed by April 2005 for implementation by September 2005.</p>
<p>(Page 100 – Item 7.38) Audit has recommended that the ESF should:</p> <p>(a) ensure that candidates on its supply teacher list have met the requirements of the Education Ordinance on teacher registration so that they can be readily appointed as supply teachers;</p>	<p>(Page 101 – Item 7.39) The ESF generally agrees with the audit recommendations. It has stated that:</p> <p>(a) it regularly asks its supply teachers without registration to declare whether they are applying for the registration. Out of the 20 teachers who remained unregistered by June 2004 (when this audit was completed), 14 had declared that they were applying for the registration, 3 of whom had obtained it as of September 2004. Furthermore, 9 out of the 20 teachers without registration are no longer on the ESF's list of supply teachers of September 2004;</p>	<p>To be reviewed by April 2005 for implementation by September 2005.</p>
<p>(b) ascertain whether individual schools have appointed supply teachers contrary to the requirements of the Education Ordinance on teacher registration, and seek the advice of the Education and Manpower Bureau on whether covering approval needs to be obtained; and</p>	<p>(b) the establishment and utilisation of the supply teacher lists is now being reviewed. However, it has to be recognised that it takes some time to complete the teacher registration process; and</p>	<p>To be reviewed by April 2005 for implementation by September 2005.</p>
<p>(c) remind regularly its schools of the need to observe the requirements of the Education Ordinance on teacher registration in the appointment of supply</p>	<p>(c) when specialist subject teachers, who are in short supply, are required as cover, the needs of the school and its students may have to be considered as having priority.</p>	<p>To be reviewed by April 2005 for implementation by September 2005.</p>

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<p>teachers.</p>	<p>The ESF has insisted that the policy on the employment of only qualified teachers is strictly enforced. The ESF will give serious consideration to establishing a centrally administered supply teacher list, which enables not only the credentials of supply teachers to be verified, but also their quality to be ensured.</p>	
<p>Part 8 : Other Income and Support (Page 103 – Item 8.8) Audit has recommended that the ESF should:</p> <p>(a) request its schools to examine whether it is necessary to promote the availability of their premises and facilities for hiring by outsiders; and</p> <p>(b) regularly review the schedule of charges for hiring of school premises and facilities to ensure that the charges are appropriate.</p>	<p>(Page 103 – Item 8.9) The ESF generally agrees with the audit recommendations and has stated that schools' size, facilities and location have an impact on their letting income.</p>	<p>Actioned : This has been policy since the early 1990s; School Circular No.50 refers.</p> <p>The guidelines for hiring charges will be revised by 22 February 2005.</p>
<p>(Page 105 – Item 8.15) Audit has recommended that the ESF should encourage its schools to actively pursue the opportunities which are available to them from the QEF.</p>	<p>(Page 105 – Item 8.16) The ESF agrees to disseminate information about the QEF to its schools. It has stated that it has encouraged its schools to make QEF bids and will reiterate this in writing.</p>	<p>A letter will be sent to Principals by 31 January 2005.</p>
<p>(Page 106 – Item 8.21) Audit has recommended that the ESF should consider liaising with the EMB to disseminate the experiences and good practices of PTAs of ESF schools to the local education sector.</p>	<p>(Page 106 – Item 8.22) The ESF agrees with the audit recommendation.</p>	<p>Actioned : contact with EMB representative established on 7 January 2005.</p>



FAX TRANSMISSION

To: Ms. Dora Wei Fax No.:
Public Accounts Committee

From: John Bohan

Date: 11 January 2005

No. of pages: 1 (including this page)

Dear Ms. Wei,

The Director of Audit's Report on the results of value for money audits (Report No. 43)

**Chapter 4: Corporate governance and Headquarters administration
of the English Schools Foundation**

At yesterday's hearing, I referred to an Executive Committee minute of a meeting held on 23 June 2003. For the convenience of the members of Public Accounts Committee, a copy of that minute is attached.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive

/Encl.

c.c. Chairman, ESF



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14/F, Wu Chung House
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Wanchai, Hong Kong

18 January 2005

Clerk to the Committee
Public Accounts Committee
Legislative Council Secretariat
The Legislative Council
8 Jackson Road
Hong Kong

(Attn: Ms Dora Wai)

Dear Ms Wai

**The Director of Audit's Report on the
Results of Value for Money Audits (Report No. 43)**

**Chapter 4: Corporate Governance and Headquarters Administration
of the English Schools Foundation ("ESF")**

Thank you for your letter of 13 January 2005 addressed to Mrs Fanny Law, Permanent Secretary for Education and Manpower. As we are aware, the ESF Executive Committee ("ExCom") was briefed of the resignation of the former ESF Chief Executive, Mr Jonathan Harris, at the meeting of 27 June 2003. According to the minutes of that meeting (enclosed), no report was made on the terms of cessation.

Annex K to the strictly personal and confidential submission of the former ESF Chairman (our letter dated 11 January 2005 refers) contains the minutes of a special ExCom meeting held on 23 June 2003. Those minutes have not been provided to the ExCom members who attended the meeting. According to the minutes, the then ESF Chairman was authorized to deal with the termination of Mr Harris' employment. As we advised the Public Accounts Committee, we first became aware of the golden handshake for him through an anonymous letter issued to the press several months

教育統籌局與教育署已於二零零二年一月一日合併為新的教育統籌局。為免浪費，我們繼續使用舊文具存貨。

We are the new Education and Manpower Bureau formed by the merger of the old Bureau and the Education Department. To minimize waste, we are using our old stationery while stock lasts.

SERVING THE COMMUNITY

afterwards, and subsequently, through reading the relevant enclosures of the strictly personal and confidential submission received from the former ESF Chairman after he has resigned from the chairmanship. We understand that this golden handshake forms an integral part of the non-disclosure agreement between the ESF and its former Chief Executive.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'LAI YIU-KEI', written vertically and slightly curved.

(LAI Yiu-kei, Samson)
for Secretary for Education and Manpower

c.c. Chairman, English Schools Foundation
Acting Secretary and Chief Executive, English Schools Foundation
Secretary for Financial Services and the Treasury
Director of Audit

**Note by Clerk, PAC:*

An extract from the minutes of the ExCom meeting on 27 June 2003 attached.

**Extract from the minutes of
the ESF Executive Committee meeting
held on 27 June 2003**

X X X X X X X X

<u>Present:</u>	Mr. Jal Shroff Mr. Graham Macnaughton Mr. John Bohan Mr. Tim Hoffman Mr. Tony Tang Mr. David Reeves Mr. Gordon Lewis	Chairman Treasurer Acting Secretary and Chief Executive Chairman, Management Committee EMB's Representative Chairman, Staff Council Chairman, Academic Committee
<u>Apologies:</u>	Mr. John Shanahan Mr. Michael Haynes	Vice Chairman Chairman, JCFTA
<u>In attendance:</u>	Mr. John Tustin Mrs. Nancy Leung Mrs. Margaret Tang	Human Resources Director Executive Officer Minutes Secretary

The Chairman advised that Jonathan Harris, Secretary and Chief Executive, had resigned on 26 June 2003 with immediate effect under his terms of contract and John Bohan was confirmed as Acting Secretary and Chief Executive. John Bohan, thanked the Committee for its trust in appointing him Acting Secretary and Chief Executive. He stated that he would not be an applicant for the permanent position.

X X X X X X X X



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本署編號 Our Ref. : UB/PAC/ENG/43-4

Urgent By Fax

來件編號 Your Ref. : CB(3)/PAC/R43

21 January 2005

Clerk, Public Accounts Committee
(Attn: Ms Dora WAI)
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

[Fax No. 2537 1204]

Dear Ms Wai,

**The Director of Audit's Report on the
results of value for money audits (Report No. 43)**

**Chapter 4: Corporate governance and
Headquarters administration of the English Schools Foundation**

Thank you for your letter of 18 January 2005. As requested, I append below Audit observations and recommendations regarding the recent information provided by the former Chairman of the English Schools Foundation (ESF) relating to the extra payments made to three senior staff leaving the ESF referred to in paragraphs 4.29 to 4.34 of Chapter 4 of the Director of Audit's Report No. 43.

Staff A

As stated in paragraph 4.30 of the Audit Report, the extra payment made to Staff A upon his leaving the ESF had been approved by the Executive Committee of the Foundation. This approval was recorded in the Executive Committee's minutes of meeting. Audit considers this arrangement a good practice.

Staff B

As stated in paragraph 4.30 of the Audit Report, Audit could not find records of the Executive Committee's decisions regarding the extra payment made to Staff B upon his leaving the ESF. In his email of 17 January 2005, the former Chairman of the ESF commented that "The Secretary was wrong not to have this minuted at one of the Executive meetings". It is not clear whether this extra payment had been approved by the Executive Committee. Audit observations and recommendations on this case are stated in paragraphs 4.31 and 4.32 of the Audit Report respectively.

Staff C

As stated in paragraph 4.30 of the Audit Report, Audit could not find records of the Executive Committee's decisions regarding the extra payment made to Staff C upon his leaving the ESF. At the Public Accounts Committee's public hearing on 10 January 2005, the Acting Chief Executive of the ESF provided some new information relating to the departure of Staff C. In addition, the Secretary for Education and Manpower provided the Committee with some related information vide his letter of 11 January 2005. The salient points of this additional information included:

- (a) on 7 January 2005, the former Chairman of the ESF told the Acting Chief Executive of the ESF in a telephone conversation that the Executive Committee of the ESF met on 23 June 2003 before the cessation of Staff C's service;
- (b) according to the minutes of the Executive Committee meeting held on 23 June 2003 provided by the former Chairman of the ESF to the Acting Chief Executive of the ESF on 7 January 2005:
 - (i) the meeting was attended by seven members of the Executive Committee, including the Chairman, the Vice Chairman, the Treasurer, the Chairman of the Management Committee, the Education and Manpower Bureau (EMB)'s representative, the Chairman of the Staff Council, and the Chairman of the Academic Committee;
 - (ii) the meeting resolved that the employment of Staff C be terminated; and
 - (iii) the meeting also resolved that the former Chairman of the ESF be authorised to deal with such termination including but not limited to discussion with Staff C, giving the relevant notice, agreeing on the terms of cessation at the former Chairman's discretion and generally all such acts as would be necessary to effect the termination;
- (c) the minutes of the Executive Committee meeting held on 23 June 2003 had not been entered in the ESF's minute books. The Acting Chief Executive of the ESF said that this was the reason why Audit and he himself were not aware of this Executive Committee meeting; and

- (d) the former Chairman of the ESF told the Acting Chief Executive of the ESF that he had circulated the minutes of the meeting held on 23 June 2003 to all who attended the meeting.

In his letter of 18 January 2005 to the Committee, the Secretary for Education and Manpower said that:

- (a) the minutes of the Executive Committee meeting held on 23 June 2003 had not been provided to members who attended the meeting;
- (b) the EMB became aware of the extra payment made to Staff C when an anonymous letter was issued to the press several months after the departure of Staff C;
- (c) in February 2004, the former Chairman of the ESF included the minutes of the Executive Committee meeting held on 23 June 2003 as one of the enclosures in his submission to the EMB; and
- (d) according to the minutes of the Executive Committee meeting held on 27 June 2003, the former Chairman of the ESF advised the meeting that Staff C had resigned on 26 June 2003 with immediate effect. However, the terms of cessation of Staff C's service were not included in the minutes of meeting.

Audit considers it unacceptable that the minutes of the Executive Committee meeting held on 23 June 2003 have not been entered in the ESF's minute books. As stated in Regulation 2.3 of the Regulations of the English Schools Foundation:

"Minutes of the proceedings of every meeting of the Foundation, Executive Committee, Standing Committee, School Council or any committee shall be entered in a book kept for that purpose and after confirmation signed by the chairman of such meeting or of the following meeting, and shall when so entered and signed be prima facie evidence of the facts therein stated."

So far, there is no evidence which shows that the contents of the minutes of meeting held on 23 June 2003 provided by the former Chairman of the ESF were agreed by all members attending the meeting. Even if there is such evidence, Audit considers it unacceptable that:

- (a) the Executive Committee authorised the former Chairman of the ESF to agree with Staff C the terms of cessation at his discretion without seeking its final approval (see paragraph 4.31 of Chapter 4 of the Director of Audit's No. 43); and
- (b) the former Chairman of the ESF did not report at the subsequent Executive Committee meeting the extra payment made to Staff C.

In the light of the new Audit observations, in addition to Audit recommendations in paragraph 4.32 of Chapter 4 of the Director of Audit's Report No. 43, Audit recommends that the ESF should:

- (a) enter all minutes of Executive Committee meetings in its minute books; and
- (b) refrain from delegating to any person the authority to agree on the terms of cessation of a senior staff member without the final approval of the Executive Committee.

Yours sincerely,



(Patrick LEUNG)
for Director of Audit

c.c. Secretary for Education and Manpower
Permanent Secretary for Education and Manpower
Chairman, English Schools Foundation
Acting Secretary and Chief Executive, English Schools Foundation
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred WONG)

**Hearings of the Public Accounts Committee
Value-for-Money Audit on the English Schools Foundation**

Chapter Five: School Administration of the ESF

Speaking Notes for the SEM

Thank you Chairman.

2. I must start off my response by saying thank you to the Director of Audit and his team for their hard work in this comprehensive audit exercise. As we responded in the Report, the Audit findings would provide a useful reference to Government, the ESF, other stakeholders and the community at large in respect of the issues under study.
3. I shall also thank the ESF Chairman for initiating the suggestion of making the ESF an audited organization in March this year. By doing so, she is leading the ESF to take a big step forward. The ESF is moved closer to the level of transparency and accountability it should have delivered. We look forward to seeing continued and concerted effort of the ESF community towards this direction in the days ahead.
4. In an overall term, Government's policy is not to micro-manage any subvented organizations. As far as schools are concerned, we promote school-based management and would normally defer to the school management to administer their own school. The ESF enjoys the same autonomy in formulating its school policies as in the case of private international schools. Accordingly, we have not had any active participation in the business covered in Chapter Five of the Audit Report.
5. This notwithstanding, we find the Audit observations and recommendations generally sound. We urge the ESF to give due considerations to the Audit findings and put in place improvement measures as early as possible where appropriate. We also urge that proper checks and balances are made available within the ESF such that similar problems, if happened in future, could be identified at an earliest opportunity and rectified in the interests of the students.
6. Thank you.



1. Opening statement

We thank the Honourable Chairman and members of the PAC for the opportunity to give evidence in relation to the observations of the Director of Audit.

When the new members of the Executive Committee of the English Schools Foundation (ESF) took office in March of this year we were acutely aware of the many problems and deficiencies within the organization. In order to have a comprehensive understanding of the problems and demonstrate our resolve for reforms and accountability we invited the Director of Audit to conduct a Value for Money Audit. In addition we invited the Corruption Prevention Department of the ICAC to provide advice on ways to improve the ESF administrative process.

We thank the Director of Audit and his colleagues for conducting such a thorough study at such short notice and in such a narrow time frame.

Despite deficiencies relating to governance and management the schools within the ESF system have consistently provided high quality education. This evidenced by:

- **Examination results:** 99 percent of our students achieved pass levels in this year's GCE A-levels examinations with 40 percent of our entries achieving Grade As
- **University entrance:** In 2004-05, ninety five percent of our graduates have gained entrance to universities: 7% in Hong Kong, 43% in the UK, 20% in North America, and 30% in Canada, Australia and other countries. This is despite the fact that we are non-selective in our student intake provided the child can benefit from an English medium of instructions and the fact that 10% of our students have special educational needs.
- **Parent satisfaction:** An overwhelming majority of our parents express satisfaction with the teaching and learning experience of the their students.
- **Student satisfaction:** An overwhelming majority of our students enjoy going to school.

The larger question we need to address is: What does the HKSAR need? We respectfully submit that:

1. It needs to support a segment of its educational system that has consistently provided high quality affordable education in the English medium.
2. It needs to provide students with a learning environment that is multicultural and bilingual.
3. It needs to provide more opportunities for mainstreaming students with special needs.
4. It needs a curriculum that is based on investigative, "liberal" methods of teaching and learning and has international recognition.

To fulfil these needs the ESF is willing and able to work with the Education and Manpower Bureau (EMB) and the community at large to achieve better integration with local schools in terms of improving the standard of English, continuing professional development for teachers, training of student teachers and school leadership.



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1 February 2005

Ms. Miranda Hon
Public Accounts Committee
Legislative Council Building
6 Jackson Road
Central
Hong Kong

Dear Ms. Hon,

**The Director of Audit's Report on the
Results of value for money audits (Report No. 43)**

Chapter 5: School Administration of the English Schools Foundation (ESF)

Thank you for your letter of 24 January 2005. The actions referred to in your letter have all been achieved. The target dates and actual dates achieved are tabulated below using the same references as in your letter.

	<u>Subject</u>	<u>Target Date</u>	<u>Actual Date</u>
(a)	School Councils meetings	31 January 2005	31 January 2005
(b)	School Council members' personal interests and declaration registers	20 January 2005	31 January 2005
(c)	An alternative arrangement with bankers	20 January 2005	20 January 2005
(d)	Asset recording and checking	31 January 2005	31 January 2005
(e)	Procurement guidelines	31 January 2005	31 January 2005
(f)	Properly document the quotations	31 January 2005	31 January 2005
(g)	Assessment form to document the assessment of applicant for school posts	20 January 2005	9 January 2005
(h)	Appointment sub-groups in School Councils	24 January 2005	9 January 2005

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TO EXCELLENCE IN EDUCATION



I trust that this meets your requirements. A Chinese translation will follow.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive

c.c. Secretary for Education and Manpower
Permanent Secretary for Education and Manpower
Director of Audit



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20 December 2004

Ms. Miranda Hon
Public Accounts Committee
Legislative Council Building
8 Jackson Road
Central, Hong Kong

Dear Ms. Hon,

School Reviews and Inspections

Thank you for your letter of 16 December 2004 concerning the request by the Public Accounts Committee at the meeting held on 10 December 2004. I enclose a folder with the following contents.

1. A note written by ESF's Education Development Director explaining the ESF's three-tier approach to school evaluation.
2. The procedures governing the Review of ESF schools by the ESF's central Education Team.
3. Reports on Inspections/Reviews of the following schools.

(a)	Island School	(OFSTED)	Nov 2002
(b)	Cross Phase Survey	(OFSTED)	Nov 2002
(c)	Beacon Hill School (1&2)	(OFSTED)	Oct 2002 & Oct 2004
(d)	Quarry Bay School	(ESF review)	May 2004
(e)	King George V School	(ESF review)	Oct 2004
(f)	Kowloon Junior School	(ESF review)	Nov 2004
(g)	Sha Tin Junior School	(ESF review)	Nov 2004
(h)	Peak School	(ESF review)	Mar 2004
(i)	Clearwater Bay School	(ESF review)	May 2003

There are no Chinese translations of these reports. Following the discussion between my secretary and your colleague, Ms. Szeto, I understand that this is acceptable.

Yours faithfully,

John Bohan
Acting Chief Executive

/Encl.

c.c. Secretary for Education and Manpower
Permanent Secretary for Education and Manpower
Director of Audit

**Note by Clerk, PAC:*

Reports on Inspections/Reviews not attached.

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TO EXCELLENCE IN EDUCATION

To: John Bohan, Acting Secretary and Chief Executive

Re: School Review and Evaluation

The English Schools Foundation has three fold approach to school evaluation. We evaluate all institutions as well as commissioning surveys of educational quality across the Foundation. The three levels are as follows:

1. School Self-evaluation. Research suggests that the key to school improvement is robust and effective self-evaluation. All schools evaluate their performance in the following ways:

- systematic observation of teaching and learning;
- a scrutiny of students' work; and
- an analysis of test and assessment data

ESF has joined EMB in the Hong Kong Schools Self Evaluation Network (HKSSSEN) and one of our principals is on the project's Steering Group.

2. School Reviews

School reviews take place on a regular cycle (see attached procedures and sample reports). These reviews are led by myself and members of my Education team. All are qualified registered inspectors under Ofsted's authorisation. I was formerly a senior HMI (Her Majesty's Inspectors) of England, with oversight of about 6,000 schools. As with the EMB's system of inspections, these are internal but are rigorous. Last month, ESF and EMB agreed on a mutual exchange of evaluators on school inspections. ESF uses Ofsted's inspection criteria on school reviews.

3. External Inspections and Surveys

We commission external evaluations to ensure objectivity and to help us answer questions to which we need answers. Our emphasis is strengthening (1) and (2), thereby diminishing the need for external institutional inspections. Instead, we will commission external surveys of educational quality which will affect all our schools.

In the attached pack, I have enclosed external inspection reports of Island School, Beacon Hill School (and its reinspection) and a survey of cross-phase liaison between primary and secondary schools.

In the past, such inspections were commissioned from HMI and Ofsted, the recognised world leaders in this field. However, we now will go through a competitive tendering process. We are planning two external surveys in 2004-05, one on special educational needs (SEN) and one on the provision for students for whom English is an additional language to their mother tongue.

Please do not hesitate to contact me if you require any further information (granger@fmo.esf.edu.hk) or 93861870.

Graham Ranger, 17 December, 2004

Procedures Governing the Review of ESF Schools

Inspection and evaluation tell you about the quality and standards of a school – what it does well and what it does less well. Along with self-evaluation, it contributes to a school's ability to check on its work and helps guide further improvement.

Introduction

1. School reviews are an ongoing part of the evaluative or quality assurance work of the Foundation.
2. School reviews help to define clearly what a school is doing well and what it is doing less well (see above). This is part of the process of continuous school improvement. In the ESF, rigorous self-evaluation is our aim. Review helps to validate this.
3. Timing. A school review is a partnership between the school concerned and others on the review team. A review will take place:
 - ideally in the first or second term of the tenure of a newly appointed Principal, to help give that Principal and the School Council a clear view of the school's strengths and weaknesses;
 - every 3 years approximately, on a cycle; or
 - in exceptional circumstances, at the request of the Secretary and Chief Executive.

After discussion, the Principal/Chair of the School Council will be informed by letter (electronically sent) at least 3 weeks but not more than four weeks prior to the date of the review's commencement.

Before the review the following will take place:

- a briefing from the review team leader to the Chair of Council/School Principal/leadership team, and staff if the school wishes;
- the team leader of the review will publish the criteria and any proforma by which the quality of teaching and learning, leadership and management and standards of achievement will be judged;
- the Principal/Chair of Council, in partnership with the team leader, will brief the staff about the review; and
- the Principal will write a self-evaluation report and distribute this to the team leader. If the Principal is newly-appointed, initial observations will be shared and discussed.

