

A. Introduction

The Committee's Report

The Audit Commission ("Audit") conducted a value for money audit on the Direct Subsidy Scheme ("DSS") covering the administration and supervision of the scheme and the governance and administrative matters of DSS schools. The Committee noted that Audit had selected four DSS schools for field audits in order to obtain a better understanding of the operation of schools under the DSS. Apart from visiting four schools, Audit had also reviewed all the records of the Education Bureau ("EDB") on DSS schools. Such records included the register of school managers, school annual plans, development plans, audited financial statements, service agreements and tenancy agreements, etc. The review carried out by Audit at the EDB covered all DSS schools.

2. Audit's findings were contained in two separate chapters of the Director of Audit's Report No. 55 ("Audit Report"), i.e. "Administration of the Direct Subsidy Scheme" (Chapter 1) and "Governance and administration of Direct Subsidy Scheme schools" (Chapter 2).

3. The Committee held four public hearings on 29 November 2010 and 2, 13 and 20 December 2010 respectively to receive evidence on the findings and observations in the above two chapters of the Audit Report.

4. The Committee's Report sets out the evidence gathered by the Committee which is relevant to the issues identified in the above two chapters of the Audit Report and further revealed at the public hearings, as well as the Committee's conclusions and recommendations on those issues. The Report is divided into the following parts:

- A. Introduction;
- B. Service agreement with school sponsoring body;
- C. Service agreement with incorporated school governing body;
- D. School fee remission/scholarship schemes;

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- E. Revision of school fees;
- F. Financial management;
- G. Admission process;
- H. Monitoring school performance;
- I. Direct subsidy scheme subsidy;
- J. International schools in the direct subsidy scheme;
- K. Human resource management;
- L. General administration and other governance issues; and
- M. Conclusions and recommendations.

Disclosure of the identity of and information on the DSS schools studied in the Audit Report

5. Since the publication of the Audit Report, the issues relating to DSS schools as identified by the Director of Audit had aroused wide public concern and there had been public speculation about the identity of the schools examined by Audit. To prepare for the public hearings, the Committee requested the EDB to provide it with the names of the four DSS schools which had been visited by Audit and their irregularities. In view of the public concern over the matter, the Committee also made clear to the EDB that it did not have any objection to the bureau's making public the information sought by the Committee.

6. In his letter of 23 November 2010 in *Appendix 9*, **Mr Michael SUEN, Secretary for Education**, informed the Committee that:

- the EDB was mindful of the agreement between the Committee and the Administration with respect to the disclosure of information, as set out in the Financial Circular No. 2/2010 that "during the period between the tabling of the report in the Legislative Council ("LegCo") and the public hearings, any public debate on the issues to be further investigated should be avoided by both sides as far as possible so as to ensure that the

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Public Accounts Committee can carry out public hearings smoothly and in a fair manner and that we should refrain from initiating any publicity to counter the Audit findings.";

- with the above understanding, the EDB set out in Annex A of his letter the information sought by the Committee, on the basis of the information provided by Audit, for the Committee's internal reference before the public hearings commenced on 29 November 2010;
- the Audit Report involved not only the four schools visited by Audit but also all DSS schools in general. The EDB considered it more appropriate to provide information relating to all DSS schools covered in the Report, rather than singling out the four schools concerned. The EDB believed that the availability of such information would facilitate a comprehensive and fair discussion of the issues involved. The information covering all DSS schools studied in the Audit Report, on the basis of the details provided by Audit, was in Annex B of his letter; and
- as the EDB was the subject of the audit, it would respond to issues relating to the findings of the Audit Report at the Committee's public hearings. It was therefore of the view that the disclosure of the sought information on individual DSS schools to the public at that juncture might undermine the previous agreement between the Committee and the Administration (as set out in the Financial Circular No. 2/2010) and inevitably encourage public debate on issues relating to the four schools highlighted in the Audit Report. This would also not be just and fair to the schools concerned. However, if the Committee was of the view that the sought information could be disclosed to the public, it was prepared to do so accordingly.

7. After considering the Secretary for Education's response, the Committee wrote to him on 24 November 2010 stating that:

- the Committee had carefully reviewed the agreement between it and the Administration, which was reflected in the Financial Circular No. 2/2010, and the issues raised in the Audit Report. The Committee considered that the identity of the schools *per se*, although closely related to those issues, was not an issue relevant to the audit findings. A proper disclosure of the names of the schools concerned by the

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Administration should not undermine the agreement between the Committee and the Administration; and

- having considered all relevant circumstances, the Committee was of the view that the Secretary ought to make public the information provided in his letter of 23 November 2010.

8. The **Secretary for Education** released to the public the information on all DSS schools reported to have irregularities, as set out in Annex B of his letter of 23 November 2010, in the evening of 24 November 2010.

Declaration of interests and opening remarks

9. At the Committee's first public hearing on the Audit Report held on 29 November 2010, **Hon Cyd HO Sau-lan** declared that Ms Ada WONG, who was the School Supervisor of a DSS school named the HKICC Lee Shau Kee School of Creativity, was her friend and had sponsored her in the LegCo elections held in 2008.

10. **Hon Paul CHAN Mo-po** declared that his daughter was studying in an international school. In addition, he was currently a Council Member of Caritas-Hong Kong ("Caritas") and had been the Chairman of Friends of Caritas. Caritas operated DSS schools but he was not involved in those schools.

11. **Hon Ronny TONG Ka-wah** declared that his son had studied in the Diocesan Boys' School.

12. **Mr Benjamin TANG, Director of Audit**, and the **Secretary for Education** made opening remarks at the public hearing on 29 November 2010. The full texts of their remarks are in *Appendices 10 and 11* respectively.

B. Service agreement with school sponsoring body ("SSB")

Requirement to enter into service agreement

13. The Committee referred to the Secretary for Education's opening remarks in which he said that the EDB was of the view that the current DSS school system and its monitoring mechanism were working well, and the majority of the issues raised in the Audit Report were operational and technical in nature. The Secretary also said that the EDB would take timely and proper follow-up measures with individual schools found to have irregularities. The Committee, however, pointed out that the Audit Report had revealed a lot of cases of non-compliance with the EDB's guiding principles or requirements, some of which were serious, and that the EDB had failed to ensure timely rectification of those problems.

14. The Committee cited as an example the problems relating to the service agreements between the EDB and the SSBs of DSS schools ("SSB Service Agreements"). According to paragraphs 3.2 to 3.4 of Chapter 1 of the Audit Report, from the 2000-2001 school year¹ onwards, the SSB of a school joining the DSS is required to enter into an SSB Service Agreement with the EDB upon admission to the DSS. In addition, the SSBs of schools are required to enter into an SSB Service Agreement upon being allocated with school premises, or receiving capital subvention exceeding \$21 million. Of the 72 DSS schools, 57 are required to enter into an SSB Service Agreement with the EDB.

15. Paragraph 3.5 of Chapter 1 reported that up to 30 June 2010, five (9%) of the 57 schools still had not entered into an SSB Service Agreement with the EDB, and the signing of the agreement had been overdue for about 18 months to eight years. Paragraph 3.11 further revealed that of the 52 schools which had entered into the agreements, there were delays ranging from less than one year to exceeding seven years in respect of 26 (50%) schools.

16. Against the above background, the Committee queried whether the EDB:

- had not performed its monitoring role over DSS schools effectively to ensure that their governance, accountability and transparency were up to the required standard and public expectation; and

¹ Unless otherwise specified, all years mentioned hereinafter refer to school years which start on 1 September of a year and end on 31 August of the following year.

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- had not attached sufficient importance to the gravity of the problems in the administration of DSS school.

17. The **Secretary for Education** responded that:

- a lot of the problems identified by Audit had arisen due to historical reasons. When the DSS was first introduced, in order to encourage more schools to join the scheme, the Administration had adopted a more lenient and flexible approach by allowing some schools which had initially met the admission criteria to join the DSS first and then fulfill the relevant requirements gradually. At that time, it was thought that the schools would be able to complete the admission requirements within a short time. However, it turned out that things were not as easy as previously believed;
- regarding the signing of SSB Service Agreement, it was originally anticipated that the EDB would be able to settle the matter in one or two years' time, but as it turned out, the matter had dragged on for eight years. This was mainly because the schools had a long history and had their own incorporation ordinances. The schools argued that some of the terms and conditions of the SSB Service Agreement were not consistent with the provisions in their incorporation ordinances and would infringe their rights;
- some schools also encountered legal problems with the requirement to acquire non-profit-making status and it took a long time to resolve the conflicts with them;
- to prevent the occurrence of similar situation, all schools joining the DSS from 2007 onwards must have met all the criteria before they were formally admitted; and
- the EDB attached importance to the monitoring of DSS schools and accepted the criticism and recommendations in the Audit Report. In fact, some of the problems mentioned in the report had been discovered by the EDB before the audit review. For example, it was the EDB which had found out that a school had purchased properties improperly and it had demanded the school to rectify the problem over the years. But the school repeatedly ignored the requests. The EDB had been

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ineffective in following up the cases of non-compliance identified. The EDB was toothless towards non-compliant schools.