During the review

- the team will be led by one of the Education Team of the Foundation;

- the team will usually comprise members of the Education Team, senior leader(s) from ESF schools and a representative from the school under review, usually a Deputy Principal;
- the school-based elements of the review will take place, wherever possible, within a single (Monday – Friday) working week. Duration will depend on the size of the school/size of the team;
- the evidence to inform judgements is gathered by:
 - lesson observations;
 - discussion with staff and students, Council Chair, parent representatives;
 - analysis of students’ work; and
 - scrutiny of documents, including a self-evaluation (provided by the Principal in advance of the review) and longitudinal assessment data.

Working Principles

- the review will aim to observe lessons of all staff present during the week;
- brief oral feedback will be given to teachers as soon as possible after a lesson has been observed;
- lessons are graded for the purpose of the main findings of the review. Details of individual lessons may be discussed with the Principal;
- school senior management team members who are not involved as team members are offered the opportunity to observe lessons jointly with members of the review team; and
- oral feedback is given to the Principal on a daily basis and emergent judgements are shared.

After the review

- oral feedback will be given to the Principal, Chair of Council and senior leadership team on the final school-based day of the review. The principal may then give brief oral feedback to the staff;
- oral feedback will be given to staff by the review team/principal within 5 working days of the end of the review;
- a draft report is sent to the Principal/Chair of School Council for discussion and any factual correction;
- a full written report is given to the Principal/Chair of Council within ten working days of the end of the review;
- a presentation and oral feedback are given to the School Council. A full written report is given to each member of the School Council;
- a full written report is provided for: the Secretary and Chief Executive; each member of the Education team; the Director of Human Resources; the Financial Controller; and
- the leader of the review team provides a summary of the report (2 sides of A4 maximum) to the FMT and the Executive Committee, copied to the Principal/Chair of Council.
- the school leadership prepares:
 - a summary report for parents, discussed first with the leader of the review team;

- a post-review action plan, addressing the key issues for development, incorporating this into the school development/improvement plan.
- the Education Team:
 - negotiates programmes of support with the school leadership;
 - continues to support and monitor the school's development;
 - in partnership with the Principal's self evaluation report, the CEO's representative on the Council gives regular feedback on the school's progress in implementing its plan of action.

NB

- Strengths and successes of schools will be disseminated to other schools in the Foundation, so that all will benefit.
- In the rare cases where a school is found to have significant weaknesses, monitoring will take place at least ½ termly.

The Academic Committee will act as a forum for the discussion/suggested amendment of the review process.

Graham Ranger, 5th October 2004



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4 January 2005

Ms. Dora Wai
Public Accounts Committee
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms. Wai,

Hearings of the Public Accounts Committee
Report No. 43 of the Director of Audit

Chapter 5: School Administration of
The English Schools Foundation

I am writing to clarify two matters which were raised at the hearing held on 10 December 2004.

1. One honourable member appeared to believe that I had been a member of the ESF Executive Committee for ten years. This is not correct. I became a member of the Executive Committee only when I was appointed Acting Secretary and Chief Executive. This appointment was approved at the Executive Committee meeting held on 27 June 2003. I will relinquish this Acting position (and therefore membership of the Executive Committee) on the arrival of the new Secretary and Chief Executive on 14 February 2005.
2. There was debate about EMB inspection of ESF schools. I suggested that EMB inspectors could participate in ESF school reviews. In fact, such an invitation to the Chief Inspector (EMB) had already been given by ESF's Education Development Director on the previous day, 9 December 2004, and accepted on the same date. The offer is a reciprocal one.

I would be grateful if this letter could be drawn to the attention of the members of the Public Accounts Committee. I will also provide a Chinese translation shortly should the Committee wish to include a copy of this document in the Report.

Yours sincerely,

John Bohan
Acting Secretary and Chief Executive

c.c. Secretary for Education and Manpower
Chairman, English Schools Foundation
Secretary for Financial Services and the Treasury
(Attn: Mr. Manfred Wong)
Director of Audit

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23 December 2004

Ms. Miranda Hon
Public Accounts Committee
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms. Hon,

**The Director of Audit's Report on the
results of value for money audits (Report No. 43)**

Thank you for your letter of 22 December 2004 concerning the ESF Audit Committee. This was approved at the Executive Committee meeting held on 23 November 2004.

I attach the paper considered by the Executive Committee which sets out the powers and duties of the Audit Committee.

With respect to the reporting line, the Audit Committee will report to the Executive Committee (see item 1.8 of the attachment). Audit Committee will also recommend to the Foundation the appointment or re-appointment of the external auditors (see item 1.4 of the attachment).

I trust that this meets your requirements.

Yours sincerely,

John Bohan
Acting Chief Executive

c.c. Secretary for Education and Manpower
Permanent Secretary for Education and Manpower
Director of Audit

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**EXECUTIVE COMMITTEE MEETING
ON 23 NOVEMBER 2004**

**FOR DISCUSSION AND DECISION
ON THE FORMATION OF AUDIT COMMITTEE**
(to be established by the Executive Committee)

I. POWERS AND DUTIES

1. To keep under review the effectiveness of the ESF's management, financial, risk management, and other internal control systems for ensuring accountability, probity, regularity, value for money, efficiency and economy.
2. For this purpose to examine the annual accounts and to monitor the implementation of approved recommendations of internal and external audit reports.
3. To monitor the scope and effectiveness of the work of the internal audit service, including its planning and operation of the work and results incorporated in its reports.
4. To recommend to the Foundation the appointment or re-appointment of the external auditors.
5. To consider with the external auditors the scope of their audit and subsequently the results thereof.
6. To consider any other audit related matters, including issues arising from reports of external bodies such as the Government's Audit Commission and the Public Accounts Committee of the Legislative Council.
7. To investigate such other matters as it deems necessary to ensure the compliance of the highest standards of corporate governance.
8. To report to the Executive Committee at least annually on the adequacy and effectiveness of the ESF's management and financial control systems.

II. MEMBERSHIP

1. The Chairman, to be appointed by the Executive Committee from amongst those lay members with audit, financial or accounting experience.
2. Two members, appointed by the Executive Committee.

III. OFFICERS IN ATTENDANCE

1. Acting Secretary and Chief Executive / Chief Executive
2. Financial Controller

15 Nov 2004

The Government of the Hong Kong Special Administrative Region

房屋及規劃地政局

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Housing, Planning and Lands
Bureau
Murray Building,
Garden Road, Hong Kong

本局檔號 Our Ref.

HPLB(CR)(P1) 1-160/08 Pt. 2

來函檔號 Your Ref.

CB(3)/PAC/R43

11 December 2004

(6 pages)

(By Post and Fax: 2537 1204)

Ms Miranda HON
Clerk to Public Accounts Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms Hon,

**The Director of Audit's Report on the
results of value for money audits (Report No. 43)**

Chapter 6: Grant of land at Discovery Bay and Yi Long Wan

At the Public Account Committee (PAC)'s public hearing held on 8 December 2004, Members made some comments on Part 2 of the captioned Audit Report. We would like to provide the following information to clarify the relevant matters -

The authority of the then Secretary for the New Territories (SNT) to execute the land grant in 1976

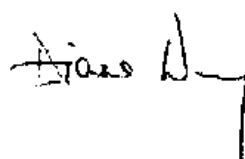
2. A Member cast doubt on the basis and authority of the land grant executed on 10 September 1976, on the ground that the development concept of Discovery Bay (DB) in 1976 already deviated from the concept plan approved by the Executive Council (ExCo) in 1973.

3. We wish to clarify that the ExCo Memorandum in December 1973 intended to seek approval-in-principle for the development project to proceed. In crystallizing the concept into the concrete proposal, the whole package was submitted to ExCo in July 1976, with a copy of the "Particulars and Conditions of Exchange" attached as an annex to the ExCo Memorandum. This annex, except for some very minor details on the lots to be surrendered and the dates in the original blanks to be subsequently inserted, was basically the same as the eventual "Particulars and Conditions of Exchange" signed between the then SNT and the developer on 10 September 1976 (see paragraph 2 above). ExCo noted the deviation from the 1973 concept, the safeguards in response to the request from ExCo in 1973, and most importantly the terms and conditions of the Conditions of Exchange. In brief, ExCo took the decisions in July 1976 on an informed basis. Therefore, the land grant was made by the then SNT in September 1976 with the full authority conferred by ExCo.

The authority of the then SNT to approve subsequent changes to the development

4. Under General Conditions Nos. 1 and 2, and Special Conditions Nos. 6, 7 and 19, the authority to approve the construction and demolition of buildings on the lot and to approve the Master Layout Plan rested with the then SNT. Extracts from the original copy of the Particulars and Conditions of Exchange are attached.

Yours sincerely,



(Miss Diane Wong)

for Secretary for Housing, Planning and Lands

c.c. D of L (Attn: Mr Patrick Lau 2868 4707
Mr Graham Ross
Mr C M Lau) 2850 5104

Internal - AA/SHPL

GENERAL CONDITIONS

1. The Grantee shall apply to the Secretary for the New Territories (in these Conditions hereinafter referred to as "the Secretary") for the lot to be set out on the ground. If the Grantee erects any building otherwise than in due accord with such setting out, he shall, when called upon by the Secretary, so to do, demolish such building and shall rebuild as directed by the Secretary. If the Grantee fails to demolish any building as aforesaid, it shall be lawful for the Secretary to have such building demolished, and the Grantee shall pay on demand the amount certified by the Secretary to be the cost of such demolition.

2. In the event of the demolition at any time during the tenancy of any building or structure erected on the lot or any part thereof after the date hereof the Grantee shall replace the same either by a sound and substantial building or structure of the same type and of no less volume or by a building of such type and value as shall be acceptable to and within such period as shall be specified by the Secretary.

3. (a) The boundaries of the lot shall be determined by the Secretary (whose decision shall be final) before the issue of the Crown Lease.

(b) The Grantee shall permit boundary stones properly cut and marked with the number of the lot to be fixed at each angle thereof and either in or on the land itself or in or on any building erected thereon as may be required by the Secretary, and shall pay the fees prescribed by him therefor as well as the prescribed fee for the re-fixing of such boundary stones which, through being lost, damaged or removed, need replacing.

4. Should it at any time be mutually agreed between the parties hereto that any portions of the roads within the lot are to be handed over to the Government, they shall be handed over free of cost.

5. The Grantee shall not permit sewage or refuse water to flow from the lot to any adjoining land or allow any decaying, noisome, noxious, excrementitious or other refuse matter to be deposited on any portion of the lot and shall see that all such matter is removed from the premises in a proper manner or treated and disposed of in such manner as the Director of Urban Services shall approve or require.

/6. The.....

(b) The Grantee shall in accordance with (a) of this Special Condition erect, maintain and keep in use on the lot membership club houses and a leisure resort and associated facilities which shall include an hotel or hotels, a dam, a reservoir, salt and fresh water storage and treatment areas, a sewage treatment plant, a refuse disposal plant, a cable-car system, a ferry pier and a non-membership golf course (in these Conditions called "the minimum associated facilities"). In addition to the minimum associated facilities but not in substitution therefor the Grantee may erect and operate such other facilities and structures as are or may be shown on the Master Layout Plan approved under Special Condition No. 6 hereof.

6. (a) Prior to the commencement of any work on the lot the Grantee shall submit for the prior approval of the Secretary within six months of the date of this Agreement a Master Layout Plan and Development Schedules (hereinafter together called "the Master Layout Plan") showing delineated and coloured thereon:

- (i) the positions of the roads proposed to be made;
- (ii) the general location and nature of the buildings proposed to be erected on the lot;
- (iii) all breakwaters, piers or other marine structures which it is proposed to erect; and
- (iv) the stages or phases by which it is proposed to develop the lot.

(b) In complying with Special Condition No.5 hereof the whole of the Lot shall be developed or redeveloped to the satisfaction of the Secretary in conformity and in accordance with the Master Layout Plan approved and signed by the Secretary who shall retain a copy thereof, and no alterations whatsoever shall be made by the Grantee to the Master Layout Plan or to the development or any redevelopment without the prior consent in writing of the Secretary, it being agreed that in the case of minor alterations such consent shall not be normally withheld.

(c) The Master Layout Plan and any plan amending the same signed by or on behalf of the Grantee and the Government shall be deposited and kept at District Land Office, Islands.

7. Subject to the obligations and restrictions regarding development mentioned in Special Conditions Nos. 5 and 6 and subject also to Special Conditions Nos. 59, 54(a) and 56, the lot or any part thereof, or any building or buildings erected or to be erected thereon shall not be used and the Grantee shall not permit or suffer the use thereof for any purpose other than for the purposes of the club houses, courses, leisure resort facilities and /the minimum....

the minimum associated facilities indicated on the Master Layout Plan, And such recreational, residential and commercial purposes and uses ancillary thereto as may be approved in writing by the Secretary, and in particular no building or part thereof erected or to be erected on the lot shall be used for any purpose other than the purpose for which it is designed and intended to be used as indicated on the Master Layout Plan and in the Occupation Permit issued in respect of such building by the Building Authority under the Buildings Ordinance.

8. (a) Subject to (b), (c) and (d) hereof the Grantee shall not except with the prior consent of the Secretary and in conformity with any conditions imposed by him (including the payment of such fee as may be required by him) -

- (i) assign, underlet, part with the possession of or otherwise dispose of the lot or any part thereof or any interest therein or any building or any part of any building thereon or enter into any agreement so to do, or
- (ii) mortgage or charge the lot or any part or parts thereof of any interest therein or any building or any part or parts of any building thereon except for the purpose of the development thereof and then only by way of a building mortgage or mortgages in such form and containing such provisions as the Secretary shall approve or require.

unless and until he shall have in all respects observed and complied with those Conditions to the satisfaction of the Secretary and then only subject to the provisions of Special Conditions Nos. 9 and 10 hereof.

(b) Notwithstanding anything to the contrary herein contained the Grantee (which expression shall, for the purpose of these Special Condition No.8(b) only, exclude its successor and assigns) may, after the date hereof but before the Grantee has in all respects observed and complied with these Conditions to the satisfaction of the Secretary and for the purpose of development of the lot but not otherwise, subject to the prior written consent of the Secretary and in conformity with any conditions imposed by him (including the payment of any fee as may be required by him), assign the whole of the lot or, subject also to Special Condition No.10 hereof, any part or parts thereof to the Grantee's subsidiary company or subsidiary companies. For the purpose of these Conditions "subsidiary company or subsidiary companies" shall mean only a company or companies of which the Grantee has effective control and not less than 51% of the issued shares in which at the time of such assignment or assignments are owned by the Grantee. The Grantee shall not at any time before he has in all respects observed and complied with these Conditions to the satisfaction of

/the Secretary ...

or their support in good and substantial repair and condition. In the event that as a result or arising out of any such formation, levelling or development any landslip, subsidence or falling away occurs at any time, whether in or from the adjacent hillside or banks and whether the same be Crown or leased land, or in or from the lot itself, the Grantee shall at his own expense reinstate and make good the same and shall indemnify the Government from and against all costs, charges, damages, demands and claims whatsoever which shall or may be made, suffered or incurred through or by reason of such landslip, subsidence or falling away. In addition to any other rights or remedies herein provided for breach of any of the conditions hereof the Secretary shall be entitled by a notice in writing to call upon the Grantee to carry out such construction and/or maintenance or to reinstate and make good any falling away, landslip or subsidence, and if the Grantee shall neglect or fail to comply with such notice within the period specified therein the Secretary may forthwith execute and carry out the work and the Grantee shall on demand repay to the Government the cost thereof.

17. (a) In the event of spoil or debris from the site or from other areas affected by any development of the lot being eroded and washed down on to public lanes or roads or into road-culverts, sewers, storm-water drains or nullahs or other Government properties, the Grantee shall be held responsible and shall pay to the Government on demand the cost of removal of the spoil and debris from or of damage to the public lanes or road-culverts, sewers, storm-water drains or nullahs or other Government properties. The Grantee shall indemnify the Government against all actions, claims and demands arising out of any damage or nuisance to private property caused by such erosion and washing down.

(b) No earth, debris, spoil of whatsoever nature, or building materials shall be dumped on any adjoining Crown land.

18. The Grantee shall pay to the Government on demand the cost of removing, diverting and reinstating elsewhere as may be required any footpaths, drains, sewers, nullahs, water courses, pipes, cables, wires, utility services or any other works or installations on the lot or on areas adjacent thereto which the Secretary may consider it necessary to remove, divert or reinstate upon any development thereof.

19. The design and disposition of any buildings to be erected on the lot shall be subject to the approval in writing of the Secretary, and the plot ratios of any building or buildings erected or to be erected on the lot shall be as specified in the approved Master Layout Plan.

/20.



地政總署
LANDS DEPARTMENT

電話 Tel: 2231 3088
 傳真 Fax: 2868 4707
 本署編號 Our Ref: LD 1/IS/PL/82 (TC) XX1
 來函編號 Your Ref: CB(3)/PAC/R43
 Email: dof1@landsd.gov.hk

8 January 2005

Legislative Council
 Legislative Council Building
 8 Jackson Road
 Central
 Hong Kong

(Attn : Ms Miranda HON)

Dear Ms Hon,

**The Director of Audit's Report on the
 results of value for money audits (Report No. 43)**

Chapter 6 : Grant of land at Discovery Bay and Yi Long Wan

I refer to your letter of 15th December 2004 and provide the requested additional information as follows :-

Public hearing on 8 December 2004

- (a) ***The government official(s) who drew up the lease conditions that were submitted to the Executive Council in July 1976 (paragraphs 2.7 and 2.8 of the Audit Report refer).***

We have no record as to how the lease conditions were drawn up or by whom.

- (b) ***In your opinion, whether or not the changes proposed in Master Layout Plan (MLP) 4.0 were changes to the basic concept of the Discovery Bay (DB) development (paragraphs 2.10 and 2.11 of the Audit Report refer).***

The resort concept was still a substantial element in MLP 4.0, but the introduction of "garden houses" appears to have introduced the likelihood

of permanent residence in a significant amount of the gross floor area (gfa). Although this did not conflict with the conditions of grant, there was a change.

- (c) *Minutes/records of the meeting(s) relating to the consideration of MLP 4.0 submitted by Developer A.*

The records of the meetings relating to the consideration of MLP 4.0 are :

- (i) Minutes of meetings held on 18.10.1977 (App. I)
- (ii) Notes of meeting held on 19.10.1977 (App. II)

Public hearing on 13 December 2004

- (d) *A copy of the letter dated 1 February 1983 from the Hong Kong Resort Company Limited referred to in the memo of the Registrar General (L.O.) dated 3 March 1983.*

Letter dated 1.2.1983 is at App. III

- (e) *A copy of the letter dated 25 November 1989 from the Director of Buildings and Lands to Developer A.*

Letter dated 25.11.1989 is at App. IV

- (f) *Whether, before the Secretary for City and New Territories Administration (SCNTA) approved MLP 5.0 which removed the requirement for the provision of the public golf course in February 1982, there had been inter-departmental discussions on the deletion of the golf course and, if so, records/minutes of the relevant discussions (paragraphs 3.5 to 3.11 of the Audit Report refer).*

There are no records of any inter-departmental discussions on the deletion of the non-membership golf course prior to the approval of MLP 5.0 in February 1982.

- (g) *Documents showing why the then Recreation and Culture Department welcomed the proposal that other recreational facilities would be provided in place of the public golf course (paragraph 3.8 of the Audit Report refers).*

There are no documents showing why the then Commissioner for Recreation & Culture (C for RC) welcomed the proposal that other

recreational facilities would be provided in place of the public golf course.

- (h) According to Table 3 in paragraph 4.16 of the Audit Report, the Lands Department (Lands D) had not charged premium for the changes made in the MLPs prior to 7 June 1994 (i.e. MLPs 3.5, 4.0, 5.0, 5.1, 5.2, 5.3, 5.4 and 5.5) although change in land use was involved and the area of housing accommodation was increased. (a) What the policy in the 1970s and 1980s on the charging of premium when approving change in land use was; (b) whether policy allowed the Lands D or the authority for land administration not to charge premium on change in land use when approving the MLPs; and (c) whether there had been cases in the 1980s in which premium was not charged on similar change in land use.**

The policy on changes of use requiring lease modifications has remained constant, in that where such a lease modification would bring about an increase in value, a premium is charged. In respect of changes in use involving only a change in MLP, however, it is apparent that in the 1970s and 80s no charge was made (as long as there was no increase in total gfa). There was no specific policy statement on this issue at that time. We have no record of premium being charged for an MLP change not involving a lease modification in the 1980s.

- (i) Whether the Lands D and the bureaux/department responsible for land administration in the 1970s and 1980s had the authority to charge premium when approving changes in MLPs 3.5, 4.0, 5.0, 5.1, 5.2, 5.3, 5.4 and 5.5 (paragraph 4.21 of the Audit Report refers).**

Authority was not lacking.

- (j) Whether or not it was normal practice in the 1970s and 1980s that premium would not be charged as long as the gross floor area of a site did not exceed a certain limit even though there was a change in land use.**

It was the normal practice not to charge premium for changes to MLPs which did not require a modification of the lease in 1970s and 80s as long as there was no increase in total gfa.

- (k) Whether, according to legal advice, the Administration may now amend the MLP in respect of the DISCOVERY BAY development to include in it the public golf course and the cable car system, given that these facilities are still provided in the lease conditions.**

The Administration cannot unilaterally amend the MLP.

- (l) *With reference to paragraph 4.24 of the Audit Report, how the Revenue Assessment Manual and the Lands Administration Office Instructions (LAOI) will be amended (please provide the English and Chinese wording of the amendments).*

Para 4.24 makes reference to the five recommendations in para 4.23 which have been dealt with by the following amendments to the LAOI, RAM and lease conditions as indicated.

- (a) *Specify the GFA, gross site area and other necessary requirements of the replacement public facilities of a development, before approving the deletion of facilities, especially public facilities, from an MLP.*

Add to LAOI as follows :-

“An MLP will normally show the layout of the site, the orientation of the buildings to be erected and a schedule showing the GFA and gross site area for each type of facilities to be provided. Where a revision is proposed, the revised MLP will show all of the new facilities to be provided. Any facilities to be deleted from a previous MLP must be shown by a separate schedule to be attached to the new MLP. This will enable tracking of changes in MLPs.”