18. Given that the problem relating to the signing of SSB Service Agreements by the five schools had dragged on for a long time, the Committee enquired about the actions that the EDB had taken during the period to resolve the matter, and whether it had contemplated taking punitive measures, such as issuing advisory or warning letters, against the schools concerned.

19. The **Secretary for Education** and **Mr Raymond WONG, Permanent Secretary for Education**, responded that:

- of the five schools, currently only three schools, i.e. Schools C, D and E, had not yet entered into SSB Service Agreements with the EDB, while the other two had already done so;
- the EDB's discussion with the three schools about the terms and conditions of the SSB Service Agreements began after they had been admitted to the DSS. As they had disagreements with the EDB over some of the terms and conditions of the agreements due to their unique historical circumstances, the EDB endeavoured to find solutions that were acceptable to both parties. Progress had been made over the years. The schools were indeed very cooperative and had reached consensus with the EDB over many issues. It was therefore not appropriate to issue advisory or warning letters to the schools or take other punitive actions against them; and
- following the EDB's requirement that all schools joining the DSS from 2007-2008 must sign the SSB Service Agreements before they were admitted to the scheme, there would be no question of DSS schools negotiating the terms and conditions of the service agreements with the EDB after admission.

20. The Committee further asked:

- about the details of the terms and conditions which had been disagreed by Schools C, D and E and the main point of contention; and

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- the actions that had been taken by the EDB to expedite the signing of the SSB Service Agreements, as well as the latest position of the matter.

21. In Annex L of his letter of 17 December 2010 (in *Appendix 12*), the **Secretary for Education** stated that:

- Schools C, D and E were aided schools with their own incorporation ordinances before joining the DSS. The three schools did not accept the terms in the draft SSB Service Agreement² relating to the school governance structure. The draft agreement stipulated that the School Management Committee ("SMC") should comprise the principal, representatives from the SSB, parents and teachers, other community members or professionals and, where appropriate, alumni. The schools did not agree that they should modify their governance structure, which was already stipulated in their respective ordinances, following their admission to the DSS. They considered that they should be allowed to follow their proposed governance composition at the time of their application and approval for joining the DSS. Having regard to the unique circumstances, the EDB had, having sought the advice of the Department of Justice ("DoJ"), agreed to revise the draft agreement allowing them to be managed and operated under their original governing framework;
- two of the above three schools (i.e. Schools C and E) were also concerned about a clause in the SMC Service Agreement that they were required to transfer to the Government at the SMC's own cost and expense all assets and inventories purchased with government subsidies or funds generated by the school upon termination of the service agreement. They disagreed with the clause because owing to their long history, they had many assets and inventories acquired prior to their turning to the DSS which, in their view, should not be transferred to the Government upon termination of the SMC Service Agreement. The EDB had been liaising with and reminding the schools to expedite the signing of the agreements by sending reminders and holding meetings. In September 2010, the EDB agreed to take into account their unique historical circumstances and intended to refine the related clause on the transfer of assets to the Government upon the termination of the SMC Service Agreement. Advice from the DoJ was being sought. Once

² From the 2000-2001 school year onwards, each school joining the DSS is required to sign both the SSB Service Agreement and the School Management Committee Service Agreement.

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the relevant revision of the SMC Service Agreement was agreed by both parties, the SSB Service Agreements would be signed; and

- as for the remaining school (i.e. School D), its SSB agreed in August 2010 to sign the SSB Service Agreement subject to some minor amendments to a few clauses. Advice from the DoJ on the SSB's proposed revisions was being sought and the service agreement would be signed as soon as practicable.

22. Regarding the Secretary for Education's statement that the EDB was toothless towards non-compliant schools, the Committee referred to paragraph 1.18(c) and (d) of the Chapter 1 of the Audit Report which outlined a range of administrative and punitive measures that could be taken by the EDB against such schools, including issuing advisory or warning letters, appointing school managers to the SMC/Incorporated Management Committee ("IMC"), and withdrawing the subsidy payable to the school with a resultant loss of DSS status. The EDB might even terminate the SMC/IMC Service Agreement at any time before the expiry of the agreement.