- (b) *Keep a proper record of the approved replacement public facilities and use it to verify subsequently that the facilities have been built.*

Add to LAOI as follows :-

“All public facilities required under a lease or MLP should be provided within a time period to be prescribed. Proper records should be maintained of any approved replacement facilities and appropriate action must be taken to verify that the facilities are built within the specified time frame.”

- (c) *On approval of MLP changes, assess the premium implications of such changes and collect premium, if any and,*
- (e) *Clearly stipulate in the LAOI and RAM that the LandsD should charge premium and administrative fee, if any for approval of MLP changes.*

Revise LAOI and RAM as follows :-

“Approval

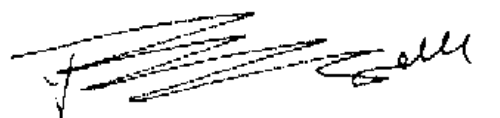
When giving approval to a Master Layout Plan, which leads to giving consent or variations of restrictions under certain *lease* conditions, the Director *will* impose *such* conditions (including payment of *an additional premium or consent fee* and appropriate admin. fee) as he considers appropriate. *As to whether a modification premium or consent fee is charged, this will depend on whether there is any enhancement of value.* When considering such approval, comments from relevant departments, e.g. Transport Department in respect of parking spaces, may be taken into account. Fee for such approval should normally be assessed on the same basis as lease modification and should be approved by Valuation Committee/Valuation Conference. (M 29 in LD TI 11/87/17(I))”

- (d) *In drawing up lease conditions, state explicitly in the conditions that premium will be charged on making changes to an approved MLP.*

Master Layout Plan Clause (c) to be amended as follows :

“The approved Master Layout Plans shall not be amended, varied, altered, modified or substituted without the prior written consent of the Director who may in granting such consent impose such conditions including payment of additional premium and no amendment, variation, alteration, modification or substitution of the approved Master Layout Plans shall be valid or binding on the Government or the Purchaser/Grantee unless a record thereof shall have been signed by the Director and the Purchaser/Grantee and deposited by the Purchaser/Grantee with the Director.”

Yours sincerely,



(J. S. Corrigan)
Director of Lands (Ag)

Encl.

cc - w/o encl
Secretary for Housing, Planning and Lands
Secretary for Financial Services and the Treasury
(Attn : Mr Manfred Wong)
Director of Audit
AA/SHPL

[ID: DiscoveryBay_Quert_080105]

Appendix I

Minutes of Discovery Bay Meeting
held at District Office, Islands
on 18.10.1977 at 10:00 a.m.

Present : Mr. P.A. Ward (Chairman) P.G.L.A., N.T.A.H.Q.
Mr. M. McGraw C.E.S./D., N.T.A.H.Q.
Mr. D.G. Dear S.E.S./S.D.(2), D.O. Islands
Mr. H.J. Walton-Masters (Secretary) E.S./Islands
Mr. LAM Ding-kwok A.D.O.L. (Lantau)
Mr. R.J. Clibborn-Dyer Planning & Research Division,
R.H.K.P.F.
Mr. J.F. Wilson Police Traffic H.Q.,
R.H.K.P.F.
Mr. Phillip Lau Senior Building Surveyor,
Building Ordinance Office
Mr. R.A. Wheatley Planning Group (P.G.)
Fire Services Dept.
Mr. HAU Hung-chi Planning Group (P.G.),
Fire Services Dept.
Mr. A.F.T. Chan C.F.O./M.T., T.P.O.
Mr. S.F. Lau Agricultural & Fisheries
Dept.
Mr. P.L. Leung Port Works Division, P.W.D.
Mr. Y.L. Chung Port Works Division, P.W.D.
Mr. J.H. Gould Marine Department

1. The meeting opened at 10:10 a.m. with an explanation of the layout area and the changes proposed. The proposed height of the buildings was mentioned in that there would appear to be no height restrictions. The principal change involves a large increase of residential units.

2. The question of height was again raised and it would seem that most of the high rise buildings will be in the Tai Pak area.

3. The whole concept seems to have been changed from a resort to a garden town. The changes do not, however, seem to be against the Lease Conditions.

Ferry Pier

4. Can the new location take fire boats? This is essential. Minimum depth 12 feet.

Cable Car

5. More information will be needed later about the cable car.

Fire Station

6. No problems at present.

Fire Requirements

7. Detailed talks required later. High rise could cause problems.

8. In general terms, the fire facilities would seem to be adequately provided subject to detailed plans.

Port Works

9. There will be a need to re-gazette Areas 8 and 18. No objection to change in emphasis.

Marine Department

10. Will be reply later.

Drainage Works

1. Purely technical points-gazetting required if sewer outfall changed. More details required later.

Agricultural & Fisheries

12. See reply. Seems to be a loss of open space. Area of most concern 2a, b & c (garden houses). Buildings should be kept low.

Police

13. No communication by land in and out of the area. Speed of access by emergency services could be a problem. Road system on site not too clear. Plans of road system required. Individual transport for garden houses? Types of vehicles. People - there all the time? Influx at weekends? Emergency plans? Police do not like it as the concept has changed. Vehicles will have to be licenced if the vehicles go where the public can go. All Police Points are subject to detailed plans.

14. Police presence will have to be increased. Premises to be owned by Government? Do not wish to be a private police force. Both Police and two stations need to be surrendered to Government. Proposed lease terms would seem to cover this point. More accommodation needed particularly at ferry pier. Berthing of police launch? Better helicopter site.

15. For Police Force and Fire Services Department, more details required at an early date.

Planning

16. Increase in number of units has far reaching planning implications. Recreation to housing. Planning against change of concept. No longer a leisure resort. Garden Houses - exact layout required. Is this good enough? Generally more details required before any approval even in principle required.

Water Supplies

17. No Government water supply.

18. No question of extending catchwater area.

19. Is there enough water for all these people?

Building Ordinance

20. No comment at this stage.

General Summary

21. Approval in principle cannot be given until more details are sent.

22. If detailed requirements can be met, then approval in principle will have to be given apart from Planning Reservations subject to Secretary for the New Territories' approval.

23. Planning Division and Police Force are against the revised concept due to the increase in population.

24. Developer to be asked to show how these extra houses and 35,000 people can be given water.

Distribution to :

S. for N.T. (2)
C. of Police (2)
C.B.S./N.T.(E)
D. of Fire Services (2)
C.F.O./N.T.
D. A. F.
C.E.F.W. (2)
D. of Marine
P.G.W.E./W.S.D.
C.E.D.W.
D.O.
S.E.S./S.D.(2)
A.D.O.L.(L.)

DESRIOT OFFICE, ISLANDS

19th October, 1977

Notes of Meeting concerning the
Discovery Bay Project held at
District Office, Islands on
Wednesday, 19th October 1977 at 2:30 p.m.

Present :

Government Officials

Mr. Victor C.H. Yung	(Chairman)	D.O. Islands
Mr. P.A. Ward		P.G.L.A., N.T.A.
Mr. M. McGraw		C.E.S./D.
Mr. D.G. Dear		S.E.S./S.D. (2)
Mr. H.J. Walton-Masters	(Secretary)	E.S./Islands
Mr. J. LAM Ding-kiok		A.D.O.L. (Lantau)

Hong Kong Resort Co. Ltd.

Mr. Payson M. Cha	Director of H.K. Resort Co. Ltd.
Mr. W.J. Reynolds	Estate Manager Central Enterprises
Mr. J. Marriott	Consultant
Mr. W. O'Neill	Project Director
Mr. R. Way	Chief Planner Lyon Associates (H.K.)

P.G.L.A. reported on S.N.T.'s initial comments which fall into 4 main headings :-

- (a) Serious reservations on the number of units.
- (b) Does not like the fact the emphasis has changed from lettings of rooms etc. to sales of residential units.
- (c) The staging would seem to indicate that the 'Resort project' are being constructed later.

.... / (d)

- (d) There is a much larger population than the original scheme and there could well be a residential population of 25,000 - 35,000 people. He feels that the recreational facilities have not been increased in proportion to this increase in population.

3. G.E.S./S.D.(2) then outlined the Government Departments' comments, a copy of which was circulated. C.E.S./D. made an additional point that B.O.O. would prefer to see plans showing individual house plots and some detailed plans of house types. This could help with speedier passing of plans later. This would be similar to the procedure adopted at Tai Sang Wai.

4. The following general points were made by the Government representatives :-

- (a) There was concern over the general management concept of the scheme. If the scheme turned into a town, Government would be left with management problems.
- (b) In the original scheme there was to be an internal managed vehicle scheme. It is understood that it will now be a mini bus and taxi service.
- (c) In the holiday flat part of the scheme would the developer retain and let any of the units.
- (d) The coastal area on which garden houses were shown was not considered a good point and Government would prefer to see these areas left unspoilt.
- (e) Minor layout plans would be useful although it was agreed this would be subject to change.

5. The Developers made the following points:-

- (a) The main Government points as outlined on the notes in paragraph 3 were mainly points of detail.
- (b) The security, police and emergency problems were ones that of which the developers were fully aware and would want to solve in a 'public' way in order to satisfy potential buyers.
- (c) There would always be an administrative presence in the area as the communal projects would be retained by the Company. The presence would tend to diminish, however, as time went on. There was some interest from Hotel Groups to manage some of the flats.
- (d) The population estimate of 35,000 would seem to be excessive.

.... / (s)

- (e) There is a need to define what type of population. Day visitors, week-end stayers and permanent visitors. It was noted that the Government would consider the scheme a 'resort' success if there was a large influx of people over the week-end. There was a switch in emphasis from an international resort to a Hong Kong resort.
- (f) When the details of the scheme were published more swimming pools and minor recreational facilities would become more apparent.
- (g) The approval of the Master Plan was an essential first stage before details could be considered.
- (h) The need to get on with the scheme was emphasised and time was a costly commodity for the developers. The new scheme designed to be more financially viable than the old scheme.

6. The Developers noted that the meeting with S.N.T. the following week was an important one and that S.N.T. would wish to be satisfied over the points made in paragraph 2 together with the water problem, heights of buildings, road-widths, protection of the coastal area and emergency services.

Non Master Plan Points

- 7. All the Tai Pak Lots have been acquired.
- 8. All houses have now had their roofs removed.
- 9. Lot 365 in D.D. 352 - Nothing on Crown Land around the houses.
- 10. Graves - This matter was now in hand.
- 11. An extension to include the village area and other lots is now required and the developer is to apply in writing.
- 12. The next progress meeting was arranged for 2:30 p.m. on Tuesday, 1st November 1977.
- 13. Mr. Merricot asked if he could keep a copy of the notes on the meeting on 18th October 1977 and was informed he could on a 'confidential - without prejudice basis'.
- 14. The meeting closed at about 4.00 p.m.

DISTRICT OFFICE, ISLANDS

20th October 1977

Hong Kong Resort Co. Limited

(Incorporated in Hong Kong)

Head Office: Rosty Building, 26th Floor 71 Des Voeux Road, Central Hong Kong Tel: 5-260362 & Cable: RESORTCO Telex: 65179 HKRCC/HK

February 1, 1983

Lands Department Headquarters
Murray Building
Garden Road
Hong Kong

Attn. Mr. J.R. Todd
Director of Lands

Dear Sir,

Discovery Bay - Conditions of Exchange

Further to our letter of 22 Nov. 1982 and following Mr. Marriott's meeting with Mr. Todd and Mr. Mills on 26 Jan. 1983, we write to confirm that we will shortly submit to you a schedule of the total we have expended on Phase I of the project. Each item of expenditure will be backed by an appropriate completion certificate and will be related to Master Plan 5.0. We will also submit a table comparing the number of completed housing units, GSA etc. with the Master Plan 5.0 table.

Simultaneously we will request the District Land Officer to grant us a partial certificate of compliance in respect of Phase I as now completed by us. Previously you wished us to supply an "as-built" Phase I Supplementary Master Plan but we now understand that this will not be necessary as the Phase I Supplementary Master Plan is regarded as having been superseded by Master Plan 5.0.

We would appreciate your confirmation that, once you are satisfied that we have spent not less than \$600 million and once a partial certificate of compliance has been granted, we will then be free under Special Condition 8(d) to assign other parts of the lot for development in accordance with the Conditions of Exchange.

Hong Kong Resort Co. Limited

(Incorporated in Hong Kong)

Head Office: Realty Building, 26th Floor 71 Des Voeux Road, Central Hong Kong Tel: 5-260361-8 Cable: RESORTCO Telex: 63179 HKACL HX

Lands Department Headquarters
Attn. Mr. J.R. Todd

Page 2

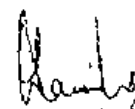
We would also like to place on record our understanding that:-

- (a) the Building Covenant (SC5(a)) will be deemed to have been completed, as regards both amounts and dates, once you are satisfied that we have spent not less than \$600 million. Thereafter we will still of course have to complete the full development within a reasonable period. The planned dates for the remaining stages will be indicated in our Phasing Plan which we will need to modify from time to time as circumstances change;
- (b) you see no need for the Conditions of Exchange to be formally amended to reflect the deletion of the non-membership golf course and the cable car system (already agreed), the refuse disposal plant (under consideration by government) and the hotel (apparently not yet agreed) from the minimum associated facilities in SC 5(b). Also you regard the lease plan as having been effectively superseded by Master Plan 5.0. We understand that, although our Conditions of Exchange were originally approved by the Executive Council, power to amend the Conditions has since been delegated to you.

With regard to (b) above, we would welcome from you in due course a formal letter confirming the amendments that have so far been agreed. We think this should be registered at the Land Office so that it can be inspected by any potential assignee who wishes to check on the position.

Reverting to the opening 3 paragraphs of this letter, it will inevitably take us a little time to assemble the necessary documents to submit to you before we can be free to assign under Special Condition 8(d). Since we are anxious to press ahead with all possible speed, we have asked Mr. William Kwan to submit to the Registrar General on our behalf an application under the Land Officer's Consent Scheme for the sale of Area 6B and a joint venture in respect of Area 6C.

Yours faithfully,
HONG KONG RESORT CO. LIMITED



Elaine Li

c.c. District Land Officer
Registrar General

EL/JCHM/mc

屋宇地政署總辦事處
香港花園道英利大廈



BUILDINGS AND LANDS DEPARTMENT
HEADQUARTERS
MURRAY BUILDING, GARDEN ROAD,
HONG KONG

電話 Tel: 5-8482004

Appendix IV

本署檔案 Our Ref: (20) in BLD 2/1/IS/PL/82(MLP) III

25 November 1989

來函編號 Your Ref: HKR/FR-7/L1631/89

Mr. Jeremy Marriott
Executive Director
Hong Kong Resort Company Limited
1st floor
Commercial Centre
Discovery Bay
Lantau
Hong Kong

Dear Mr. Marriott,

Lot 385 in B.D. 352
Discovery Bay, Lantau

Thank you for your letter dated 31 November 1989. I have noted your arguments which were the same points you raised at our last meeting. As a matter of fact, I have been taking up your points since the meeting and am now in a position to give you a definitive reply.

While you have been persistent in alleging that your revenue-earning gross floor area (GFA) should have been 613,155m² (6.6 million square feet), I have to hold to a different view.

There has been no conclusive evidence to show that your revenue-earning GFA ought to be 613,155m². In Tim Mills' letter of 14 April 1988 in reply to Roger Thompson's letter of 29 March 1988, the point about what should have been the agreed revenue-earning GFA at the outset has been made categorically clear. The Grantee agreed to pay a premium of \$61.5 million in return for an approved Master Plan 3.5 in which the GFA of 6.6 million square feet was shown to have included the GFA for Public Works, Fire and Police Station and the School. The net GFA permissible for housing, hotel and commercial (i.e. revenue-earning) was 6.38 million square feet. This was the deal which must have been struck after taken on board all pertinent considerations by both parties at the time. It would be inappropriate for me, nor for you, now to open up discussion and speculate how the deal had been agreed and why it should have been so agreed.

/2.....

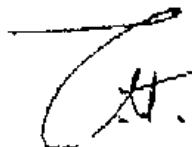
Although Master Plan 4.0 has showed an increase in revenue-earning GFA by the same amount originally set aside for the Public Works' GFA, the reason behind is still unclear. Whatever reasons one might attribute to the increase can only be conjectures. However, one thing is clearer on my records : this matter has been given a very detailed consideration and the Government stance is that 608,510m² should now be the permissible revenue-earning GFA for your Discovery Bay development and no more. Any attempt to increasing it, if justified and approved by Government, will attract additional premium.

You mentioned deduction of the estimated cost of building the police and fire stations from the original premium calculation. I confirm that this was the case. It proves, however, nothing but the fact that the land occupied by the buildings was intended to be non-revenue-earning. If it had been a revenue-earning site, the value of it should have been deducted from the premium as well, not just the cost of the building alone. The deduction therefore speaks for itself; that is, the intention was to reimburse you of the cost of the building which could have been considered more of the Government's obligation to provide such accommodation.

I have to dispute your statement that Government has set a precedent for adjusting the figures administratively in the case of MP 4.0, thereby giving you a stronger case to argue in favour of your recent application for inclusion of the school GFA into the revenue-earning GFA. As I said, the rationale behind such an adjustment is unknown and Government should not be bound by it for no convincing reasons. On the other hand, MP 4.0 has formed the basis by which you and Government have abided. MP 4.0 has now evolved to MP 5.4 and yet the revenue-earning GFA remains at 608,510m².

In short, your request for adjusting the present revenue-earning GFA to include the school GFA has to be rejected. I regret that I am unable to be of further assistance to you in this matter.

Yours faithfully,



(H.K. Ho)
for Director of Buildings & Lands

bcc DLO/Islands

香港特別行政區政府

The Government of the Hong Kong Special Administrative Region

房屋及規劃地政局

香港花園道美利大廈
電話 Tel: 2848 2266
傳真 Fax: 2845 3489Housing, Planning and Lands
Bureau
Murray Building,
Garden Road, Hong Kong

本局檔號 Our Ref. HPLB(CR)(PL) 1-160/08 Pt. 3

來函檔號 Your Ref. CB(3)/PAC/R43

10 January 2005

Ms Miranda HON
Clerk to Public Accounts Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road
Central
Hong Kong

Dear Ms Hon,

**The Director of Audit's Report on the
results of value for money audits (Report No. 43)**

Chapter 6: Grant of land at Discovery Bay (DB) and Yi Long Wan

Thank you for your letter of 15 December 2004 to the Secretary for Housing, Planning and Lands and I have been authorized to reply on his behalf.

The additional information requested by the Public Accounts Committee at the hearings is as follows :-

Public hearing on 8 December 2004

- (a) *minutes of the meetings relating to the decision that there was no need to report to the Executive Council regarding the change in the concept of the Discovery Bay (DB) development, including the minutes of the Development Progress Committee meetings held on 10 October 1985 and 14 November 1985 (paragraphs 2.17 to 2.21 of the Audit Report refer).*

The minutes of the Development Progress Committee meetings held on 10 October 1985 and 14 November 1985 are at Annexes A and B respectively. As far as we could ascertain, no other record of meeting is relevant to the point referred to in your question.

- (b) *a copy of the Executive Council paper of 11 March 2003 concerning the DB Outline Zoning Plan (paragraph 2.24 of the Audit Report refers).*

As a matter of principle, Executive Council (ExCo) papers are confidential documents and cannot be released. However, following the ExCo's approval on 11 March 2003, a Legislative Council (LegCo) Brief on "Approved Discovery Bay Outline Zoning Plan No. S/I-DB/2 was issued subsequently. A copy of the LegCo Brief is at Annex C.

Public hearing on 13 December 2004

- (c) *regarding the deletion of the public golf course, documents during the period July 1977 (when Developer A proposed to change the public golf course to some other form of public recreational use) and February 1982 (when the Secretary for City and New Territories Administration (SCNTA) approved MLP 5.0 which removed the requirement for the provision of the golf course) which were relevant to the SCNTA's decision to approve MLP 5.0 despite the objection to deleting the golf course (paragraphs 3.5 to 3.10 of the Audit Report refer).*

The Lands Department (Lands D) locates from its file records one document which might be relevant, namely an unsigned letter dated 20 March 1979 from Developer A to the then Secretary for the New Territories. The letter together with its enclosure is at Annex D. In the letter, Developer A explained why he/she considered a non-membership golf course not viable and sought approval to abandon the concept and to provide other active public recreation as replacement.

- (d) *whether, in the 1970s and 1980s, there was any project which, similar to the DB development, had undergone a change in development concept from that of an area with recreational and*

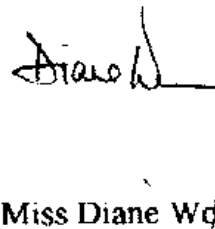
leisure facilities to a residential development, and whether there was any project in respect of which the application for change in development concept was not approved.

There was no other project for recreational and leisure facilities similar to that of the DB granted in 1970s and 1980s. Therefore, the question of whether change in development concept of such development had been approved or rejected does not arise.

(e) the total revenue generated by the entire DB development in the past 30 years.

As far as Lands D is concerned, a total of some \$2.09 billion has been collected in respect of the DB development. This figure comprises land premium, Government rent up to 1996/97 (Government rent is collected by the Rating and Valuation Department after 1997), premium charges for changes to the Master Layout Plan, waiver fees and rental for short term tenancy and administrative fees.

Yours sincerely,



(Miss Diane Wong)

for Secretary for Housing, Planning and Lands

c.c. D of L (Attn: Mr John Corrigan 2868 4707
Mr Graham Ross
Mr C M Lau) 2850 5104

Internal – AA/SHPL

CONFIRMED (14.11.85)

DEVELOPMENT PROGRESS COMMITTEE

Minutes of the 43rd Meeting held on 10 October 1985
in the L&W Branch Conference Room, Murray Building, 21/F

Present

Mr. J. Todd, SLW (Ag.) (Chairman)
Mr. F.D. Roome, DL (Ag.)
Mr. G.B.O'Rorke, DNTD
Dr. J.W. Hayes, RS(NT)
Mr. A.N. Savage, PAFS(1) for DFS
Mr. R.G. Scurfield, PAS(T)4 for S for T
Miss M. Seddon, AD(P)(Ag.) for D of H - Item 4
Mr. E.K.Y. Lee, Sr. Econ. for SES
Mr. R.J.S. Law, PEPO/N for CEP
Mr. K.T. Kuo, UADA

In Attendance

Mr. A.G. Eason, DS(LW)1
Mrs E. Wong, DS(LW)2
Mr. J.M. Wigglesworth, PGTP - Item 9
Mrs E.M. Boshier, PAS(LW)1
Mr. L.K.C. Wong, GTP/U
Mr. B.C.K. Fung, STP/NTDB
Mr. S. Lau, STP/SR3
Mr. Parrish Ng, AS(LD)
Mr. J. Figueiras, Consultant (MHA))
Mr. K. White, Consultant (MHA)) Item 1
Mr. J. Whitefield, Consultant (MHA))
Mr. R.B. Hanna, PM/TPF) Items 1, 5, 6 & 7
Mr. H.K. Chan, CTP/TPF)
Mr. K. Austin, PM/ST - Item 8
Mr. T.J. Mills, GLA/DH - Item 10
Mr. K.K. Tse, AS/LG (Secretary)

Item 10 : Discovery Bay Revised Master Plan
(DPC Paper No. 83/85)

- 10.1 Before introducing the Discovery Bay Revised Master Layout Plan, GLA/DH proposed two amendments to the paper : -

Para 7 : replace "Completion" by "Compliance".