23. To ascertain whether the EDB had made effective use of the existing administrative and punitive measures in dealing with non-compliant schools, the Committee asked whether the EDB had issued any advisory or warning letters to DSS schools in relation to the malpractices and irregularities highlighted in the Audit Report.

24. **The Secretary for Education and Mrs Michelle WONG, Deputy Secretary for Education**, responded that:

- the EDB had all along adopted a lenient and tolerant attitude towards non-compliant schools and allowed them more time for rectification of identified problems because it did not want to affect the schools' teaching and learning, particularly the interest of students;
- very often the EDB could bring about improvement through various means, such as giving verbal advice, and did not need to issue warning letters. When the EDB discovered problems through checking of the schools' audited accounts or through the EDB's audit inspections, it would issue management letters to the schools concerned to demand

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rectification. The EDB would take into consideration different factors, such as the explanation provided by the schools, the gravity of the irregularities and the schools' willingness to rectify the mistakes, and exercise professional judgement in deciding the appropriate follow-up actions; and

- so far the EDB had issued warning letters in respect of two DSS schools mainly due to administrative malpractices of the schools. Regarding those malpractices and irregularities relating to the governance and administrative matters of DSS schools which were covered in Chapter 2 of the Audit Report, the EDB had issued a number of advisory letters.

25. In Annex D of his letter of 10 December 2010 (in *Appendix 13*), the **Secretary for Education** informed the Committee of the number of advisory letters that had been issued to DSS schools by the EDB in the past three years from 2007-2008 to 2009-2010 and the main content of the letters. Regarding the mechanism on the issuance of advisory and warning letters, the **Secretary for Education** explained that:

- on detecting any irregularities or non-compliances committed by schools through EDB's audit inspections or examination of the audited accounts submitted by schools annually, EDB would issue advisory letters to the schools concerned and demand rectification;
- advisory letters would also be issued to the schools which failed to follow other requirements of the EDB, such as those concerning the submission of audited accounts and signing of the SSB/SMC/IMC Service Agreements, etc; and
- for schools with serious management problems and which failed to rectify the non-compliance and irregularities despite repeated advice or reminders, a warning letter would be issued demanding the schools to rectify the non-compliance and irregularities. The warning letter would state clearly the relevant consequences as prescribed in the Education Ordinance (Cap. 279) (e.g. appointing school managers to the SMC by the EDB) in the event that the school failed to rectify the situation within the specified period.

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Compliance with service agreement

Incorporation of school governing body

26. Paragraphs 3.16 and 3.17 of Chapter 1 of the Audit Report revealed that although under the SSB Service Agreement, a DSS school should form an SMC before it commenced operation, 18 DSS schools formed their SMCs only after they had commenced operation. The delays ranged from two days to about nine years, with an average of three years. Moreover, up to June 2010, three DSS schools, which commenced operation in 2004-2005 to 2008-2009, had not incorporated their school governing bodies. The Committee queried why the EDB had not enforced the requirements of the SSB Service Agreement.

27. The **Secretary for Education** said that experience showed that some new schools could not follow the required timeframe stipulated in the SSB Service Agreements to form their SMCs or incorporate their school governing bodies, etc. Hence, the EDB had allowed them a longer period of time, i.e. one year, to complete the relevant procedures to meet the requirements.

Tax exemption status of SMC/IMC

28. According to the SSB Service Agreement, the SSB should ensure that the SMC/IMC will acquire a tax exemption status under the Inland Revenue Ordinance (Cap. 112) ("IRO"). As stated in paragraph 3.19 of Chapter 1 of the Audit Report, up to 30 June 2010, the SMCs/IMCs of three DSS schools that commenced operation in 2004-2005 to 2008-2009 had not yet acquired the tax exemption status under the IRO. The Committee asked:

- why the SMCs/IMCs of the three schools had not yet acquired tax exemption status; and
- when the EDB became aware that the SMCs/IMCs had not acquired tax exemption status and the actions that had been taken to ensure that they would acquire the status without delay.

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29. In Annex B of his letter of 8 December 2010 (in *Appendix 14*), the **Secretary for Education** explained the reasons for the long time taken by the SMCs/IMCs of the three schools to acquire tax exemption status. The updated position of the matter, as provided by the **Director of Audit** (in his letter of 27 January 2011 in *Appendix 15*), the **Secretary for Education** (in his letter of 28 January 2011 in *Appendix 16*), and the EDB at the end of January 2011, were also set out below:

First school

- the school turned into a DSS school in September 2008. The person who assisted in drafting the Memorandum and Articles of Association ("M&AA") of the SMC worked on a voluntary basis and thus spent a long time studying and revising the related documents. Also, the SMC had spent much time on discussing and amending the M&AA at its meetings. The EDB had all along maintained dialogue with the school, reiterating the requirement for the SMC to conclude the SMC Service Agreement by 31 August 2009;
- the EDB had also been communicating with the school with regard to its establishment of an incorporated SMC and acquisition of the tax exemption status. According to the information provided by the school on 9 August 2010, the SMC of the school had acquired the tax exemption status with retrospective effect from 7 June 2010. The SMC subsequently signed the SMC Service Agreement with the EDB on 10 September 2010;

Second school

- the school (a primary school) turned from an aided school to a DSS school on 1 September 2008. The EDB had all along maintained close contact with the school with regard to the establishment of an IMC, signing of the service agreement and application for the tax exemption status;
- regarding the SMC Service Agreement, the SSB requested that the alumni manager(s) of the (primary) school be nominated by the Alumni Association of the secondary section of the school, instead of by the Alumni Association of the (primary) school. The EDB and the SSB had quite a number of discussions on the issue, and hence the progress

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of completing the drafting of the M&AA and acquiring tax exemption status by its SMC was delayed;

- the SSB finally accepted the EDB's suggestion that the alumni manager must be an alumnus of the school. The school completed further amendments to the M&AA of the SMC in November 2010, and filed an application to the Inland Revenue Department for tax exemption status of the SMC in early January 2011;

Third school

- the school commenced operation on 1 September 2004. Consensus could not be reached on the draft SSB Service Agreement since the SSB had reservation about the conditions related to the SMC therein. After a series of communication and negotiation, the SSB executed the SSB Service Agreement with the Government on 15 July 2009;
- in the course of the negotiation on the SSB Service Agreement, the EDB had maintained contact with the SSB for the signing of the SMC Service Agreement. The EDB had also urged it to complete the preparation of the M&AA for incorporation and application for tax exemption status; and
- after the conclusion of the SSB Service Agreement, the school indicated that it was drafting the M&AA and was committed to completing the task within 2009-2010. The EDB had liaised with the school many times and urged it to expedite. Finally, the SMC was incorporated under the Companies Ordinance (Cap. 32) on 9 November 2010. The school informed the EDB on 9 December 2010 that tax exemption status had been granted by the Inland Revenue Department with retrospective effect from 9 November 2010.

Director of Audit's access right to records and accounts

30. According to paragraph 3.32 of Chapter 1 of the Audit Report, the current standard SSB Service Agreement included a clause to provide the Director of Audit with the right of access to the records and accounts of the DSS schools. However, of the 52 SSB Service Agreements signed, only 34 included such a clause. The Committee asked why the EDB had not enforced the requirement in respect of the

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other 18 schools and about the action that the EDB would take to address the situation.

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

- the SSB Service Agreements of the 18 schools concerned were signed at an earlier date and did not contain the clause allowing the Director of Audit the access right to the schools' records and accounts; and
- the problem had already been rectified. In the EDB Circular No. 12/2010 issued in November 2010, the EDB had required all DSS schools to keep proper administrative and financial records and provide them for examination by the Director of Audit when required. The requirements in the circular were also applicable to the 18 schools.

32. As requested by the Committee, the **Secretary for Education** provided a copy of the EDB Circular No. 12/2010 in Annex C of his letter of 8 December 2010 (in *Appendix 14*).

Measures to enhance the monitoring and supervision of DSS schools

33. In view of the widespread compliance problems in DSS schools, the Committee asked about the measures that the EDB would take to enhance its monitoring and supervision of DSS schools.