Para 14 : delete the first sentence.

- 10.2 GLA/DH described the Discovery Bay Revised Master Layout Plan (No. 6.0) with which he said the developer, the Hong Kong Resort Co. Ltd, wanted to replace the current Master Layout Plan (No. 5.1) to improve the viability of the project. He pointed out that, in submitting the revised plan, the developer proposed to depart significantly from the original concept of a leisure and recreational facility to that of a 'first home' residential community. Under the new proposals some of the development originally proposed for the upland areas would be redistributed to the lowland areas, bringing it close to the commercial centre and the pier, in the form of 25 high rise blocks ranging from 14 to 22 storeys. Moreover, the Company wanted the original plan to have a public golf course and two hotels to be dropped, to regard the hotel requirement as optional and to convert the "surplus" commercial and hotel GFA to residential GFA on a metre for metre basis. GLA/DH also asked DPC to consider whether the revised proposals should be submitted to ExCo for endorsement as the latter had approved the Discovery Bay exchange grant in July 1976.

- 10.3 In discussion, the following main points were noted :

- (a) development concept : DS(LW)1 stated that as flat owners were free to use their flats either as first or holiday homes, the original resort concept could not be enforced. PAFS(1) suggested that there was no point in formally approving the change in concept since the change was already taking place;
- (b) location of the high rise buildings : Members were generally concerned about the compatibility of the proposed high rise residential development with the surrounding environment, especially on the headland, i.e. Area 4 (Phase IV development). The proposed buildings in Phase III, i.e. Areas 6E, 6B4, 6B2, were less objectionable because they would be situated against a backdrop of hills. The Chairman asked if the developer would want to commence work on Phase III without receiving the go-ahead for Phase IV. GLA/DH said that he probably would ;

- (c) community facilities : PGTP asked if there would be enough community facilities for the residents if the development concept changed. GLA/DH thought that there would be little requirement to provide additional community facilities as only a marginal increase in the planned population was involved. However, in view of the current emphasis on first homes, GLA/DH agreed that the developer should be asked to provide more public recreational facilities;
- (d) ferry service : it was noted that the inadequacy of the ferry service had long been a matter of complaint among the residents and was compounded by the fact that, while Government had insisted on the provision of full pier facilities at Discovery Bay, no corresponding provision in the harbour area had been made. PAS(T)4 said he would look into the problem;
- (e) consultation : RS(NT) suggested, and DPC accepted, that consultation should be carried out on a wider basis, especially with the residents. STP/NTDB said that although there was no town planning objection, in principle, to the transfer of residential CFA from the upland to the lowland areas, reservations had nonetheless been expressed over the location of the high-rise blocks from the town planning point of view;
- (f) implementation timing : GLA/DH said that the Company would like to implement the revised plan as soon as possible, and was therefore seeking approval urgently; and
- (g) approval : the Chairman said that CS's advice would be sought as to whether ExCo approval was required

10.4 DPC

agreed that

- (a) the requirement for building the public golf course and the cable car could be deleted and the developer asked to provide other compensatory public recreational facilities (e.g. tennis courts) ;
- (b) the requirement to build one or more hotels could be made optional rather than obligatory ;
- (c) the requirement to show the timing of the remaining stages or phases of development on the Master Layout Plan could be omitted ;
- (d) the proposal to change the overall concept of the development did not require formal approval as it was unenforceable in any case ;

- (e) the proposals in respect of Phase III of the development were acceptable in principle ; and
- (f) the proposals beyond Phase III, particularly as regards high rise development on the headland, were unacceptable.

Date of Next Meeting

14 November 1985.

Lands and Works Branch
October 1985

CONFIRMED (11.11.85)

DEVELOPMENT PROGRESS COMMITTEE

Minutes of the 44th Meeting held on 14 November 1985
in the L&W Branch Conference Room, Murray Building, 21/F.

Present

Mr. N.K. Chan, SLW (Chairman)
Mr. J.R. Todd, DL
Mr. K.W.K. Kwok, DNTD(Ag)
Mr. G. Leung, PAS(HK&K) for RS(HK&K)
Dr. J.W. Hayes, RS(NT)
Mr. C.K. Taylor, AFS(W) for DFS
Mr. J.A. Kessler, CE(T) for S for T
Mr. A.R. Crosby, AD(P) for D of H
Mr. E.K.Y. Lee, Sr. Econ. for SES
Mr. R.J.S. Law, PCPO/N for CEP
Mr. K.T. Kuo, UADA

In Attendance

Mr. A.G. Eason, DS(LW)1
Mrs E. Wong, DS(LW)2
Mr. J.M. Wigglesworth, PGTP - Item 5
Dr. Y.L. Choi, GE/OS
Mr. P. Ng, AS(LD)
Mr. R. Garrett, Consultant (Maunsell)) Item 1
Mr. C. Goodwin, Consultant (Maunsell))
Mr. R.B. Hanna, PM/TPF) Items 1-2
Mr. H.K. Chan, CTP/TPF)
Mr. I.T. Brownlee, STP/SA - Item 5
Mr. Y.Y. Ng, GE/NT) Item 6
Mr. B.C.K. Fung, STP/NTDB)
Mr. K.K. Tse, AS/LG (Secretary)

(Extract)

Item 4 Matters Arising

4.1 Clarification of meaning
 (Item 10 of minutes)

RS/NT explained that when he suggested consultation should be carried out on a wider basis in sub-para 10.3(e), he meant it should be carried out by the Company.

4.2 CS's advice on the Discovery Bay case
 (Item 10 of minutes)

 The Chairman reported that CS considered there was no need to go to ExCo or LDPC as the Phase III development followed on from the development so far approved and did not represent a major change in principle.

* * * * *

LEGISLATIVE COUNCIL BRIEF

**Town Planning Ordinance
(Chapter 131)**

**APPROVED DISCOVERY BAY
OUTLINE ZONING PLAN NO. S/I-DB/2**

INTRODUCTION

At the meeting of the Executive Council on 11 March 2003, the Council ADVISED and the Chief Executive ORDERED that the draft Discovery Bay Outline Zoning Plan (OZP) No. S/I-DB/1A should be approved under section 9(1)(a) of the Town Planning Ordinance (the Ordinance) and renumbered as No. S/I-DB/2.

BACKGROUND

2. On 16 May 2001, pursuant to section 3(1)(a) of the Ordinance, the Chief Executive directed the Board to prepare an OZP for the Discovery Bay area. On 14 September 2001, the draft Discovery Bay OZP No. S/I-DB/1 was exhibited for public inspection under section 5 of the Ordinance.

A 3. The approved Discovery Bay OZP No. S/I-DB/2 is at Annex A for Members' reference. A set of Notes, at Enclosure I to Annex A, lists out the uses which are always permitted and those which may be permitted on application to the Board. The Notes form a part of the approved OZP. An Explanatory Statement in respect of the approved OZP is at Enclosure II to Annex A.

The Planning Scheme Area

4. The Planning Scheme Area (the Area), covering about 810 hectares of land, is located in the eastern part of Lantau Island. It comprises the area mainly bounded by the proposed Lantau North (Extension) Country Park to its north, west and south, and Tai Pak Wan to its east. To the further east is Peng Chau and to the northeast about 4 kilometres away is the Hongkong Disneyland (under construction) in Penny's Bay. The boundary of the Area is shown in a heavy broken line on the approved OZP.

5. The population of the Area was about 15,600 in 2001. Having regard to the character of the Area, environmental considerations and the existing and planned infrastructure provision,

the approved OZP provides for a planned total population of about 25,000 persons for the Discovery Bay development and 200 persons in the rural settlements upon full development.

Land Use Zonings

6. The planning intention relating to the Area is primarily to conserve the natural setting of the Area and to allow for compatible low-density development which provides for a mix of residential and recreational uses. It adopts the urban design concept of maintaining a car-free and low-density environment while concentrating commercial and major community and open space facilities at more accessible locations. One activity node each around the ferry piers in Tai Pak Wan and Yi Pak Wan have been earmarked on the approved OZP. A stepped building height approach with low-rise on the headland and coastal lowland and high-rise development for the inland is adopted.

7. About 101 hectares of land are zoned "Residential (Group C)" ("R(C)") for low-density housing development compatible with the sub-urban character. This zoning covers the existing and proposed residential areas in the Discovery Bay development in Tai Pak and Yi Pak. This zone is sub-divided into 11 sub-areas with further sub-divisions to reflect the variations in height and building form in individual neighbourhood. Another seven hectares of land are zoned "Residential (Group D)" ("R(D)") to encourage improvement to and upgrading of existing temporary domestic structures and houses at Nim Shue Wan and Cheung Sha Lan. In this zone, very low-rise and low-density development may be permitted on application to the Board.

8. About 188 hectares of land are zoned "Other Specified Uses" for uses such as commercial complex cum residential development, hotel, golf course, marina, sports and recreation club, staff quarters, petrol filling station, service area and reservoir, etc.. Some 10 hectares of land are zoned "Government, Institution or Community" ("G/IC") to demarcate existing and reserved sites for major Government, institution or community facilities serving the needs of the local residents as well as visitors. Major existing Government, institution or community facilities include schools, a fire station/ambulance depot, post office, electricity sub-station, telephone exchange, pumping stations and the Trappist Haven Monastery. This zone is divided into four sub-areas, with variations in maximum height and/or Gross Floor Area (GFA) restrictions.

9. About 11 hectares of land are zoned "Open Space" ("O") to cover the existing beach in Tai Pak and the proposed central park and waterfront promenade at Yi Pak. The fringe areas in the central and southern parts are zoned "Green Belt" ("GB"), while the uplands in the west

and north are zoned "Conservation Area" ("CA") to define the limit of development and to protect the natural landscape. The two zones take up about 167 and 241 hectares respectively. The mangrove area at Yi Pak and the coastal areas at Tai Pak, Sam Pak and Sze Pak are zoned "Coastal Protection Area" to protect the natural coastlines and coastal features. This zone covers about 13 hectares.

10. Part of the proposed Lantau North (Extension) Country Park, about 63 hectares, is also included in the approved OZP and zoned "Country Park". All uses within this zone are subject to the provisions of the Country Parks Ordinance (Cap. 208).

11. In order to preserve the existing amenity and character of the Area and to avoid excessive development, development restrictions on building height, plot ratio and/or GFA are stipulated in the Notes for most of the land use zones.

Objections

12. During the exhibition of the draft Discovery Bay OZP No. S/I-DB/1, 674 valid objections were received, of which 41 objections were subsequently withdrawn. The objections were mainly against the "Other Specified Uses" annotated "Golf Course" ("OU(Golf Course)") zoning for the proposed second golf course site, the extent of the conservation-related zones, the non-adherence to the approved Master Plans under the lease, and the proposed 24-storey hotel and 25-storey developments in Yi Pak. In particular, there were conflicting views between two groups of objectors i.e. some residents of Discovery Bay and Green Lantau Association and the Hong Kong Resort Company Ltd. (HKR), the developer for the Discovery Bay development. The residents requested that the "OU(Golf Course)" site should be rezoned to "CA" to preserve the existing natural environment. The HKR, however, proposed to extend the "OU(Golf Course)" zone to the area zoned "CA" adjoining the existing service reservoir to help facilitate the linking up of the proposed and existing golf courses.

13. After giving consideration to the objections, the Board decided to propose amendments to the draft OZP to meet/partially meet some of the objections, including rezoning the "OU(Golf Course)" site to "CA" and "GB" zones because the site was not suitable for golf course use as development would displace a piece of natural environment and affect some natural streamcourse and some popular hiking trails, re-provisioning for the second golf course by rezoning a site zoned "R(C)12" and a small piece of adjacent land zoned "GB" to the north of the existing golf course to "Other Specified Uses" annotated "Golf Course cum Residential Development" ("OU(Golf Course cum Residential Development)")

to centralise the golf course facilities in one location, adjusting the boundary of certain zones and amending the Notes of the OZP.

14. On 14 June 2002, the proposed amendments were notified in the Gazette under section 6(7) of the Ordinance. 526 valid further objections were received and four of them were subsequently withdrawn. The further objections were all related to the proposed amendments to the second golf course. After considering the further objections under section 6(8) of the Ordinance on 19 July 2002, the Board decided to meet/partially meet some of the further objections by reverting part of the "OU(Golf Course cum Residential Development)" zone back to "GB" so as to avoid unnecessary cutting of natural slopes and extension of development area at a visually prominent upland location which would cause visual intrusion to the Hong Kong Disneyland. The proposed amendment was also confirmed by the Board as a decision made under section 6(9) of the Ordinance.

IMPLICATIONS OF THE PROPOSAL

15. Approval of the draft OZP itself has no financial or civil service implications.

Economic Implications

16. The further population increase in the Area will be about 9,400 mainly from the future phases of the Discovery Bay development in Yi Pak. There will be positive economic implications arising from the revenue generated from the premium collected from the private residential development, investment on the infrastructure work and jobs created.

Environmental Implications

17. The approved Discovery Bay OZP No. S/I-DB/2 provides the planning framework to guide future development and redevelopment of the Area. Appropriate planning controls have been adopted in the light of the environmental and infrastructural constraints in the Area.

Sustainability Implications

18. The approved OZP does not have major sustainability implications. It nevertheless strikes a balance between conserving the natural environment of the Discovery Bay area and providing compatible low-density development in a car-free environment.

PUBLIC CONSULTATION

19. Consultation with the Peng Chau/Discovery Bay Area Committee (the Area Committee) was conducted on 7 August 2001. Members of the Area Committee had no adverse comments on the draft Discovery Bay OZP but considered that private cars should be allowed to use the Discovery Bay Tunnel Link. The Board considered that the tunnel link should be restricted to the use of residents' services buses and emergency vehicles, taking into account the capacity constraint of the external road links of Lantau and the need to maintain the relatively car-free environment of the Discovery Bay development.

PUBLICITY

20. The approved Discovery Bay OZP will be printed and exhibited in accordance with section 9(5) of the Ordinance. A press release will be issued on the date of exhibition. A spokesman will be available for answering media enquiries.

ENQUIRY

21. Any enquiry on this brief can be addressed to Miss Ophelia Y.S. Wong, Assistant Director of Planning/Board, Planning Department, at Tel. No. 2231 4606.

PLANNING DEPARTMENT

March 2003

MARCH 20, 1979

Ref: F-222 P4

The Hon. D. Akers-Jones, OMG, JP
Secretary for the New Territories
New Territories Administration
4/F 15/F, H.K. Housing Authority HQ. Building
101, Princess Margaret Road
Kowloon.

Dear Mr. Akers-Jones.

Discovery Bay - Non-membership Golf Course

As you are aware we have now awarded a contract for the dam diversion tunnel to Aoki Construction Co, of Japan. We have awarded this contract initially because of delays in our negotiations with a third party known to you who is keen to participate. Whatever the state of these negotiations we propose to award by 1 June 79 the second major infrastructure contract which will provide serviced land for housing at Tai Pak. This will be followed or possibly accompanied by a contract for the dam.

We have taken advantage of this enforced lull to engage Messrs. Chankland Cox to review and refine Master Plan 4.0. One area on which the planners have focused is Area 16, Non-membership Golf Course. You will recall that Area 16 comprises some of the flattish land inland from Tai Pak through which access can be gained via a low saddle to a small beach at the northern extremity of our development area. Between Tai Pak and this small beach is a hill rising to over 100 ft.

Master Plan 3.5 showed a hotel on top of the hill, a public works area on the small beach and an 18 hole golf course plus 675 housing units in the remainder. The golf course itself occupied 47 acres. Master Plan 4.0 shows this entire area as Non-membership Golf Course.

We have considered the economics of such a golf course and have concluded that it is not viable. Even if it were viable, the users would be drawn exclusively from the higher-income brackets and relatively few people would make use of this large tract of land. I attach a paper which seeks to explain these points in more detail.

.....2/-

Page 2

March 20, 1979

The Hon. D. Akers-Jones, CMG, JP
New Territories Administration
Kowloon.

We acknowledge our responsibility to provide active recreation for the public, i.e. non Club members, at Discovery Bay but feel we could better discharge this responsibility by providing some form or forms of recreation other than golf. We are therefore writing to seek your approval in principle.

- (a) to abandon the concept of a Non-membership Golf Course and
- (b) instead to locate either in the same general area or elsewhere within the site a suitable area or areas for active public recreation.

Once we have your approval in principle we will consider the forms of active recreation that will be most suitable and will of course keep you advised on our thinking.

Yours sincerely,
HONG KONG RESORT CO. LIMITED

Rayson Cha
Managing Director

Encl:
YC/ph

Non-membership Golf Course

1. Conclusion

1.1 Economically, the non-membership golf course does not seem viable.

1.2 Various factors have been looked at. These are:

- a. the captive market.
- b. the cost of the game i.e. equipment etc.
- c. the operation cost and corresponding charges for players.

2. The Captive Market

2.1 There is a total of 2,500 - 3,000 golf members in Hong Kong, about 2,500 of whom belong to the Royal HK Golf Club and 300 belong to the Shek O Country and Golf Club. The 300 odd corporate memberships issued by the NMGSC were very popular and there is a waiting list of 50. The Shek O club gives priority to applicants who hold senior executive positions. These factors indicate several points:-

- 2.1.1 Only a very small percentage of the population is interested or even plays golf.
- 2.1.2 many enthusiastic golfers are white-collar executive workers, middle-upper income class.
- 2.1.3 Many companies, most probably those hiring expatriate personnel, would buy a nominee debenture for senior staff.

In toto, therefore, golf seems to be a "wealthy man's game", appealing to the higher income groups - a very small proportion of the "public".

3. The Cost to the Player

3.1 Golf clubs vary from HK\$600 per set of 7 to HK\$4000 per set of 14. For beginners, a set of 7 is sufficient and the cost, depending on the name brand, varies from HK\$600 - HK\$1500 per set.

3.2 Golf shoes is a must - minimum costing HK\$240 per pair.

3.3 New golf balls cost HK\$80 per dozen. (used HK\$36 per dozen)

3.4 Caddy and green fees charged vary from HK\$100 to HK\$200. This is a variable dependant on the management and maintenance costs of the course.

In total, using minimum figures, a person who wants to play golf without belonging to a club must spend roughly HK\$1000 for the equipment and HK\$100 each time for green fees. The weekend green fee for visitors is now HK\$150.

.....2/-

4. Cost of Operating the Golf Course

No estimate has yet been made for constructing a 18-hole course in Area 16 as shown on Master Plan 4.0 but obviously, because of the terrain, the capital outlay would be considerable.

Maintenance cost varies but roughly, depending on the configuration and quality of the course, the maintenance comes to about \$1 million per year for a 18-hole golf course plus its ancillary facilities.

Moreover, from the operations of numerous golf courses around the world, it has been shown that the maximum number of players using a 18-hole golf course per day is roughly 260. Assuming that there is a total of 90 - 100 public holidays per year (Sundays, public holidays and half day Saturdays) and assuming the weather for 45 - 50 days of this period is unsuitable for playing, the total number of the public served per year on such a non-membership golf course is only 11,700 to 13,000.

Not only does such a facility serve a small percentage of the public but also it is doubtful whether a non-membership golf course would be a viable economic enterprise. In order to recover both the capital and the recurrent costs, the green fees charged per person would be phenomenal bearing in mind the frequency of use is highest during weekends only.

MEMO

From	Registrar General (L.O.)	To	Government Land Agent (Disposal)
Ref. (46)	L.O. 40/1582/73 IV (NTS)	Your Ref. (174)	LND 1/IS/PL/82 IX
Tel. No.	5-95336	dated	28.2.83
Date	3rd March 1983		

Discovery Bay
Lot 385 in DD 352, Lantau

I have the following comments to make on the letter of the Hong Kong Resort Company Limited dated 1.2.83 :-

(a) Paragraph 3 (Page 1)

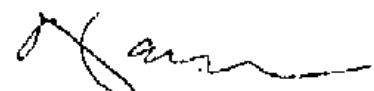
I agree that subject to Special Conditions 9 and 10 of New Grant No. 6122 if the Grantee shall have first satisfied you that not less than \$600 million have been spent on some parts of the lot in respect of which a partial certificate of compliance has been issued he may under Special Condition 8(d) assign other parts of the lot solely for the purpose of development in accordance with the Master Layout Plan and in compliance with the conditions in the New Grant.

(b) Paragraph 4(a) (Page 2)

I confirm that the company's understanding with regard to Special Condition 5(a) is correct.

(c) Paragraph 4(b) (Page 2)

If you have agreed that Master Plan 5.0 has superseded the original Master Plan and if Master Plan 5.0 does not show or refer to the non-membership golf course and the cable car system, I agree that there would be no need to modify New Grant No. 6122 so far as these two facilities are concerned. I also agree that the letter confirming the agreed amendments should be registered in the District Land Office, Islands.



(L.S. Shum)
p. Registrar General
(Land Officer)

LSS/is

Land Policy Meeting Paper LPM 3/87

For discussion on 25.5.87

File Ref: BLD 1/IS/PL/82 XI

Lot 385 in DD 352, Discovery Bay, Lantau

Recommendation

Members are asked to approve that the maximum permitted gross floor area for the residential, commercial and hotel areas be fixed at $613,155 \text{ m}^2$ and that the minimum gross floor areas for the public works and community facilities be those as shown in the present and proposed Master Layout Plan (MLP) No.5.3 as $24,875 \text{ m}^2$ and $18,040 \text{ m}^2$ respectively.