34. The **Secretary for Education** informed the Committee, in Annex E of his letter of 10 December 2010 (in *Appendix 13*), that:

- the EDB had conducted briefing sessions for DSS schools in June 2010 with a view to enhancing the daily operation and management of the schools;
- the EDB recapitulated in the EDB Circular No. 12/2010 on "Use of Non-government Funds in Direct Subsidy Scheme Schools", issued on 5 November 2010, the prevailing rules and regulations as well as guidelines on the proper use of non-government funds for compliance or reference by DSS schools as appropriate;

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- the EDB had strengthened the communication with the Hong Kong DSS Schools Council ("DSS Schools Council") and provided support for its working group on enhancement of internal control in DSS schools, which was newly established in August 2010;
- more extensive checking would be conducted through the audits of selected schools by the School Audit Section; and
- noting the observations and recommendations of the Public Accounts Committee and Audit, the EDB would step up efforts to improve the governance of DSS schools. To this end, the Secretary for Education had tasked the Permanent Secretary for Education to consider a review of the governance framework, internal control and enforcement mechanism and financial management of DSS schools. A Working Group would be set up in early January 2011 under the EDB with inputs from the DSS and academic sector, as well as from relevant professionals experienced in governance, financial management and related areas to take forward the review and address the issues raised by the Public Accounts Committee and Audit.

35. According to the information provided by the EDB at the end of January 2011, the Working Group had already been set up. Background briefing sessions would be organised for members in February 2011 to enhance their understanding of the origin and development of the DSS policy, the current regulatory regime, wide diversity in the background of DSS schools, and the observations made by Audit and during the public hearings of the Public Accounts Committee.

36. Noting that the EDB had issued a large number of circulars to DSS schools, the Committee asked how the EDB could ensure that the schools would comply with the guidelines/requirements therein.

37. The **Permanent Secretary for Education** replied that before issuing a new circular, the EDB would review and consolidate the existing ones. It would also consult the DSS Schools Council on the contents of the circulars. In fact, the EDB had maintained good communication with the DSS Schools Council through regular meetings. The EDB also expected the schools to fulfil their responsibility to comply with the requirements and guidelines set out in the circulars.

C. Service agreement with incorporated school governing body

38. Under the DSS, the SMC/IMC of a DSS school should enter into an SMC/IMC Service Agreement with the EDB within one year after the school has commenced operation. Paragraphs 4.4 and 4.5 of Chapter 1 of the Audit Report revealed that 53 DSS schools were required to enter into SMC/IMC Service Agreements by June 2010. However, as at 30 June 2010, 13 of them had not signed the agreements, including three which subsequently signed the agreements in July and August 2010.

39. According to the SMC Service Agreement, the composition of the SMC shall comprise the principal, representatives from the SSB, parents, teachers, other community members/professionals and, where appropriate, alumni. The Education Ordinance prescribes that an IMC should compose of SSB managers, the principal, teacher managers, parent managers, alumni managers and independent managers. Yet, paragraphs 4.12 and 4.13 of Chapter 1 of the Audit Report revealed that the composition of some IMCs and SMCs did not comply with the requirements stipulated in the Education Ordinance and the SMC Service Agreements respectively.

40. In view of the widespread compliance problems, the Committee doubted the effectiveness of the EDB's supervision of DSS schools to ensure that they would put in place a proper governance structure.

41. The **Secretary for Education** and the **Permanent Secretary for Education** responded that some of the problems were in fact discovered by the EDB and the schools had subsequently provided explanations for the non-compliance. For instance, for the two IMCs that did not have the principal, the principals of the schools were appointed on an acting basis pending completion of their Certification for Principalship. However, the EDB admitted that there was room for improvement in its supervision of DSS schools. On the other hand, the EDB considered that it was the schools' responsibility to ensure that the composition of their SMCs/IMCs was in compliance with the requirements of the SMC Service Agreements and the Education Ordinance.

D. School fee remission/scholarship schemes

School fee income set aside for fee remission/scholarship schemes

42. According to paragraph 3.2 of Chapter 2 of the Audit Report, DSS schools are required to administer a fee remission/scholarship scheme in order that students will not be deprived of the chance to study at DSS schools solely because of their inability to pay school fees. The Committee noted with concern the following audit findings:

- 22 DSS schools had not set aside the required amounts of school fee income for the purpose of their fee remission/scholarship schemes;
- contrary to the EDB's requirement, two of the four DSS schools visited by Audit had not mentioned their fee remission/scholarship schemes in their prospectuses. The other two DSS schools had not provided full details of their schemes (e.g. the eligibility criteria and the maximum percentage of fee remission) in their prospectuses;
- only 47 (65%) DSS schools had mentioned on their websites that fee remission/ scholarship schemes were available to students, and only 23 of these 47 schools had provided details of the schemes;
- the eligibility criteria of the fee remission schemes offered by two DSS schools were less favourable than the government financial assistance schemes to students; and
- in 14 DSS schools, the utilisation of their fee remission/scholarship schemes was 50% or less.