Background

2. The Conditions of Exchange dated 10 September 1976 states that 6,578,381.2 sq.ft. of agricultural land and 42,179.6 sq.ft. of building land totalling 6,620,560.8 sq.ft. be surrendered in exchange for the grant of 66,217,000 sq.ft. of Government land. These Conditions do not specify a maximum gross floor area permitted but refer to the development being in accordance with an approved Master Layout Plan. The basis of the exchange was basically 1:1 ratio in that the approved MLP No.3.5 permitted a gross floor area of 6.6 million sq.ft. ($613,155 \text{ m}^2$) which excluded the Recreational Areas but included $15,794 \text{ m}^2$ for Public Works; $1,858 \text{ m}^2$ for the Fire and Police Station and $2,787 \text{ m}^2$ for the school totalling $20,439 \text{ m}^2$. The residential, commercial and hotel gross floor areas totalled $592,716 \text{ m}^2$. (Option 1) In 1977, the first revision to MLP No.3.5 was approved as MLP No. 4.0 which showed 6,550,000 sq.ft. ($608,510 \text{ m}^2$) (Option 2) but wrongly converted this to $607,000 \text{ m}^2$ for the residential, commercial and hotel areas. Whilst the community facilities i.e. the school, fire and police station were included in the overall permitted gross floor area of 6.6 million sq.ft. ($613,155 \text{ m}^2$), the area devoted to Public Works ($15,794 \text{ m}^2$) was excluded and hence the increase in the residential, commercial and hotel areas by the same amount. Subsequent revisions of the MLP's in 1981 (MLP No.5), 1983 (MLP No.5.1), 1985 (MLP No.5.2) which is the current approved plan

showed the same amount of gross floor areas (wrongly converted as 607,000 m²) for the residential, commercial and hotel areas but showed an increase in the Public Works and community facilities to 42,915 m². Both these figures of 607,000 m² and 42,915 m² are also shown in the proposed MLP No.5.3 which is present under review.

Arguments

Three options are as follows:-

Option 1 - 592,716 m²

3. This figure represents the residential, commercial and hotel gross floor areas as contained in the original MLP No.3.5. However, the total gross floor area permitted of 613,155 m² (6.6 million sq.ft.) includes 20,439 m² devoted to public works and community facilities. The Hong Kong Resort Company submits that this is inequitable in that the whole of the 613,155 m² should apply to the residential, commercial and hotel areas as stated under Option 3.

Option 2 - 608,510 m²

4. This figure is shown wrongly on the currently approved MLP No.5.2 as 607,000 m² and is again shown on the proposed MLP No.5.3 presently under review. This figure of 607,000 m² originated from the first review of the original MLP No.3.5 and was approved in 1977 as MLP No.4.0, and has been shown in subsequent revisions of the MLP since. The correct figure of 608,510 m² represents an increase of 15,794 m² over Option 1 and is due wholly to the exclusion of the public works areas comprising a sewage treatment plant, storage yard, refuse disposal plant, ferry and service areas.

Option 3 - 613,155 m²

5. As mentioned above this figure represents the maximum permitted gross floor areas on the original MLP No.3.5 and formed the basis for the 1976 exchange. Whatever reasons there may have been in 1976 for requiring Hong Kong Resort Company to surrender land on a foot-for-foot basis in exchange for

gross floor areas which included 220,000 sq.ft. (15,794 m²) for public works and (4,645 m²) for community facilities, the Company submits that this is no longer equitable or appropriate in that the 6.6 million sq.ft. surrendered should now equate only to the residential, commercial and hotel areas. The Company further argues that MLP No.3.5, approved in 1976, considerably under-estimated the gross floor areas required for public works and community facilities when compared with the proposed MLP No.5.3 which gives an increase of 22,476 m² as the following table shows:

	<u>MLP 3.5</u>	<u>MLP 5.3</u>
Public Works/ transport	15,794 m ²	24,875 m ²
Fire and Police	1,858 m ²	2,860 m ² (as built)
School	2,787 m ²	15,180 m ² [1,954.8 m ² as built 891.8 m ² being built]
	<u>20,439 m²</u>	<u>42,915 m²</u>

This was partly because MLP No.3.5, with 1,750 hotel rooms and 2,675 condominium units, was slanted towards a resort concept and a second home. The present MLP No.5.2 and the proposed MLP No.5.3 is devoted largely to first homes for local people and this has greatly increased the requirement for public works and community facilities. For example, in MLP No.5.2 the Company has provided a 25,075 m² site for a school with 24 primary and 36 secondary classrooms - to date 11 classrooms have been built and 8 are about to be built in connection with Phase III. So far as the Fire and Police Station are concerned, not only the Company provide a bigger building, at Government's requirement, than was originally anticipated, but the cost was \$6.6 million as against the \$2.25 million which was allowed against the premium. The Company argues that the core infrastructure, already built at a cost of some \$700 million is able to support additional gross floor area and an increased population. The reservoir has a capacity of 750 million gallons and, once adjacent catchment areas are tapped, will be able to supply a population of over 30,000. The Company deemed it prudent to build a larger reservoir than that envisaged in MLP No.3.5, approved in 1976, which had a capacity of only

600 million gallons. The Company also planned the reconstituted Tai Pak Beach, the culverts and the drains to cope with the worst storm anticipated in 200 years, whereas this could have been planned for 25 years and periodic flooding would have had to be accepted. Part of this high infrastructure cost is attributable to Government's encouragement or insistence. For example, Government encouraged the enlargement of the reservoir and insisted upon a dual carriageway with a 24 ft. road reserve through the centre of the development. As so much money had to be spent "up front" on the infrastructure, the viability of the project depends upon its full utilisation.

Conclusion

6. Option 1 relates directly to the 1976 transaction and the original MLP No.3.5 whereby the public works and community facilities were included in the permitted gross floor area of 6.6 million sq.ft. (613,155 m²). This would be difficult to enforce now in view of MLP No.4.0 and its subsequent revisions and would obviously be strongly resisted by the Company.

7. Option 2 relates to MLP No.4.0 and its subsequent revisions whereby the public works areas of 15,794 m² were excluded from the overall permitted gross floor area of 6.6 million sq.ft. and reflects the present position shown on the current MLP No.5.2 (to be correctly converted from imperial to metric i.e. 6,550,000 sq.ft. = 608,510 m² not 607,000 m²).

8. Option 3 seeks to exclude the community facilities in addition to the public works areas in Option 2, from the overall permitted gross floor area of 6.6 million sq.ft. (613,155 m²). Whilst it must be recognised that in any development of this nature, there must be a certain amount of community facilities to be provided, and in this case there is a school plus Government facilities in the Fire and Police Station, it is arguable whether these should be accountable in the overall permitted gross floor area of 613,155 m² (6.6 million sq.ft.). However, the value of the increased gross floor area between Options 1 and 2 (4,645 m²) worth approximately \$11.6 million in premium terms is offset against the cost of constructing the increased school facilities alone of 12,393 m² (15,180 m² in MLP No.5.3 against 2,787 m² in MLP No. 3.5) which would cost over \$24 million excluding fitting-out costs.

9. Whichever of the options are now considered appropriate, given the history of this development, will be shown on the next revision of the MLP. This figure will then form the basis for future negotiations over the premium to be charged for any further increase in the permitted gross floor area. Any subsequent increases made in respect of the public works areas and community facilities will not then be a factor which needs to be taken into account, as has been the case with the recreational facilities. If the recommendation is agreed, then this could be reinforced by a modification of the Conditions of Exchange.

Buildings & Lands Department

May 1987

Submitted by PGLA/S - GLA/HK

DOCUMENT SUMMARY

Document Id: 1354L
Document Name: BLD 1/IS/PL/82 XI
Operator: pk
Author: TM/pk

Comments: L.385 DD 352 Dis.Bay

STATISTICS

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RevisedLand Policy Meeting

Minutes of Meeting held at 2.30 p.m. on Monday,
25 May 1987, in Buildings and Lands Department
Conference Room, 2nd Floor, Murray Building

Present:

Mr. CHAU Cham-son	-	DBL(Chairman)
Mr. SHUM Lap-shing	-	ARG
Mr. A.P. Asprey	-	DS(LW)
Mr. D.M. Scott-Will	-	PGLA(G)
Mr. F.D. Roome	-	PGLA(S)
Mrs. Rita Lau	-	PAS(NT) for RS(NT)
Mr. Frankie Lui	-	PAS(HK&K) for RS(HK&K)
Mr. G. Gately	-	AD/P (Secretary)

In Attendance:

Mr. M.J. Lewis	-	PAS(LW)
Mr. T.M. Mills	-	GLA/HK for Item III

I. Confirmation of Minutes of Last Meeting

In view of the large number of amendments proposed by DS/LW and PAS/LW, a revised set of Minutes is attached.

II. Matters Arising2. Item V - Resumption of Private Streets (LPM Paper No. 1/87)

PAS(HK&K) reported that he had written to S for T and understood that S for T's approval was now being sought for the preparation of draft drafting instructions on the proposed amending legislation.

3. Item VI - Petrol Filling Stations

The Secretary reported that copies of the information sheet on standards and locational factors for petrol filling stations had been obtained from the Town Planning Office and sent to PAS/LW and the other Members of the Meeting.

III. Lot 385 in DD 352 Discovery Bay (LPM Paper No. 3/87)
(BLD 1/IS/PL/82 XI)

4. At the request of PGLA/S, GLA/HK was invited to join the meeting for this item. The Chairman briefly explained the background to the case. The Discovery Bay project had originally been launched as a recreational resort development. Subsequent amendments to the original Master Plan had been dealt with by the NTA prior to the formation of Lands Department and the sum total now was that the Discovery Bay project represented a new town. There was little option but to accept all the previous amendments and recognize the updated version.

5. GLA/HK then briefed the meeting on the three options described in LPM Paper No. 3/87. This led to a lengthy discussion which indicated differing views on the best solution even within the Land Administration Office.

Action
PGLA/S

6. It was eventually agreed to adopt Option 2 with a permitted gross floor area of 608,510 m² which would form the basis for future negotiations over any premium to be charged for increases in GFA in future.

IV. Re-development Orders and Exclusion Orders (Draft ExCo Paper)
(BLD 1/HPY/58 III)

7. DS/LW referred the meeting to the LWB re-draft of an ExCo paper prepared and circulated by BLD. He queried the need for this submission now. He also felt that there were two policies in conflict. One policy encouraged comprehensive rather than piecemeal development whilst the other policy urged people to develop sites and not sit on them for speculative purposes.

8. PGLA/S said that the BLD drafts had been discussed and agreed by LAM and circulated accordingly. He felt that the paper had been held up for so long that it was no longer worth pursuing. It should be dropped and resurrected if need be.



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本署編號 Our Ref UB/PAC/ENG/43-3

1 February 2005

來函編號 Your Ref CB(3)/PAC/R43

Clerk, Public Accounts Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road, Central
Hong Kong
(Attn: Ms Miranda Hon)

Dear Ms Hon,

**The Director of Audit's Report on
the results of value for money audits (Report No. 43)
Chapter 6: Grant of land at Discovery Bay and Yi Long Wan**

Thank you for your letter of 26 January 2005 requesting for my comments on the Director of Lands' explanation in his letters dated 8 January 2005 and 25 January 2005 regarding paragraph 4.17 of the Audit Report, which stated that the Lands Department (Lands D) had not charged premium for the changes made in MLP 5.5 and earlier prior to 7 June 1994, and that the reasons for not assessing and/or charging premium for the changes in those Master Layout Plans (MLPs) were not documented. I set out my comments as follows:

- (a) *the reply to Question (j) on p.3 of the Acting Director of Lands' letter dated 8 January 2005 in which he stated that, "It was the normal practice not to charge premium for changes to MLPs which did not require a modification of the lease in 1970s and 80s as long as there was no increase in total gfa."*
- (i) *"Normal practice" not substantiated.* As far as could be ascertained from the Lands D's records, the acting Director of Lands' statement was not substantiated in either the Lands Administration Office Instructions or the Revenue Assessment Manual. Audit is not aware of any approval from the Executive Council (ExCo) for such "normal practice";
- (ii) *Increase in total GFA and change in user mix.* Audit would like to recapitulate the increase in total GFA and changes in user mix (mentioned in Note 3 in para. 2.8, para. 2.10 and Table 3 in para. 4.16 of the Audit Report), as follows:

User	MLP 3.5	MLP 4.0	MLP 4.0 increase/ (decrease) over MLP 3.5
	GFA (m ²)	GFA (m ²)	GFA (m ²)
(a) Housing accommodation	-	524,000	524,000
(b) Resort accommodation	401,342	-	(401,342)
(c) Hotel accommodation	140,284	32,000	(108,284)
(d) Commercial	51,097	45,000	(6,097)
(e) Others	41,341	40,600	(741)
Total GFA per MLP	634,064	641,600	7,536
Discrepancy (Note 2)			1,510
Increase in total GFA			9,046

} (Note 1)

Note 1: In April 1977, ExCo was informed of the GFA of the resort and hotel accommodation (para. 2.8 of the Audit Report refers).

Note 2: According to the Lands D, the discrepancy was due to a conversion error (from square feet to square metres).

As shown in the above table, the approval of MLP 4.0 in January 1978 had resulted in:

- an increase in total GFA over that approved in MLP 3.5; and
- a significant change in user mix, particularly the deletion of the resort accommodation and the addition of 524,000 square metres housing accommodation GFA (para. 2.10 of the Audit Report refers).

The then New Territories District Planning Division of the Town Planning Office also commented in mid-October 1977 that there was a corresponding increase of residential areas (para. 2.11 of the Audit Report refers);

- (iii) it is also relevant to point out that, while the then Secretary for the New Territories was delegated with the authority to approve changes to MLPs (para. 2.9 of the Audit Report refers), Audit is not aware that he had been given any explicit authority of not charging premium if there was enhancement in value arising from changes in lease conditions;

(iv) **Changes to MLP.** According to the Director of Lands' statement in the Public Accounts Committee (PAC) hearing held on 13 December 2004, the MLPs and the lease conditions of the Discovery Bay site had equal standing and effect (line 36 on page 17, and lines 5 to 7 on page 71 of the PAC Verbatim Report dated 13 December 2004 refer). Therefore, any modification of the MLP (such as the increase in the total GFA and the significant change in user mix in MLP 4.0 over MLP 3.5) would in substance tantamount to a modification of the lease conditions;

(v) **Deletion of public golf course and cable car system constituted lease modifications.** The provision of the public golf course and the cable car system was a mandatory requirement stipulated in **Special Condition 5(b) of the lease of the Discovery Bay development** (paras. 3.2, 3.6 Note 17, 3.16 and 3.20 of the Audit Report refer). Moreover, because of the importance attached to the public golf course proposal, the developer's responsibility to maintain the public golf course was more particularly referred to in **Special Condition 54(c) of the lease** (para. 3.6 and Note 17 of the Audit Report refers). In the circumstances, the deletion of:

- the public golf course in MLP 5.0 in February 1982 (by the then Secretary for City and New Territories Administration -- para. 3.7 of the Audit Report refers); and
- the cable car system in MLP 5.1 in February 1985 (by the Director of Lands — paras. 3.16 and 3.20 of the Audit Report refer)

constituted **modifications of the lease conditions.**

(vi) To conclude, as mentioned in para. 4.21 of the Audit Report, the Government might have suffered losses in revenue. The Lands D had not assessed the implications, financial or otherwise, of the deletion of the facilities, and the reasons for not assessing and/or charging premium for the changes in those MLPs were not documented (paras. 3.20 and 4.17 of the Audit Report refer);


(b) ***the Director of Lands' letter dated 25 January 2005***

- (i) According to Section 7 of Land Administration Policy on Modification and Administrative Fees (amended on 1 April 1984), as a general rule for lease modification, "Premium will normally be required representing the difference in value between the lot as formerly restricted and as modified..... The general principle relating to the assessment of modification premia is that the lessee must pay for any enhancement in the value of the lot deriving from the modification";
- (ii) in other words, premium assessment should be done by comparing the current land values under the modified lease conditions (and/or MLP) and the original lease conditions;

- (iii) having regard to the general rule in (b)(i) above, the unit land cost (accommodation value) and the valuation benchmark (i.e. ground floor shop value) adopted at the date of execution of the lease conditions are not relevant to the premium assessment of a lease modification at a later date (para. 3 of the Director of Lands' letter dated 25 January 2005 refers);
- (iv) in view of this, Audit does not concur with the Director of Lands' views that "adopting the highest use value among the mix in calculating the land premium to be paid by the developer upfront for the grant... had obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted GFA was not exceeded."; and
- (v) furthermore, as explained in para. a(ii) above, there had been an increase in total GFA and changes in user mix since the change from MLP 3.5 to MLP 4.0. Audit therefore also does not concur with the Director of Lands' view quoted in (b)(iv) above and his conclusion that he does "not consider it appropriate to compute the premium for each of the changes made to the MLP prior to 7 June 1994."

A Chinese translation of this letter will be forwarded to you shortly.

Yours sincerely,



(Peter K O Wong)
for Director of Audit

c.c. Secretary for Housing, Planning and Lands
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred Wong)
Director of Lands



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 來函檔號 *Your Ref:* CB(3)/PAC/R43

25 January 2005

Clerk
 Public Accounts Committee
 Legislative Council
 8 Jackson Road
 Central
 Hong Kong
 (Attn: Ms Miranda Hon)
 [Fax: 2537 1204]

Dear Ms Hon,

**The Director of Audit's Report on the
 results of value for money audits (Report No. 43)**

Chapter 6: Grant of land at Discovery Bay and Yi Long Wan

I write further to para. 2 of my letter of 24 January 2005 regarding the request of the PAC for information on the estimated amounts of premium involved in each of the changes made in the MLPs prior to 7 June 1994 based on the market conditions at the time when the changes were made (your letter of 2 December 2004 refers).

On the basis of file records, the original premium of \$61.5 million charged for the Discovery Bay development land exchange was based on an estimated sale price of \$300/ft² which was applied to the total GFA for all the

uses permitted (i.e. without distinguishing between commercial, residential and hotel). This valuation was supported by the analysis of the two public land auctions in Mui Wo conducted in 1973. These land auctions produced a ground floor shop value at about \$300/ft² and upper floor residential flat value at about \$200/ft² which we believe were adopted as the benchmark for valuing Discovery Bay at that time. Moreover, the unit land cost (commonly known as accommodation value (AV)) derived from the estimated sale price also compared favourably with that of two land exchanges in Mui Wo and Cheung Chau for hotel development in the early 1970s.

The application of \$300/ft² to the total GFA permitted under the approved MLP meant that the enhancement, if any, in subsequent changes to the MLP had already been captured in the approval of the first MLP by adopting the highest use value among the mix in calculating the land premium to be paid by the developer upfront for the grant. This had obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted GFA was not exceeded. That being the case, we do not consider it appropriate to compute the premium for each of the changes made to the MLP prior to 7 June 1994.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'P. Lau', written in a cursive style.

(Patrick Lau)

Director of Lands

c.c. Secretary for Housing, Planning and Lands
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred WONG)
Director of Audit



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16 February 2005

Ms Miranda Hon
 Clerk to PAC
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 Legislative Council Building
 8 Jackson Road
 Central
 Hong Kong
 [Fax: 2537 1204]

Dear Ms Hon,

**The Director of Audit's Report on the
 results of value for money audits (Report No. 43)**

Chapter 6: Grant of land at Discovery Bay and Yi Long Wan

Please refer to the Director of Audit's letter to you dated 1 February 2005 copied to me and others. While the concern of the Director of Audit is appreciated, it is incumbent on me to make sure that the issues involved are understood in the proper context. I write therefore to set the record straight and to facilitate consideration by the Public Accounts Committee in perspective.

2. To set the scene, I wish to set out the basic considerations underlying the handling of the Discovery Bay case in the seventies and eighties –

- (i) Since the subject land grant contained an MLP clause to enable the Administration to exercise detailed control over the implementation of the development within the approved parameters stipulated in the lease conditions, premium would not be charged on each and every occasion when amendments to the MLP were made, unless such changes would require lease modification and/or there was an increase in the total permitted GFA (for revenue generating purposes). This practice adopted for cases under similar situations in that period was also adopted in this case.
- (ii) How the premium for the land transaction concerned was calculated was explained in my letter dated 25 January 2005, namely the highest land use value among any of the permissible mix as specified in the MLP was adopted. This means that Government was able to capture the highest revenue income at the outset without any downside risk due to fluctuations in the property market. On the part of the developer, the certainty in his financial commitment under the land transaction plus the flexibility of being able to make more timely decisions in response to changes in market conditions would arguably be essential for a project of this magnitude and nature.
- (iii) On the above basis, as explained in my letter dated 25 January, 2005, this has obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted (revenue-generating) GFA was not exceeded.

3. I would now offer my more specific response to the Director of Audit's comments, as follows:

Audit's Comments	Our Response
(a) <i>the reply to Question (j) on p.3 of the Acting Director of Lands' letter</i>	Our response as provided, is factual to the best of our knowledge. It should be

dated 8 January 2005 in which he states that, "It was the normal practice not to charge premium for changes to MLPs which did not require a modification of the lease in 1970s and 80s as long as there was no increase in total GFA."

(i) "Normal practice" not substantiated. As far as could be ascertained from the Lands D's records, the acting Director of Lands' statement was not substantiated in either the Lands Administration Office Instructions or the Revenue Assessment Manual. Audit is not aware of any approval from the Executive Council (ExCo) for such "normal practice";

appreciated that most land administrative practices evolve over time in the light of experience and changes in circumstances and the Lands Department did not come into existence until 1982. Our understanding of the practice prevailing two to three decades ago should not be negated simply by the Director of Audit being unable to locate any written material to substantiate our statement.

(ii) Increase in total GFA and change in user mix. Audit would like to recapitulate the increase in total GFA and changes in user mix (mentioned in Note 3 in para 2.8, para 2.10 and Table 3 in para 4.16 of the Audit Report), as follows (see footnote on the next page):

It has to be re-emphasized that, despite the changes to the GFA in various MLPs up to MLP 5.5, the revenue - generating GFA did not exceed the permitted maximum of 608,510m² as determined by the Land Policy Meeting (LPM) held on 25 May 1987. Copies of the paper and the minutes of the LPM have been forwarded to the PAC at its second hearing on 13 December 2004.