43. The Committee pointed out that the fee remission/scholarship schemes administered by DSS schools served the important function of ensuring that not only students from well-off families would have the choice of studying in DSS schools, but students from grass-roots families would also have a fair chance of being admitted. In the light of the above audit findings, the Committee questioned whether:

- the low utilisation rate of the fee remission/scholarship schemes in some schools was attributable to parents not being informed of the availability of the schemes;

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- needy parents had been discouraged from applying for their children's admission to DSS schools due to lack of information on the schemes; and
- the EDB was aware of some schools' non-compliance with its requirements on the schemes, and how the EDB could ensure that DSS schools would not become "noble schools" which only served the rich.

44. The **Secretary for Education** responded that:

- the EDB's major concern in monitoring DSS schools was the quality of education provided by the schools. Although the EDB should monitor the schools' compliance with its requirements, this was not, and should not, be the focus of the EDB's supervision;
- the EDB did not perceive any serious problem with the fee remission/scholarship schemes administered by DSS schools. There were channels for needy DSS school students to apply for fee remission/scholarship. The utilisation rate of the schemes in different schools varied with individual schools' circumstances. For some schools, the utilisation rate was low because their students were rich and did not need financial assistance, while the utilisation rates for some other schools were high;
- it was not true that all DSS schools charged high school fees. Some schools charged very low fees. It was also a misconception that DSS schools were the best schools in Hong Kong and students who could not study in such schools could only attend inferior ones. In fact, a lot of good schools had not joined the DSS; and
- the fundamental principle of establishing the DSS was to inject diversity into Hong Kong's education system and increase parental choice. DSS schools provided parents with a viable alternative to government and aided schools. To meet their operational and developmental needs, DSS schools were allowed greater flexibility in various areas, including school management, resources deployment, staff appointment, curriculum design, student admission and fees collection, etc. so that they could cater for the diverse needs of their students in a more speedy and responsive manner.

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45. The **Permanent Secretary for Education** supplemented that:

- the EDB considered the fee remission/scholarship schemes administered by DSS schools an important element of the DSS. The EDB had not taken the problem lightly and had strictly enforced the relevant requirements; and
- when the EDB discovered that a school had not set aside sufficient amount of school fee income for fee remission/scholarship scheme purpose, the EDB would follow up with the school and request it to make good the shortfall. When a DSS school's reserve for the fee remission/scholarship scheme accumulated to an amount that exceeded half of its annual school fee income, the EDB would require the school to submit a deployment plan on how the reserve could be more effectively deployed, such as reducing the school fee and subsidising students' expenses on books, stationery or extra-curricular activities. If the situation warranted, the EDB would also discuss with the school the feasibility of relaxing the eligibility criteria for the scheme.

46. The Committee queried whether the widespread non-compliance problems of DSS schools were attributable to systemic loopholes or human errors. According to the EDB's organisation chart provided in Annex C of the Secretary for Education's letter of 25 November 2010 (in *Appendix 17*), the responsibility for monitoring DSS schools were shouldered by different subject divisions of the EDB headed by the relevant Principal Assistant Secretaries. It appeared to the Committee that there was no dedicated high-level body in the EDB to oversee the administration of the DSS and the schools' compliance with the DSS requirements. To ascertain if this was the case, the Committee asked:

- whether there was a dedicated body in the EDB to take charge of the implementation of the DSS and if there was, who headed such body;
- how the EDB's subject divisions would deal with the malpractices and irregularities identified from the annual audited accounts submitted by DSS schools, and whether they would report serious cases, such as when a school committed the same malpractice in successive years, to higher level staff; and
- whether the problem of under-provision of some DSS schools' fee remission/scholarship schemes had been reported to high-level staff in

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the EDB, including the Permanent Secretary for Education and the Secretary for Education.

47. The **Deputy Secretary for Education** responded that:

- the Task Force on DSS, set up in 2000, was responsible for overseeing the DSS. It met quarterly to review the policies and practices of the DSS, proposed criteria for DSS applications, and recommended DSS applications for approval. The Task Force was under her chairmanship, and its members included the representatives of relevant subject divisions of the EDB; and
- where necessary, the decisions made by the Task Force would be brought up to higher level staff such as the Permanent Secretary for Education, or other meetings of the EDB which were attended by more senior staff, for consideration, but those staff would not be invited to attend the Task Force's meetings.