<p>(iii) it is also relevant to point out that, while the then Secretary for the New Territories was delegated with the authority to approve changes to MLPs (para 2.9 of the Audit Report refers), Audit is not aware that he had been given any explicit authority of not charging premium if there was enhancement in value arising from changes in lease conditions;</p>	<p>Please see paragraph 2 above. The last paragraph of my letter dated 25 January 2005 is relevant.</p>
<p>(iv) Changes to MLP. According to Director of Lands' statement in the Public Accounts Committee (PAC) hearing held on 13 December 2004, the MLPs and the lease conditions of the Discovery Bay site had equal standing and effect (line 36 on page 17, and lines 5 to 7 on page 71 of the PAC Verbatim Report dated 13 December 2004 refer). Therefore, any modification of the MLP (such as the increase in the total GFA and the significant change in user mix in MLP 4.0 over MLP 3.5) would in substance</p>	<p>Please see paragraph 2 above. My letter dated 25 January 2005 is also relevant.</p>

<p>tantamount to a modification of the lease conditions;</p>	
<p>(v) Deletion of public golf course and cable car system constituted lease modifications. The provision of the public golf course and the cable car system was a mandatory requirement stipulated in Special Condition 5(b) of the lease of the Discovery Bay development (paras 3.2, 3.6 Note 17, 3.16 and 3.20 of the Audit Report refer). Moreover, because of the importance attached to the public golf course proposal, the developer's responsibility to maintain the public golf course was more particularly referred to in Special Condition 54(c) of the lease (para 3.6 and Note 17 of the Audit Report refers). In the circumstances, the deletion of:</p> <ul style="list-style-type: none"> - the public golf course in MLP 5.0 in February 1982 (by the then Secretary for City and New Territories Administration – para 3.7 of the Audit Report 	<p>The deletion was dealt with by way of consent given under the MLP clause set out in SC 6 of the Conditions of Exchange which reads as follows : -</p> <p><i>".....the whole of the Lot shall be developed or redeveloped to the satisfaction of the Secretary in conformity and in accordance with the Master Layout Plan approved and signed by the Secretary who shall retain a copy thereof, and no alterations whatsoever shall be made by the Grantee to the Master Layout Plan or to the development or any redevelopment without the prior consent in writing of the Secretary....."</i></p> <p>The then Registrar General in 1983 had advised that there would be no need to modify the lease insofar as the deletion of the non-membership golf course and the cable car system were concerned. A copy of the advice has been forwarded to the PAC at its second hearing on 13 December 2004.</p>

<p>refers); and - the cable car system in MLP 5.1 in February 1985 (by the Director of Lands – paras 3.16 and 3.20 of the Audit Report refer).</p> <p>constituted modifications of the lease conditions.</p>	
<p>(vi) To conclude, as mentioned in para 4.21 of the Audit Report, the Government might have suffered losses in revenue. The Lands D had not assessed the implications, financial or otherwise, of the deletion of the facilities, and the reasons for not assessing and/or charging premium for the changes in those MLPs were not documented (paras 3.20 and 4.17 of the Audit Report refer)</p>	<p>As explained in my letter dated 25 January 2005 we do not consider that there might have been loss in revenue as suggested and the need to calculate such figures does not arise.</p>
<p>(b) The Director of Lands' letter dated 25 January 2005.</p> <p>(i) According to Section 7 of Land Administration Policy on Modification and Administrative Fees (amended on 1 April 1984), as a general rule for lease</p>	<p>S. 7 of LAP remains a valid rule for general application for assessing premium arising from lease modifications. The case in question is not inconsistent with s. 7 of LAP. As explained in my letter dated 25 January 2005 and set out above we do not concur with the Director of Audit's views that a series of further premiums should have been collected for changes in</p>

modification,
"Premium will normally be required representing the difference in value between the lot as formerly restricted and as modified The general principle relating to the assessment of modification premia is that the lessee must pay for any enhancement in the value of the lot deriving from the modification";

- (ii) in other words, premium assessment should be done by comparing the current land values under the modified lease conditions (and/or MLP) and the original lease conditions;
- (iii) having regard to the general rule in (b)(i) above, the unit land cost (accommodation value) and the valuation benchmark (i.e. ground floor shop value) adopted at the date of execution of the lease conditions are not relevant to the premium assessment of a lease modification at a later date (para 3 of the Director of Lands' letter dated 25 January 2005 refers);

the development mix, even though the revenue-generating GFA has not been exceeded and the types of uses are not beyond what were allowed in the conditions of exchange executed in 1976. Such suggestion fails to take account of the established facts of this case that the developer had already paid for such flexibility at the time of the original grant.

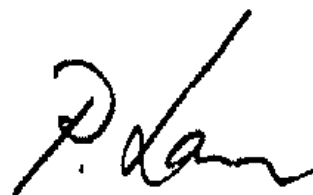
(iv) in view of this, Audit does not concur with the Director of Lands' views that "adopting the highest use value among the mix in calculating the land premium to be paid by the developer upfront for the grant ... had obviated the need for further premium assessment when changes in the development mix were subsequently made to the MLP as long as the total permitted GFA was not exceeded"; and

(v) furthermore, as explained in para a(ii) above, there had been an increase in total GFA and changes in user mix since the change from MLP 3.5 to MLP 4.0. Audit therefore also does not concur with the Director of Lands' view quoted in (b)(iv) above and his conclusion that he does "not consider it appropriate to compute the premium for each of the changes made to the MLP prior to 7 June 1994."

In conclusion, we strongly disagree with the views held by the Director of Audit in his letter of 1 February 2005 especially that "the Government might have suffered losses in revenue", having regard to the manner that the original premium was calculated. The Director of Audit's suggestion that a series of further premiums should have been collected for changes in the development mix up to 608,510m² (revenue-generating GFA) would constitute double charging since the facts established indicate that the developer, at the time of the original grant, had already paid for the flexibility of varying the development mix subsequently reflected in successive MLPs.

I should be grateful if the above comments would be taken into account in preparing and publishing the PAC's final report.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'P. Lau', written in a cursive style.

(Patrick Lau)

Director of Lands

c.c. Secretary for Housing, Planning and Lands
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred Wong)
Director of Audit



地政總署
LANDS DEPARTMENT

電話 Tel: 2231 3088
 傳文傳真 Fax: 2868 4707
 本署編號 Our Ref: LD 1/IS/PL/82 (TC) XXI
 來函編號 Your Ref: CB(3)/PAC/R43
 Email: dof1@landsd.gov.hk

8 January 2005

Legislative Council
 Legislative Council Building
 8 Jackson Road
 Central
 Hong Kong

(Attn : Ms Miranda Hon)

Dear Ms Hon,

**The Director of Audit's Report on the
 results of value for money audits (Report No. 43)**

Chapter 6 : Grant of land at Discovery Bay and Yi Long Wan

I refer to your letter of 17th December 2004 and as requested provide the following additional information :-

- (a) *It was mentioned at the hearing that the Lands Department (Lands D) had formulated measures regarding the setting out of boundaries of a government site before disposal of the site (paragraph 5.12(b)(i) of the Audit Report refers). What the details of the measures are.*

Sites for public auction or tender are normally fenced and their boundaries will be set out before sale. For sites granted by private treaty grant and extension, the plans in question include boundary dimensions and bearings, and the site area to facilitate the design of the development. The site boundaries will be set out on ground in advance or within 3 months after the completion of the land transaction so that the positions of the boundary marks can be shown to the landowner or his/her representative. Thereafter, it is the landowner's responsibility to protect the boundary marks placed on ground.

- (b) *A copy of the letter dated 10 August 1981 from Developer A to the District Office/Islands applying for a Short Term Tenancy (STT) for government land at Wong Chuk Long, which adjoins the western end of the south golf course at Discovery Bay (DB) (paragraph 5.14 of the Audit Report refers).***

Developer A's letter to DO/Is dated 10.8.1981 is attached at Appendix I.

- (c) *Whether the exclusion of the encroached government land at Wong Chuk Long from the boundary of the Lantau North (Extension) Country Park in 2001 was partly due to the fact that Developer A had repeatedly applied for a STT for the land (paragraph 5.20 of the Audit Report refers).***

LandsD's files do not contain any record showing the reason(s) for excluding the encroached government land at Wong Chuk Long from the boundary of the proposed Lantau North (Extension) Country Park in 2001. The assistance of Agriculture, Fisheries and Conservation Department and Planning Department is being sought in this regard.

- (d) *When the plan for the Lantau North Country Park extension was first proposed and finally approved.***

The draft plan in respect of the proposed Lantau North (Extension) Country Park was gazetted for public inspection on 13.7.2001. The draft plan has not yet been approved by the CE in Council.

- (e) *According to paragraph 5.15 of the Audit Report, Developer A said that the extension of the area for the golf course had been agreed in prior meetings with the Secretary for the New Territories (SNT). Whether there were records of those meetings; whether Lands D had ascertained with the SNT at that time the truthfulness of Developer A's claim of agreement with the SNT.***

LandsD's files do not contain any record of discussions between the then SNT and Developer A. Similarly we do not have any file record showing whether or not LandsD had ascertained with the then SNT the truthfulness of Developer A's claim of agreement.

- (f) *A copy of the paper of 29 July 2002 from the Lands D to the Legislative Council (paragraphs 5.23 and 5.24 of the Audit Report refer).***

D of L's letter to LegCo dated 29.7.2002 (with enclosures) is attached at Appendix II.

- (g) According to paragraph 5.33(a) of the Audit Report, the Lands D had not taken timely rectification action on the encroachments on government land at DB due to the fact that the DB development was still on-going. Whether this was a normal arrangement in the 1980s to address encroachment on government land, and whether there were cases in the 1980s which were handled in a similar manner.**

This approach was not the normal arrangement in the 1980s to address encroachment on government land.

- (h) The reasons why there was a provision concerning the rate of payment for any excess or deficiency in area of the site in the General Conditions of the lease conditions of the Yi Long Wan development, but not in those of the DB development (2nd inset under General Condition 5(a) in Appendix B of the Audit Report refers).**

The records of Master Lease conditions in LandsD show that between the grant of the lot at Yi Long Wan in 1975 and the Discovery Bay in 1976 there was a change in approach and the rate of payment condition was dropped.

- (i) The reasons for the different approaches in addressing the land encroachment problem at DB and Yi Long Wan although both developments were located in Lantau Island and developed in the same period.**

The golf course encroachment was (and remains) an unbuilt open area operated by a single entity. The grant of a STT was the appropriate means to regularize it. The circumstances of the encroachment at Yi Long Wan involving two privately owned residential blocks in multiple ownership constructed partially outside the lot are quite different from those of Discovery Bay and therefore warrant different treatment.

- (j) Regarding the amount of STT rent paid by Developer A (paragraph 5.26 of the Audit Report refers), the amount of rent originally proposed by the Lands D and the estimated amount of revenue that could have been generated by the encroached land if it had not been used by Developer A.**

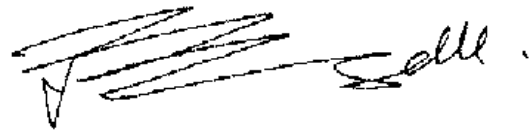
The negotiated rental of \$7.23M to cover the 21 year period from 27.10.1982 to 26.10.2003 was based on evidence of market transactions. The figure initially proposed in the negotiation by LandsD was \$11.2M for the same period.

The 3 encroached areas are remote and hard to access. The areas adjoining the encroached land at Wong Chuk Long are either steep sloping government land or private land owned by Developer A. As regards the other two encroached areas, they are largely sloping areas. We do not consider that they are capable of separate alienation or use by any party other than Developer A and as such no revenue would have been generated if they had not been used by Developer A.

- (k) *With reference to paragraph 5.24(c) of the Audit Report, the legal basis of the Lands D's view that "It could be argued that a form of tenancy had been in place".*

LandsD's view is based on the legal advice that the letter of 16.3.1983 created a relationship of landlord and tenant.

Yours sincerely,



(J. S. Corrigan)
Director of Lands (Ag)

c c Secretary for Housing, Planning and Lands	}	
Secretary for Financial Services and the Treasury	}	
(Attn : Mr Manfred Wong)	}	- w/o encl
Director of Audit	}	
AA/SHPL	}	

Encl

[DiscHay_Quest02]

Our Ref. P-3i/2393

District Officer
District Office, Islands
4/F International Building
Hong Kong

10th August 1981

Attention: Mr Bernard Chan

Dear Sir

PROPOSED TENANCY - WONG CHUK LONG

We wish to apply for a short term tenancy of the crown land coloured pink on the attached plan amounting to approximately 50,000 sq mtr. We require this land in order to ensure that a full 18 holes course is available for play by our projected opening date in the Autumn of 1982.

Variations in the building programme for the additional facilities in the Diana Farm area will mean that this area will not be completed in the time frame previously envisaged.

We trust that this request will meet with your favourable consideration and look forward to hearing from you in the near future.

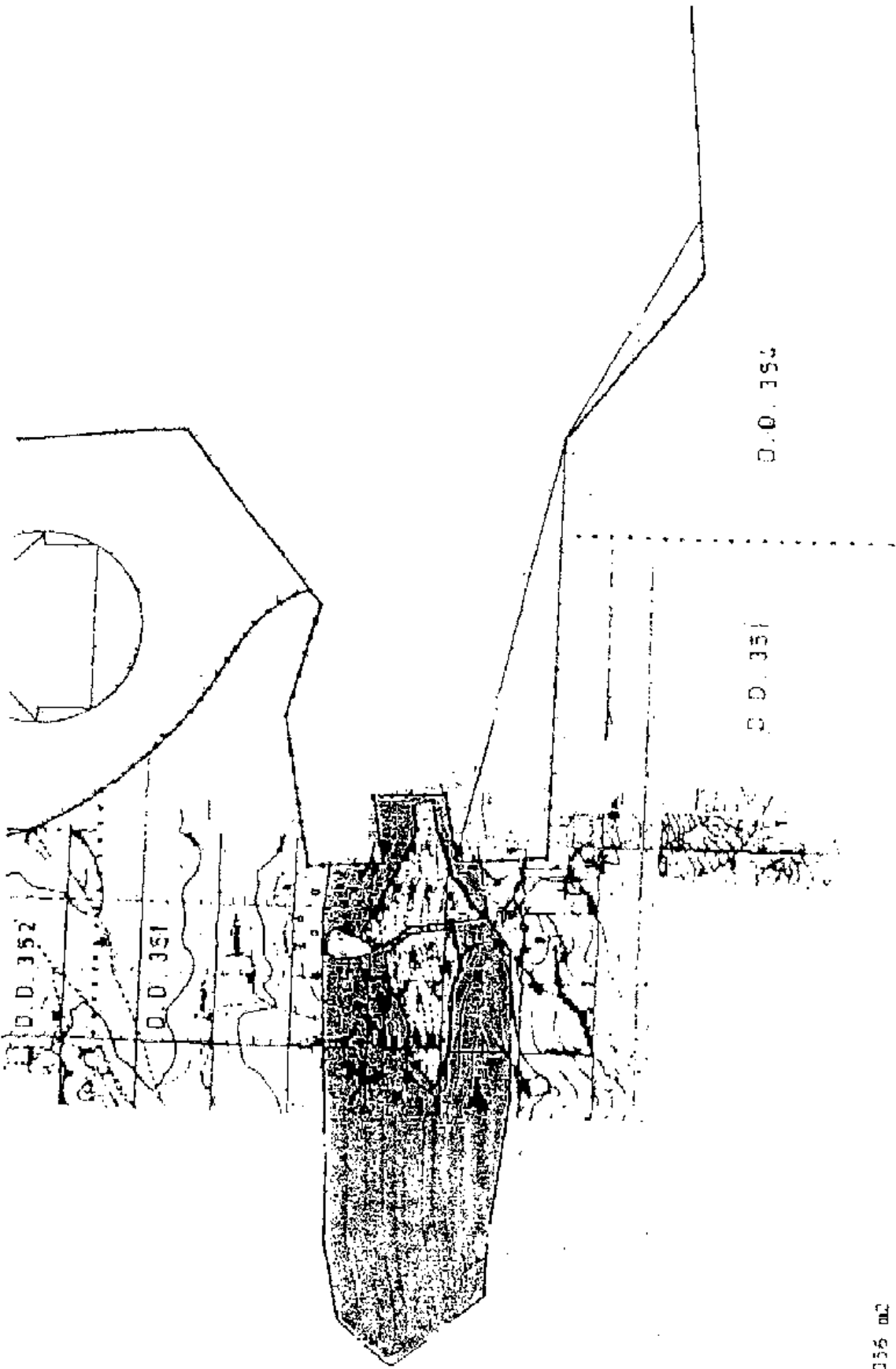
Yours faithfully
HONG KONG RESORT CO. LIMITED




Roger B Thompson
Administrative Director

RT/IM

ENC




 # 50,056 m2
 (subject)

(Subject to survey)



地政惠民 廿載新紀
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地政總署
LANDS DEPARTMENT

電話 Tel: 2231 3131
圖文傳真 Fax: 2868 4707
電郵地址 Email: adhk@landsd.gov.hk
本署傳號 Our Ref.: (27) in LD 1/IS/PL/82 XVIII
來函編號 Your Ref.: CP/C 420/2002

我們矢志努力不懈
We strive to achieve

Appendix II

香港北角渣甸道三三三號北角政府合署二十樓
20/F., NORTH POINT GOVERNMENT OFFICES
333 JAVA ROAD, NORTH POINT, HONG KONG
lands_dept@landsd.gov.hk

(Fax No. : 2521 7518)

29 July 2002

Secretary General,
Legislative Council Secretariat,
Legislative Council Building,
8 Jackson Road,
Central,
Hong Kong.

(Attn.: Miss E. Wong)

Dear Miss Wong,

Occupation of Government Land
Discovery Bay Golf Course

I refer to your letter dated 19 July 2002 and would respond to the points raised therein as follows:-

- (1) (a) The lot of Discovery Bay (DB) was granted to Hong Kong Resort Company Limited (HKR) by Conditions of Exchange (New Grant No. 6122) dated 10 September, 1976. Pursuant to Special Condition No. 54(a) of the Conditions of Exchange (see **Annex A**), HKR is permitted to operate a golf course or golf courses in the area shown coloured red hatched black on the grant plan (see **Annex B**). Special Condition 54(c) also requires HKR to provide not less than one 18-hole non-membership golf course open for use by members of the public. The original proposal as shown on Master Plan (MP) 4.0 (see **Annex C**) indicates the

provision of a non-membership golf course in the north. Another golf course was also proposed in the southern part of the lot. In 1979, HKR (see Annex D) requested for Government's agreement to (i) abandon the non-membership golf course which, as explained by HKR, would only serve a limited number of the public and not be economically viable; and (ii) allow HKR to provide either in the same area or elsewhere on DB alternative recreation facilities that would benefit a larger sector of the public. The provision of alternative public recreational facilities in lieu of non-membership golf course was considered acceptable by Government. The proposal was approved under MP No.5 (see Annex E) on 25 February 1982. The then Director of Lands in his letter dated 16 March 1983 and 21 September 1983 (see Annexes F and G) to HKR also confirmed that a separate lease modification was not required in view of the approved MP 5.0.

- (b) On 10 August 1981, HKR applied to the Government for a Short Term Tenancy (STT) (see Annex H) to cover adjoining government land at Wong Chuk Long in order to make way for a full 18-hole golf course. Although no records on processing HKR's application can be traced, it is, however, noted from the Building Plan Conference (BPC) Notes dated 7 October 1982 (see Annex I) in respect of the Supplementary Master Plan (SMP) for Golf Course and Clubhouse – Stage I that the 4th and 5th holes of the golf course are located outside the DB lot. It is also stated in the Notes that the occupation of government land would be included in Government's future rectification exercise. The SMP was approved by the BPC of Lands Department on 27 October 1982 (see Annex J).
- (c) Presumably, the then government might have contemplated to apply General Condition No. 3(a) of the Conditions of Exchange of DB to rectify the lot boundaries at a later stage rather than granting a STT to HKR. However, there is no file record to prove this intention. General Condition No. 3(a) stipulates that "*The boundaries of the lot shall be determined by the Secretary (whose decision shall be final) before the issue of the Crown Lease*". By his letter dated 16 March 1983 to HKR (3rd paragraph) (see Annex F), the then Director of Lands stated that "It may therefore be more appropriate to await the issue of the Crown Lease at the end of the whole development whereupon Government will carry out a survey of the lot boundaries".

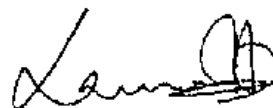
- (d) On 17 October 1996, HKR applied again for a STT (see Annex K) to cover the concerned government land which was already in use as part of the south golf course. Following consultation with the concerned departments, DLO/Is on 12 May 1998 rejected the application on the ground that the government land involved was within the proposed extension of the Lantau North Country Park at that time (see Annex L). HKR was asked to reinstate the government land. In response to DLO/Is's letter of 27 May 2002 (see Annex M) requiring reinstatement of the occupied government land, HKR requested to re-activate its previous application for a STT to cover the extended golf course (see Annex N).
- (e) It can be seen from the above that the lease governing the DB development originally made provision for both a private and public golf course. The public golf course proposal in the north was abandoned as mentioned in para. (1)(a). The existing golf course in the south was never planned as a public golf course from the very beginning. Therefore, the question of changing the nature of the golf course from public to private is considered not relevant. HKR's proposal to replace the requirement of a public golf course by alternative public recreational facilities which would benefit a large sector of the public is not unreasonable bearing in mind that golf playing was not so popular in Hong Kong twenty years ago. Government was aware of the occupation of government land in the early 1980s and it was then decided that the issue be addressed in the future boundary rectification exercise. Given the historical background above, I cannot agree that there has been mal-administration by Government in handling the matter.
- (2) Government is considering to rectify the situation by the issue of a STT to cover the areas of the DB golf course which have occupied government land. It is intended to collect rent, to be assessed on full market rent basis, with effect from the time of occupation. As the collection of rates is under the purview of the Rating and Valuation Department(R&V), you may wish to write to R & V for their advice.
- (3) Change in public recreational facility provisions in the course of large scale development like DB is not unreasonable. According to Land Registry record, the date of the (Principal) Deed of

Mutual Covenant of DB is 30 September 1982. The completed houses/flats in DB were assigned and occupied after the approval of MP 5.0 (approved on 25 February 1982) under which the non-membership golf course had already been abandoned. Therefore, the question of payment of compensation to DB residents in respect of the change is considered not relevant.

- (4) The total area of occupation on government land is in fact less than 4% of the total area of the golf course (about 104ha) within the private land in DB. It is considered that such a comparatively small additional area would not have any adverse impact on the residents of DB.

Kindly note that except for Annexes A and B, all other annexes either involve third party information or internal discussion and advice under the Code of Access to Information and should not be released to the complainant/District Council concerned.

Yours sincerely,



(Ms. Olga LAM)
for Director of Lands

Encls.

c.c. w/o encl. DPO/SK&Is, PlanD (Attn.: Ms. C.M. LI) Fax : 2890 5149
DEP, EPD (Attn.: Mr. Y.M. HUI) Fax : 2591 0558
DAFC, AFCD (Attn.: Miss C.Y. HO) Fax : 2377 4427
DO/Is, HAD (Attn.: Miss Kathy CHAN) Fax : 2815 2291
DLO/Is (Attn.: Mrs. Florence TSANG) Fax : 2850 5104

OLFT/LSK/cf

Annex F

16th March, 1983

(178) in LRD 1/15/PL/32 IX

Hong Kong Resort Co. Ltd.,
26/F, Health Building,
71 Des Voeux Road, Central,
Hong Kong.

Dear Sirs,

Discovery Bay - Lot 385 in DB 352
Conditions of Exchange

Thank you for your letter dated 1st February 1983 which I have discussed with the Registrar General. I can now confirm that, subject to Special Conditions 9 and 10 of New Grant No. 6122, once I am satisfied that not less than \$500 million has been spent on some parts of the lot in respect of which a partial certificate of compliance has been issued you may under Special Condition 3(d) assign other parts of the lot solely for the purpose of development in accordance with the Master Layout Plan No. 5 and in compliance with the conditions in New Grant No. 6122.

I also confirm that your understanding in paragraph 4(a) (page 2) in respect of Special Condition 5(a) is correct, and that in view of the agreed Master Layout Plan No. 5 there is no need for a separate modification concerning the non-membership golf course. However, since the cable-car system is shown, a separate modification would in theory be necessary, but deletion of this in any future revision of the Master Layout Plan would obviate this necessity.

Although the original lease plan with the subsequent golf course extension, enlargement of the reservoir etc. is now largely historical, the present MLP No. 5 is not subject to Government survey and can only be a guide to your Company's present and future intentions. In other words neither plan at this stage is really satisfactory. It may therefore be more appropriate to await the issue of the Crown Lease at the end of the whole development whereupon Government will carry out a survey of the lot boundaries.

Finally, I agree that a formal letter should in due course be registered in the District Lands Office, Islands confirming the amendments so far agreed.

Yours faithfully,

(Sgd.) J. R. Todd
(J.R. Todd)
Director of Lands



電郵地址 Email: dofl@landsd.gov.hk
 電話 Tel: 2231 3000
 圖文傳真 Fax: 2868 4707
 本署編號 Our Ref: LD I/IS/PL/82 (TC) XXIII
 來函編號 Your Ref: CB(3)/PAC/R43

24 January 2005

Clerk
 Public Accounts Committee
 Legislation Council Building
 8 Jackson Road
 Central
 Hong Kong
 (Attn: Ms Miranda Hon)
 [Fax: 2537 1204]

Dear Ms Hon,

**The Director of Audit's Report on the
 results of value for money audits (Report No. 43)**

Chapter 6: Grant of land at Discovery Bay and Yi Long Wan

I refer to your letter of 13th January 2005 and as requested provide the following additional information.

- (a) *An elaboration of the basis for the legal advice that "the letter of 16.3.1983 created a relationship of landlord and tenant" (the reply to question (k) in the Director's letter of 8 January 2005 (PAC/R43/CH6/GEN/9) and paragraph 5.24(c) of the Audit Report refer).*

In considering Developer A's application for a Short Term Tenancy (STT) in July 2002, Lands D had taken legal advice on the status of

the encroached land. The advice was that Government had acknowledged the occupation of the land by Developer A in a series of correspondence over a number of years since March 1983 and had indicated in writing that the encroachment would be regularized upon issue of the Crown Lease at the completion of the whole development when Government would carry out a survey of the lot boundaries. In October 1996, Developer A applied for a STT of the encroached land. This was rejected at the time as the land was within the proposed extended limits of the Lantau North Country Park. Developer A reactivated their application for a STT in mid 2002, and this was approved by the District Lands Conference in July 2002.

Based on the foregoing sequence of events and course of conduct by Government in its dealings with Developer A regarding the encroached land between the time of Government becoming aware of the encroachment in 1982 and issue of a formal STT in 2002, legal advice to Lands D was that a form of tenancy would have been created. Since Developer A has been occupying the encroached land with the full knowledge and acquiescence of Government in this period (with the intention of regularization upon the completion of the development of Discovery Bay) it could not be said to be a trespasser. It was a tenant at will from the Government, subject to agreement of boundaries and any other terms, including rent or mesne profits payable for the period of its occupation prior to issue of the formal STT. It was on this basis that Government was entitled to demand the payment of the rent or mesne profits for the period from 1982 to mid 2002.

- (b) *Regarding the Chief Secretary (CS)'s decision in 1985 that there was no need to report to the Executive Council (ExCo) on the change in concept of the Discovery Bay development (paragraphs 2.19 to 2.21 of the Audit Report refer), Sir David Akers-Jones stated in his reply of 5 January 2005 to the question on 2.21 (L2) (p.8 of Part 2) that he "accepted DPC's advice that it was unnecessary to refer to ExCo since the resort concept was maintained and the changes did not represent a major change in principle". In this connection, the Committee would like to know whether, apart from the file minute dated 17 October 1985 from Mr J R Todd (SLW) to the CS, there are any other documents/information relating to the DPC's advice to the CS*

and the process leading to CS's decision, which has not been provided to the Committee. If there is such documents/information, the Committee would like to be provided with a copy of the documents and/or the information.

I would confirm that, to the best of our knowledge, apart from that already provided to the Public Accounts Committee, there are no other relevant documents/information relating to the DPC's advice to the CS and the process leading to the CS's decision.

With regard to answer (c) of my letter dated 8th January 2005 relating to your letter of 17th December 2004 I would supplement as follows :

- (c) *Whether the exclusion of the encroached government land at Wong Chuk Long from the boundary of Lantau North (Extension) Country Park in 2001 was partly due to the fact that Developer A had repeatedly applied for a STT for the land.*

The boundary of Lantau North (Extension) Country Park originally proposed in 1996 on the one hand included part of the golf course area on encroached Government land but on the other hand excluded another part on encroached Government land. Following consultation among concerned Government departments, the Director of Agriculture, Fisheries and Conservation excluded the entire encroached area from the proposed boundary of Lantau North (Extension) Country Park in 1999. This was reflected in the draft map for the Lantau North (Extension) Country Park gazetted in July 2001 and the Discovery Bay Outline Zoning Plan gazetted in September 2001. There was no information on record that the STT applications by Developer A had influenced the determination of the proposed boundary of an extended Lantau North Country Park.

The PAC has also requested information on the estimated amounts of premium involved in each of the changes made in the MLPs prior to 7 June 1994 based on the market conditions at the time when the changes were made (your letter of 2 December 2004 refers). I would revert on this question separately.

The PAC may also be interested to know that the dimension plan survey for the Discovery Bay development boundary has now been completed by the District Survey Office/Islands, and the setting out work will be completed by end of March 2005 (paras. 5.5 and 5.12(c) of the Audit Report refer).

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Patrick Lau', written over a diagonal line that extends from the bottom left towards the top right.

(Patrick Lau)
Director of Lands

c.c. Secretary for Housing, Planning and Lands
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred WONG)
Director of Audit

Sir David Akers-Jones

Unit 333, Block 4, Parkview
88 Tai Tam Reservoir Road
Hong Kong
Tel: (852) 2491 9319
Fax: (852) 2491 1300
E-mail: akersjon@pacific.net.hk

5 January 2005

Dr. the Hon Philip Wong, GBS
Chairman,
Public Accounts Committee
Legislative Council, HKSAR

Dear Sir,

**Response to Public Accounts Committee (PAC) Queries
Chapter 6, Director of Audit Report No.43**

Further to the letter from the Clerk of the PAC dated 14 Dec 2004, I submit my response in two parts as attached:

Part 1 – a general statement setting out the historical background to the Discovery Bay development.

Reading the transcripts of the public hearings, it seems to me that some of the expressed views on the matter lack an understanding of the period. They also reflect an apparent mistrust in the government which facilitated Hong Kong's economic development during those years. The information I have provided to the best of my knowledge and memory is due to my belief that the issues must be looked at against the whole background of the seventies and eighties during which time the developments took place.

Part 2 includes a point-to-point response to questions raised in the letter.

I have answered your questions & those raised by members of the PAC to the best of my ability and there is nothing I can usefully add to what I have written. You will appreciate that with limitation of memory, at the age of 77 and 25 years later, I cannot recall detail of the discussions on the issues. However after having read my response, if members have supplementary questions, I should be grateful if they

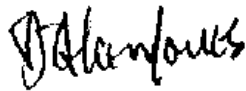
Sir David Akers-Jones

Unit 333, Block 4, Parkview
88 Tai Tam Reservoir Road
Hong Kong
Tel: (852) 2491 9318
Fax: (852) 2491 1300
E-mail: akersjoo@pacific.net.hk

would let me know what they are and I shall be glad to try to answer them.

I have arranged for this submission to be translated into Chinese and shall send it to you by 7 January.

Yours faithfully,



David Akers-Jones

Encl.

Hong Kong in 1970's to 1980's

Surrender & Re-grant of Land

The Discovery Bay development originated in 1973 when Exco authorized the Government to proceed with a scheme at Discovery Bay proposed by Mr. Edward Wong who planned to embark on a holiday resort and residential/commercial development at Discovery Bay. In 1976, Exco approved an exchange of land to Mr. Wong's company, Hong Kong Resort Company Limited. The exchange was partly land he owned and partly a Letter B exchange ie a surrender and re-grant of land he owned which he wished to develop in a certain way rather than a fresh private treaty grant.

Normally land exchanges or surrenders and re-grants do not need to go to Exco for approval because the developer is, in effect, developing his own land in accordance with a relevant Zoning Plan. On this occasion, it went to Exco probably because it involved breaking ground in the New Territories and was a very large innovative project. I was familiar with the area having first visited it as long ago as 1958 to inspect an abattoir.

In 1977, when Mr. Wong's business went into liquidation and the development was in the hands of the mortgagee bank, another developer (a joint venture) took over the development (by buying Mr. Wong's shares in his company) with the encouragement of the Hong Kong Government which feared that this huge project would founder. Understandably the Government did not want the land to remain under the control of the mortgagee.

Economic Growth in 1970's

In 1966 and 1967, Hong Kong was hit by riots and strikes. Social problems, housing shortages, unemployment were general while the economy was weak – In Christopher Howe's *The Political Economy of Hong Kong Since Reversion to China*, real GDP growth between 1973 to 75 was recorded as 1.3% on average per annum only. This was followed by a period of accelerating growth which presented government officials with a challenge of a different nature

Hong Kong enjoyed this period of rapid economic growth in the 70's under the

governorship of the late Lord Murray MacLehose. His administration saw him moderating the traditional attitude of disinterest in community problems and foresaw the need for a more balanced, progressive and proactive social development regime. Lord MacLehose's 10-year reign contributed to many achievements by Hong Kong, most notably the following:

- An ambitious housing and new town development programme which provided homes for the great number of immigrants and refugees.
- Development of the New Territories to provide sites both for huge housing developments and industrial parks. Tsuen Wan, Kwai Chung, Tai Po, Tuen Mun and Shatin were all 'products' of this era.
- An enviable transport infrastructure with the construction of the MTR system.
- Thorough Government reforms to reduce red-tape and optimize efficiency to meet spiraling community development and infrastructure demands.
- Forceful and effective combat against widespread corruption by the introduction of the ICAC which answered direct to the then Governor of Hong Kong.

Administrative Procedures

It is against this background that from as long ago as 1960 when public housing and urban development was extended to the New Territories, the NT Administration greatly strengthened its land administration with the attachment of professional chartered surveyors and lawyers to oversee land transactions with technical knowledge and expertise to ensure the public interest was properly safeguarded. As development proceeded, the number of estate surveyors seconded by the Director of Land and Survey increased dramatically while the staff of lawyers was commensurately increased.

In 1973, at the time of government's initiative to build homes for 1.5m people in the New Territories and new towns, I was appointed as the Secretary for the New Territories (SNT). This was a new post replacing the former District Commissioner. The SNT was on all fours with other government Secretaries, and he was responsible for implementing government policies and development in the New Territories. I remained in this post for an unprecedented period of twelve years. It is curious, to say the least, that the matters raised by the Director of Audit about the seventies and eighties are raised after a period of 20 –25 years and were not raised at the time or in subsequent years.

Among my staff during those years was a team of estate surveyors headed by a Principal Government Land Agent (PGLA) responsible to me as Secretary. The policies and practices of the urban area were applied to the New Territories.

Because of the relatively small number of large development sites, there were few Master Layout Plans (MLPs) in the 1970's. The practice for dealing with these plans, including the question of whether a premium should be charged, involved examination by experienced chartered surveyors to see if each complied with the underlying lease and with the appropriate development criteria. Thus the Discovery Bay MLP and changes to it emphatically required professional officers to take premium considerations of the lease into account.

For the approval of MLPs for the New Territories, the process would have the applicant typically sending the MLP to the District Office (DO), headed by an Administrative Grade Officer. The Estate Surveyor in the district, a chartered surveyor, would examine it and consult other departments where necessary before putting it with other land cases to the monthly District Conference (later the District Land Conference (DLC)) headed by the DO and attended by the Senior Estate Surveyor (SES), later a Chief Estate Surveyor (CES), and representatives of other departments. The views of all departments were taken into account.

When the District Conference or DLC approved the MLP, it would go to New Territories Administration Headquarters to PGLA/NT (via a senior officer such as a Chief Estate Surveyor) and my recollection is that PGLA/NT would table it either at the monthly New Territories Lands Meeting (NTLM) or at a similar meeting of senior administrative officers, estate surveyors and lawyers. Only when NTLM or the group of officers recommended its approval would PGLA/NT put the recommendation by a minute on the file to me as SNT for formal approval. PGLA's recommendation therefore would represent the collective view of the professional estate survey staff.

I would not have approved a MLP or changes to a MLP or any land transaction that had to be dealt with by me without a full discussion with the PGLA. If the PGLA/NT thought a premium or other conditions of approval were justified, he would have recorded it and action would have been taken.

For valuations, there was also a set procedure. A Valuation Committee met each month in HQ and was made up of Senior Estate Surveyors and Estate Surveyors from all districts. Valuations for premium etc. were made by the District Estate

Surveyors and then discussed and approved by the central Valuation Committee. If an estate surveyor in a district was uncertain whether a MLP had a valuation implication he would put it to the Valuation Committee, after discussing it with his senior. The MLP then went to PGLA/NT and NTLM or to other senior officers. Appeals by developers from Valuation Committee in NTA/HQ would go to urban area Valuation Committee.

While there were few MLPs processed in this period, the question of premium for a change for MLP was always actively considered. These were well known procedures understood by the staff. And as will be gathered from this description well established administrative procedures were in place to ensure that decisions could not be made by a single officer.

The description above is how things worked. It should inspire confidence that there was a due process to which we were all bound and which provided the ultimate safeguard for the public interest as well as the integrity of the individuals involved.

As the Secretary, I was tasked to see to it that the Governor's intention to achieve his objectives was followed, while ensuring that proper checks and balances were in place to ensure that the public interest was protected. I was authorized to make judgments but, since I was not a valuer or a professional land person, always based them on the input of my executive and professional colleagues. Thus decisions when they were made always had the benefit and support of sound professional advice and recommendations.

When the Discovery Bay project was put to Exco in 1976, the Exco Memorandum proposed that, "the land at Discovery Bay should be granted to Developer A for a holiday resort and limited residential/commercial development..." (2.7, Chapter 6, Director of Audit Report No.43). However the decision of Exco, after having considered the contents of the memorandum and the lease conditions attached to it, gave the following advice and the Governor ordered that land should be granted to the Developer for the purposes of "a holiday resort and residential/commercial development at the premium of \$61.5 million" (2.7, Chapter 6, Director of Audit Report No.43). This represents a significant change from which all subsequent developments followed. The Secretary for the New Territories, myself, would normally have been present during the discussion of this memorandum by Exco.

This Exco decision became the parameter within which the subsequent development took place and it had to conform to this decision. Did changes

conform with the development of a resort with residential/commercial development? Were they soundly based and well supported? The authority to ensure this was placed in the hands of the Secretary for the New Territories. In 1978 the Secretary for the New Territories was appointed to Exco.

Throughout its thirty years of history the development of Discovery Bay has conformed with the description that it was a resort, is a resort and will continue to be a resort. This is even reflected in the Explanatory Statement in the Discovery Bay Outline Zoning Plan of 27 years later in 2003, "it is primarily a car-free environment evolved from the original concept of a holiday resort approved in 1973. This intention [of a resort] is still maintained by the existing and planned provision ..."

A resort can take many forms but essentially it is a place where people go to get away from crowded urban living. All the residents of Discovery Bay are there for that reason and it is noteworthy that even when there is currently access by motor vehicles to Discovery Bay private transport vehicles have to stop at the perimeter!

The development of Discovery Bay was the first large-scale project of its kind in Hong Kong and development has continued over a period when dramatic changes in Hong Kong's socio economic environment have taken place. Changes to a MLP to reflect this were therefore inevitable. The important thing is that, as and when changes were proposed, they were dealt with properly by well-defined and understood procedures and were not taken by one person acting alone and autocratically.

It is noteworthy that to avoid public expenditure on the wild and rocky landscape of Discovery Bay the Developer was asked to shoulder the provision of public services and facilities which would normally be provided by the Government. These included the ferry service, building of a reservoir, provision of water and sewage treatment to the development, access roads, a fire service and police station, urban management services including cleaning and security, and to go to considerable extra expense at the request of government to provide a water supply to surrounding villages. Despite having to make these provisions which normally fall to the Government to provide the Developer was assessed and paid rates as if in the urban area.

xxx

The matter of my invitation to become a non-executive director of Mingly was mentioned during the PAC hearing. Mingly is principally an investment company. The invitation was made in year 2000, 13 years after my retirement as Chief Secretary.

Part 1 ends

Replies to Specific Items

Public Account Committee's letter dated 14 December 2004

Item (a)

2.8 (L1)

Question

On 10 September 1976, the Secretary for the New Territories executed the lease for the Discovery Bay development. However, the lease conditions did not specify the maximum and minimum gross floor area (GFA), and the gross site area of the facilities (such as the resort accommodation) to be provided by Developer A. In addition, the lease conditions did not restrict the owners to use their flats only as holiday homes. In April 1977, Exco was informed that the conditions allowed for low density development which, at the maximum, would provide over 401,342 square metres of residential resort accommodation and 140,284 square metres of hotel accommodation (Note 3).

Response

The lease was drafted by a lawyer of the Registrar General's Department. Instructions to the lawyer on what was to go into the lease conditions would have been given in the usual scrutiny by all the various interested departments, both within and outside the then Public Works Department and the New Territories Administration. There were standard clauses (then known as FG Clauses) which the various departments could direct to go into lease conditions.

I do not know why it was decided to specify the exact extent of development permitted by a master plan rather than in the lease conditions but I believe that because a master plan would combine control with flexibility. It would not then be necessary to modify the lease every time there was a change to the development. I note that para. 2.7 of the Audit Report said that the lease conditions were considered by Exco.

I cannot recall the details of the referred 1977 Exco paper. Nevertheless, the residential development of Discovery Bay development does not depart from "residential resort accommodation" which is elaborated further in my reply to item (b) below.

Note 3 (L1) in para. 2.8

Question

According to the then prevailing MLP 3.5 approved by the Secretary for the New Territories on 3 December 1975, the Discovery Bay development would provide resort accommodation of about 401,342m² GFA and hotel accommodation of about 140,284m² GFA.

Response

Presumably, this was decided after inter-departmental consideration of the submission by the developer.

2.10 (L1)

Question

In September 1977, MLP 4.0 was submitted for the Secretary for the New Territories' consideration. Under MLP 4.0:

- (a) the hotel GFA was reduced from 140,284 square metres to 32,000 square meters;
- (b) the resort accommodation GFA of 401,342 square metres was deleted; and
- (c) housing accommodation GFA of 524,000 square metres (including garden houses GFA of 301,000 square metres and holiday flats GFA of 223,000 square metres) was added.

Response

The developer would have made a formal application for approval of this MLP and the changes from the previous MLP would have been justified by the developer in such an application.

As explained by the Director of Lands at the second hearing, the total residential, commercial & hotel GFA did not increase beyond the maximum 608510 m² approved at the outset of the development. Whether or not premium was payable would have been given full consideration not by one official acting on his own but together with his

colleagues and superiors. It seems that no premium was charged after this proper consideration, no doubt taking into account the drastic slump in the property market.

2.13 (L1)

Question

In late October 1977, Developer A wrote to the Secretary for the New Territories (Note 6) to elucidate certain key concepts in the revised MLP 4.0. As Hong Kong worker would be entitled to an annual seven-day holiday with effect from January 1978, a new group of potential visitors to Discovery Bay had arisen and ways should be sought to bring the facilities within the reach of such people in addition to those who were better off. The holiday flat concept in MLP 4.0 was to build high-rise condominiums containing fully furnished units of various sizes. The units would be sold to buyers either for their own use or for leasing. Developer A was aware that, under the lease conditions, he had to provide the facilities (including the public golf course) without which the Discovery Bay development would not be complete. The facilities would only be financially viable when the housing development was reasonably advanced.

Response

This would be the justification I referred to in my response under 2.10(L1). To me, it shows clearly the intention of the developer to meet the intention of the original resort concept and to make appropriate planning changes to meet socio-economic development in Hong Kong at that time.

2.14 (L1)

Question

Approval of MLP 4.0. In November 1977, the Secretary for the New Territories accepted MLP 4.0 for the following reasons:

- (a) the basic concept of building a resort was continued;
- (b) substantial recreational facilities were brought forward in MLP 4.0;
- (c) furnished holiday flats were substituted partly for the hotel rooms and partly for the more spacious and expensive residential accommodation (Note 7) in MLP 3.5. This would open up the area to more people; and

- (d) MLP 4.0 conformed with the approved lease conditions which had been submitted to Exco.

In January 1978, the Secretary for the New Territories approved and signed MLP 4.0.

Response

The Secretary for the New Territories had authority under the lease conditions to give consent to alterations of master plans. Refer to the reply to item (b) below regarding the general procedures for processing master layout plans at that time.

I am not sure where these reasons quoted above have been extracted from, e.g. from a minute on a file? However, they appear to me at this distance of time to be adequate reasons for my decision at the time. I have no other comment as I have no other specific recollection.

As at today, I still consider that the present Discovery Bay is, in effect, a large seaside resort. This is elaborated in my reply to item (c) below.

3.5 (L3)

Question

In July 1977 (i.e. less than one year after the land grant), Developer A proposed to change the public golf course to some other form of public recreational use which would provide for more people and be a greater attraction. The Secretary for the New Territories said that he would consider quite favorably such a change if Developer A would meet that criteria. In March 1979, based on the argument that it was not economically viable to provide a public golf course, Developer A sought the Secretary for the New Territories' approval in principle:

- (a) to abandon the concept of a public golf course; and
- (b) instead, to locate within the site suitable areas for active public recreation.

Response

I understand the developer applied to waive the requirement to create a public golf course by demonstrating that such a facility with maximum usage would only accommodate a small number of players per day. Players would also incur

considerable extra expenditure and a costly ferry trip. In the early days, golf was not the popular game it has since become but even now by the nature of the game it cannot cater for mass participation. The decision not to go ahead with a full-blown public golf course at that time was supported by the responsible department for recreation - the then Recreation & Culture Department. (The strange intervention by the unrelated Highways Department was no doubt inspired by that individual's personal enthusiasm and background). No doubt, too, the department's recommendation was made because of an unwillingness on the part of the government possibly to take on the management and maintenance responsibility for something that would be a drain on resources. It should be mentioned that the membership golf course has been available to members of the public on weekdays since its completion.

The reference to Kau Sau Chau brings out a case in point. It was built with a philanthropic expenditure of charitable funds of \$500 million from the Jockey Club with the management responsibility left with the Jockey Club not the Government.

The public golf course was replaced by the much more extensively used 700m long man-made beach built with I understand some 300,000 m³ sand transported by barges from the Mainland. Both residents and visitors alike are free to use the public beach. It is enjoyed by rich and poor alike with altogether different usage from a golf course whether public or not. Compare both sides of the road at Deep Water Bay: few people on the golf course, masses on the beach. Other recreational facilities which have been provided by the developer are described in paras. 4.7 – 4.10 in the Audit Report. No doubt these developments were the subject of discussion between the developer and the Government in fulfilment of the pledge to provide an alternative to the public golf course.

3.17 (L4)

Question

In 1973, when Exco agreed that the Discovery Bay development could proceed, Exco was informed that a public golf course would be built and that 90% of the recreational facilities would be available to the public. In addition to the public golf course, a 36-hole membership golf course was included. In September 1976, the Secretary for the New Territories granted the land to the developer. However, in February 1982, after consideration of Developer A's proposal, the Secretary for City and New Territories Administration approved MLP 5.0 and the public golf course had been deleted.

Response

See previous answers.

4.2 (L1)

Question

In 1979, Developer A agreed with the Secretary for the New Territories to replace the public golf course by some active public recreational facilities in the same area or elsewhere within the Discovery Bay site. It was said that the provision of active public recreational facilities would be more appealing to the majority of the local population than a golf course. In December 1982, when the deletion of the public golf course and the cable car system was discussed, the then Recreation and Culture Department welcomed the proposal that other recreational facilities would be provided in place of the public golf course.

Response

This shows that other departments of the Government supported the deletion of the golf course. As to the cable car, which has caused considerable attention, I would like to comment as well.

Cable Car

At Discovery Bay, the land slopes quite steeply from the foreshore. Leading to the North is a steep hill and to the south an extensive undulating plateau. The cable car was to provide access to the plateau. However when the reservoir was built and further extended, the paved construction roads provided an easy and more useful access to the plateau and the cable car was deleted and the landscape and environment incidentally spared this ugly and unnecessary intrusion. It was an imaginative idea but totally unnecessary and useless hence its deletion.

5.6 (L8)

Question

In August 1978 (one month before the execution of the lease conditions), the then Government Land Surveyor of the Public Works Department said that the boundary

corners of the Discovery Bay site would be pegged by interpretation of position of points from ground features shown on Developer A's plans. He also said that no boundary dimensions would be provided as a survey would be done after fencing of the site. In May 1977, the Government Land Surveyor said that although considerable preparation for the boundary pegging was made, the pegging itself had not yet been done in order to avoid possible abortive work. The Secretary for the New Territories also agreed that such setting out would not be required at that time. In July 1977, the then District Office/Islands of the New Territories Administration informed the Government Land Surveyor that no further work should be done until Developer A had decided on the type of fence to be provided and was ready to let the fencing contract.

Response

Boundary pegging was the duty of the Government Lands Surveyor. It may have been the practice at that time that boundary pegging would be carried out upon completion of a large development to avoid abortive works. In any case, as the boundaries of this lot were very long and extended over very rough and steep terrain and this Crown Land area had never been properly surveyed (indeed I believe there was not even one proper survey for any area of Lantau at the time) it would have made good sense for the developer to proceed on indicative boundaries and to do the exact boundary fixing after development was completed. This seems to have been a reasonable explanation of what happened.

Mr McGraw referred to by the Director of Audit would have been either a Senior or Chief Estate Surveyor in New Territories Administration Headquarters with delegated authority to deal with this sort of thing.

5.15 (L5)

Question

In September 1982, Developer A submitted a Supplementary MLP 5.0 (Note 24) for the south golf course and clubhouse development to the Lands D for approval. The route plan for the 18-hole south golf course showed that the fourth and fifth holes were on government land at Wong Chuk Long. Developer A said that the extension of the area for the fourth and fifth holes had been agreed in prior meetings with the Secretary for the New Territories.

Response

Most probably there were meetings on this, but I cannot recall details of the discussions. There would have been meetings with my staff. I do not read the reference in the developer's letter as meaning necessarily that the developer had meetings with me. The developer may well have been referring to meetings with the headquarters staff of the New Territories which may not have involved meetings with me at all. Nevertheless it seems from the decision taken that the extensions into the hillside to complete the golf course onto Crown Land hillside which did not conflict with any public use at the time were seen as something which could be sorted out at a later date, which indeed they were and rent duly charged and backdated.

2.21 (L2)

Question

In a DPC meeting held on 14 November 1985, the Secretary for Lands and Works reported that the Chief Secretary considered that "there was no need to go to Exco or the Land Development Policy Committee as the ... development followed on from the development so far approved (i.e. resort development) and did not represent a major change in principle".

Response

The Development Progress Committee (DPC) was chaired by the Secretary for Lands and Works and consisted of senior officials relevant to this objective. It included the Principal Assistant Financial Secretary. In other words, it was a most senior and responsible organ of government. The year was 1985. The Joint Declaration had just been approved. HE the Governor and the Executive Council were very occupied. The Governor himself was beginning a long period of shuttling between Beijing and London. On the Chief Secretary, myself, fell additional administrative responsibilities. I accepted DPC's advice that it was unnecessary to refer to Exco since the resort concept was maintained and the changes did not represent a major change in principle.

Please refer to my reply to item (c) below.

3.7 (L1)

Question

Despite the above comments [from PGLA], in February 1982, the then Secretary for City and New Territories Administration (Note 18) approved MLP 5.0 which removed the requirement for the provision of the public golf course (295,000 square metres gross site area). In September 1982, Developer A said that:

- (a) the public golf course had limited use and was for the more wealthy people; and
- (b) some modifications had been made to public recreation aspects, encompassing a whole range of activities which appeal to all ages and income groups.

Response

I do not recall the details of the discussions relating to replacement of the public golf course with public recreation facilities. (See my response under 3.5 (L3)) My officers would have considered the matter on a collective basis at the time and would have consulted all the necessary departments.

Even with hindsight and the relevant information furnished in the Audit Report, I consider that this was a right decision at that time because

- (a) golfing was a game for the elite at that time. It did not have wide popular appeal;
- (b) more people, particularly blue and white collar workers, could enjoy the replacement public recreation facilities including the beach; and
- (c) the replacement public recreation facilities had the same gross site area as and even greater gross floor area than the public golf course (Table 2 of Audit Report refers)..

It should again be mentioned that the membership golf course has been available to members of the public on weekdays since the completion.

3.17 (L6)

Question

In 1973, when Exco agreed that the Discovery Bay development could proceed, Exco was informed that a public golf course would be built and that 90% of the recreational

facilities would be available to the public. In addition to the public golf course, a 36-hole membership golf course was included. In September 1976, the Secretary for the New Territories granted the land to the developer. However, in February 1982, after consideration of Developer A's proposal, the Secretary for City and New Territories Administration approved MLP 5.0 and the public golf course had been deleted.

Response

The public golf course was replaced with public recreation facilities of the same gross site area and even greater gross floor area as explained in above response under 3.7.

4.3 (L1)

Question

In December 1981, when submitting MLP 5.0 for the Secretary for City and New Territories Administration's approval, Developer A submitted a proposal on the provision of "replacement public recreational facilities" for day visitors with a much wider range of pursuits.

Response

See previous answers. This proposal would have been part of the overall package of amendments to the MLP the developer was putting forward.

4.4 (L1)

In February 1982, the Secretary for City and New Territories Administration approved MLP 5.0. Compared with MLP 4.0, there were changes in MLP 5.0, as follows:

Response

Based on Table 2 of Audit Report, it is noted that there was a net increase in gross floor area of recreation facilities from MLP 4.0 to MLP 5.0. Although the gross site area of the recreation facilities was shown to be reduced, the public beach in Discovery Bay was not included in the Table.

Item (b)

Question

According to paragraph 2.14 of the Audit Report, the Secretary for the New Territories accepted Master Layout Plan (MLP) 4.0 in November 1977, and approved and signed it in January 1978. According to paragraph 3.7 of the Audit Report, the Secretary for City and New Territories Administration approved MLP 5.0 in February 1982. The PAC would like to know whether you had consulted any government departments/officials or held any relevant meetings before approving MLPs 4.0 and 5.0 and, if so, details of the discussion.

Response

I was the Secretary for the New Territories from 1973 to 1985, an unprecedented period of twelve years. It is curious, to say the least, that the matters raised by the Director of Audit about the seventies and eighties are raised after a period of 20 –25 years and were not raised at the time or in subsequent years.

Among my staff during those years was a team of estate surveyors headed by a Principal Government Land Agent (PGLA) responsible to me as Secretary. The policies and practices of the urban area were applied to the New Territories.

Because of the relatively small number of large development sites, there were few Master Layout Plans (MLPs) in the 1970's. The practice for dealing with these plans, including the question of whether a premium should be charged, involved examination by experienced chartered surveyors to see if each complied with the underlying lease and with the appropriate development criteria. Thus the Discovery Bay MLP and changes to it emphatically required professional officers to take premium considerations of the lease into account.

For the approval of MLPs for the New Territories, the process would have the applicant typically sending the MLP to the District Office (DO), headed by an Administrative Grade Officer. The Estate Surveyor in the district, a chartered surveyor, would examine it and consult other departments where necessary before putting it with other land cases to the monthly District Conference (later the District Land Conference (DLC)) headed by the DO and attended by the Senior Estate Surveyor (SES), later a Chief Estate Surveyor (CES), and representatives of other departments. The views of all departments were taken into account.

When the District Conference or DLC approved the MLP, it would go to New Territories Administration Headquarters to PGLA/NT (via a senior officer such as a Chief Estate Surveyor) and my recollection is that PGLA/NT would table it either at the monthly New Territories Lands Meeting (NTLM) or at a similar meeting of senior administrative officers, estate surveyors and lawyers. Only when NTLM or the group of officers recommended its approval would PGLA/NT put the recommendation by a minute on the file to me as SNT for formal approval. PGLA's recommendation therefore would represent the collective view of the professional estate survey staff.

I would not have approved a MLP or changes to a MLP or any land transaction that had to be dealt with approved by me without a full discussion with the PGLA. If the PGLA/NT thought a premium or other conditions of approval were justified, he would have recorded it and action would have been taken.

As such, I am sure that other government departments would have been consulted and relevant meetings held prior to the approval of MLP 4.0 and 5.0. However, with limitation of memory and at the age of 77 and 25 years later, I cannot recall detail of the discussions at that time related to these master layout plans.

Item (c)

Question

The PAC would like to know the rationale for the Chief Secretary's view in October/November 1985 that there was no need to go back to the Executive Council or the Land Development Policy Committee regarding the change in the concept of the Discovery Bay development (paragraph 2.21 of the Audit Report refers).

Response

When the Discovery Bay project was put to Exco in 1976, the Exco Memorandum proposed that, "the land at Discovery Bay should be granted to Developer A for a holiday resort and limited residential/commercial development..." (2.7, Chapter 6, Director of Audit Report No.43). However the decision of Exco, after having considered the contents of the memorandum and the lease conditions attached to it, gave the following advice and the Governor ordered that land should be granted to the Developer for the purposes of "a holiday resort and residential/commercial

development at the premium of \$61.5 million" (2.7, Chapter 6, Director of Audit Report No.43). This represents a significant change from which all subsequent developments followed. The Secretary for the New Territories, myself, would normally have been present during the discussion of this memorandum by Exco.

This Exco decision became the parameter within which the subsequent development took place and it had to conform to this decision.

As pointed out in para. 2.21 of the Audit Report, I considered that there was no need to go to Exco or the Land Development Policy Committee because the development up to that time did not represent a major change in principle.

Throughout its thirty years of history the development of Discovery Bay has conformed with the description that it was a resort, is a resort and will continue to be a resort. This is even reflected in the Explanatory Statement in the Discovery Bay Outline Zoning Plan of 27 years later in 2003.

"It is primarily a car-free environment evolved from the original concept of a holiday resort approved in 1973. This intention of a resort is still maintained by the existing and planned provision"

A resort can take many forms but essentially it is a place where people go to get away from crowded urban living. All the residents of Discovery Bay are there for that reason and it is noteworthy that even when there is currently access by motor vehicles to Discovery Bay private transport vehicles have to stop at the perimeter!

The lease conditions, which had been presented to Exco, expressed the development concept by the terms "leisure resort facilities" in the user clause S.C. 7 and "leisure resort and associated facilities" in S.C. 5(b). The scope of the words "leisure resort and associated facilities" can only be understood by reference to the Master Layout Plan and the whole of the user condition.

The lease conditions, being a practical blueprint for the development, allow flexibility in that "such recreational, residential and commercial purposes and uses ancillary thereto as may be approved in writing by the Secretary" are also permitted. The changes were therefore evolutions of the original concept in the developer's thinking as the practical difficulties in developing this huge site in a viable way emerged and the need to adjust the balance between residential and commercial facilities and the leisure resort facilities became more evident.

Seaside resorts in other places, e.g. Port Grimaud in France, Blackpool in the U.K., Gold Coast in Australia, Miami in the U.S.A. cater for both permanent residents and temporary residents who come to use the resort facilities. Indeed, without a permanent population, these resort towns could not operate.

Part 2 ends

DM $\frac{5}{1}$ 05.

Opening Statement for PAC Appearance on 12 January 2005

Sir David Akers-Jones

Morning, Mr. Chairman, ladies and gentlemen of the Public Accounts Committee.
Before I take questions, I'd like to say a few words:

1. I am **over 77 years old and retired for over 17 years**. It is **very difficult** for a man of my age and who has been **out of Government so long to recall** things that took place over a quarter of a century ago. Many of the people who worked with me during the relevant time are unfortunately no longer with us.
2. I am being asked to deal with **events that took place over 25 years ago without** the benefit of any **contemporaneous papers** and both the time lapse and lack of access to information makes it very difficult to recollect details
3. However, I am here before you today, 25 years on, to protect the reputation of those who worked with me, many of whom are no longer with us and who cannot defend themselves, who served Hong Kong well and with the highest integrity.
4. I have **tried my best to piece together to the best of my ability with the assistance of former colleagues and friends as full a picture as possible** to the best of my knowledge and belief of what happened and the procedures followed by way of a full written response, which you may wish to disclose to the public.
5. I need time to recollect such past events and may not be able to give quick oral answers in addition to the written responses provided
6. It should be borne in mind that my **involvement in the Discovery Bay matter was very limited and took place over the short period of time between 1977 and 1982** when I was the Secretary for the New Territories.

My **successors** who took over my functions more or less followed a **similar policy direction**. By 1982, the functions of the Secretary for NT and its successor City & NT Administration had been taken over by Secretary for Land & Works and the Lands Department. So many departments have reviewed my work.

7. During the period when I was Secretary for NT, I had a **very capable team** of estate surveyors and legal advisers and I **relied on their expertise and assistance** when making decisions. There were well defined and established procedures and officials within a clear chain of command with no-one acting alone.
8. In my experience, there were **proper contemporaneous records** of transactions and I am very surprised to find that many documents have not been kept or are now missing.
9. In addition, before I made any decision, there would be input from various other departments.
10. In addition, neither the Director of Audit nor the **PAC** has ever previously made any recommendations or comments on the Discovery Bay Development when I was Secretary for NT or as far as I recall any time thereafter until now.
11. At the time when I was Secretary for the NT, there was **no planning controls** legislation in place in the NT. Also, there were few proposed developments the size of Discovery Bay at that time.
12. By way of background, in the early 1970's, Discovery Bay was a barren rocky area without any infrastructure and no development in the area. Moreover, the time taken to travel there in those days was quite long and so it was not foreseen, at that time, that Discovery Bay would be a suitable place for residences of people working in the urban areas of Hong Kong.
13. The original developer Mr Edward Wong had a good innovative idea but unfortunately, it later went into liquidation after heavily mortgaging the property to the bank. The whole Discovery Bay Project was at substantial risk of not proceeding at all and there were concerns that the mortgagee

bank may take possession of the land (though I am not at liberty to discuss the issues arising from that). Accordingly, it was important that the development be permitted to proceed with a certain degree of flexibility. This more flexible approach was allowed by Exco granting to the developer the land at Discovery Bay for a holiday resort/commercial development (as opposed to a previously restrictive approach adopted by Exco to restrict the use of land merely for the purposes of a holiday resort with limited residential and commercial use – note the exclusion of the word “limited” from the division of Exco). [This is quoted from paragraph 2.7 at p7 of Part 1 Chapter 6 of the Audit Report].

14. It was the lease conditions that specify the planning intention of the land (there being no outline zoning plan). In the master layout plan under the lease conditions was a mechanism for giving control with a degree of flexibility. This was drafted by a senior official in the Registrar General's Department.
15. The master lay out plan provisions incorporated into the lease conditions were clear and, following my short period of involvement in the Discovery Bay Project as Secretary for NT, was up to my successors to deal with any lease conditions (or master lay out plan provisions) as they deemed appropriate.
16. Given the barrenness, long distance, the lack of infrastructure and difficulty of access to urban areas of Hong Kong in the 1970's and there being no precedent for such an idea, it would have been difficult to assess its popularity in terms of how many people would buy holiday homes or use the recreation facilities or if it would have been different had a hotel been built. In addition, it would have been hard then let alone now to assess the value of a hotel development as opposed to a holiday home development in respect of such a risky development. With far better infrastructure and facilities provided by developers and the benefit of hindsight, it is much easier to assess the popularity of the area now, compared to a quarter of a century ago. In any event, the estate surveyors

in those days would have made their best valuation assessments at that time and I would have followed their advice and legal advice when making any decisions.

17. I believe that Discovery Bay has well surpassed expectations of being a resort though I am surprised that 25 years later, it has become such a convenient haven for commuters who like the resort environment and no-one could have dreamed that it would be so close to MTR, Disney, the airport and other transport facilities. It would have been unreasonable to limit the periods of stay of owners of holiday homes and expect them to only stay there on weekends and on retirement.
18. I believe that Discovery Bay was a resort and would remain one with its fine recreational golf and yacht club facilities, the access by the public to the golf during the week, the beach fronts and restaurant cafes and landscaping in the area. Moreover public services such as fire stations, ferry service, police station, water sewage and cleaning etc... were all provided by the developer (as opposed to by Government) from scratch. If there were no flexibility allowed by Exco and, the MacLehose and subsequent Administrations, the development would not have been commercially viable and would not have been anywhere near the success it is today.
19. It is easy with the benefit of hindsight now for people to make comments about what could have been done better. While I was Secretary of the NT, the original developer went into liquidation and Hong Kong was not the financial centre it is now but was emerging out of the recessions of the late 1960's. The Administration under Lord MacLehose encouraged dynamic and innovative ideas and projects which have been extremely successful.
20. At the relevant time, while I was Secretary for the NT, I had no better or worse relations with developers and other tycoons than other senior officials then and now. To show my lack of closeness, I was not asked to be a director (albeit an independent non-executive director) of the

Discovery Bay developer until 2000, some 13 years after my retirement as Chief Secretary: a very long time after I left Government.

21. Of the New Territories Administration which oversaw the massive development of the NT in those days, I can only say, in conclusion, that they have done a good job for Hong Kong. As is inscribed on Sir Christopher Wren's tomb in St. Paul's Cathedral in London, 'If you are looking for a memorial, look around you'.

xxx

OS

The
question arises whether, in view of the initial
EXCo approval in 1976 and the potentially
~~substantial~~ changes now contemplated, EXCo
approval need be sought at this stage. I would
think probably not but would be grateful for
your advice.



(J.R. Todd)
SLW
17/10/85



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10 January 2005

來函編號 Your Ref. CB(3)/PAC/R43

Clerk, Public Accounts Committee
Legislative Council Secretariat
Legislative Council Building
8 Jackson Road, Central
Hong Kong
(Attn: Ms Miranda Hon)

Dear Ms Hon,

**The Director of Audit's Report on
the results of value for money audits (Report No. 43)
Chapter 6: Grant of land at Discovery Bay and Yi Long Wan**

Thank you for your letter of 6 January 2005 requesting for information regarding Part 2 of the letter of 5 January 2005 from Sir David Akers-Jones on "Replies to Specific Items". I set out the information as follows:

The Committee would like to know whether there was a drastic slump in the property market in the period around 1977

- (a) Audit does not have information regarding whether there was a "drastic slump" in the property market in the period around 1977. Nevertheless, according to the "Estimates of Revenue and Expenditure for the year ending 31st March 1979", it was mentioned that there was an economic recession in 1975-76 and continuing recovery during 1976-77.

The Committee would like to know where the reasons have been extracted from

- (b) The reasons as stated in paragraph 2.14 of the captioned Audit Report were extracted from a minute dated 11 November 1977 in a Lands Department's file. The minute was written by the then Secretary for the New Territories to the then Principal Government Land Agent.

A Chinese translation of this letter will be forwarded to you shortly.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Peter K O Wong', written over a vertical dashed line.

(Peter K O Wong)
for Director of Audit

c.c. Secretary for Housing, Planning and Lands
Secretary for Financial Services and the Treasury
(Attn: Mr Manfred Wong)
Director of Lands