48. The **Permanent Secretary for Education** said that:

- the annual audited accounts submitted by DSS schools each year would first be examined by the EDB's Finance Division, and the malpractices and irregularities identified would be referred to appropriate subject divisions for follow-up. The Finance Division would also report to him the overall results of its checking of the audited accounts every year, highlighting those matters which were considered more important. Such reports were not discussed by the Task Force on DSS, but at the directorate meetings of the EDB chaired by him. Staff of the Finance Division would make suggestions for improvement and take follow-up actions. Although the Secretary for Education was not a member of the directorate meeting, he would consult the Secretary when policy issues were involved; and
- as far as he could remember, the under-provision of fee remission/scholarship schemes was not considered a very serious problem in the past few years and had not been included in the Finance Division's reports to him. He was only aware of the matter after it had been raised by Audit.

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49. **Mrs Lily TSANG, Principal Assistant Secretary for Education (Finance)**, said that:

- in the course of examining the DSS schools' annual audited accounts each year, the Finance Division would check whether all schools had set aside in the year adequate provision for their fee remission/scholarship schemes, and hence the Finance Division would be able to identify schools which had not complied with the requirement. Such cases would be referred to the EDB's regional education offices ("REOs") for follow-up. If the problem still existed in the following year, the Finance Division would again inform the REOs for them to take action; and
- the EDB noted Audit's observations that the fee remission/scholarship schemes of five schools were not funded from school fee income, and 22 schools had not set aside the required amounts of school fee income for the purpose of their fee remission/scholarship schemes. In practice, the EDB allowed the schools to fund the schemes from sources other than school fees. Moreover, the EDB and Audit adopted different approaches to determining whether a school had set aside sufficient amount for the schemes. According to the EDB's assessment, less than 22 schools had under-provided for their fee remission/scholarship schemes.

50. **Mr Steve LEE, Principal Assistant Secretary for Education (School Development)**, added that upon receipt of referrals from the Finance Division, the REO staff would issue letters to the schools requiring them to make good the shortfall. Many schools would comply with the EDB's advice and rectify the mistake. However, there was a school which was found to have set aside inadequate provision for fee remission/scholarship scheme purpose in several years. The EDB had followed up by issuing a number of advisory letters, and recently a warning letter had also been issued.

51. To ascertain the Secretary for Education's involvement in the EDB's monitoring and supervision of DSS schools, the Committee asked the Secretary for Education:

- whether he was aware of the schools' non-compliance with the EDB's requirements on the fee remission/scholarship schemes before the matter was revealed by Audit;

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- whether the EDB staff would report to him serious cases of non-compliance and malpractices, such as a school's repeated disregard of the EDB's requests to set aside sufficient amount for its fee remission/scholarship scheme; and
- about the occasions on which he had been informed of the irregularities of DSS schools.

52. The **Secretary for Education** replied that:

- he did not have knowledge of the cases of non-compliance regarding DSS schools' fee remission/scholarship schemes as reported by Audit. The EDB staff would deal with different issues by different ways depending on their gravity and nature. For technical and operational issues, staff of the subject divisions could handle them without escalating to a higher level. But he would be involved when the situation warranted a review of the EDB's policy or system; and
- most of the DSS schools complied with the EDB's requirement and set aside sufficient amount for fee remission/scholarship scheme purpose. Some had even provided more money for the schemes than required. While some schools had under-provision, the interest of their students would not be affected as long as the amount reserved by the schools for fee remission/scholarship scheme purpose was sufficient to meet the need of all their students. This could be reflected by the low utilisation rate of some schools' fee remission/scholarship scheme.

53. Regarding the occasions on which he had been informed of the irregularities of DSS schools, the **Secretary for Education** informed the Committee at the public hearings and in his letter of 1 December 2010 (in *Appendix 18*) that the irregularities identified of DSS schools were normally dealt with at the appropriate level without bringing to him personally. However, he would be informed and would give steer in those cases with policy implications and public concern. According to the EDB's records available for the past three years, the Secretary for Education had been personally involved in the following two cases:

- the case in which an SSB subsequently gave up the operation of the Pegasus Philip Wong Kin School was brought to the Secretary's attention in May 2008. The SSB indicated its wish of giving up the

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operation of the school. There were then several discussions held at the Senior Directorate Meetings of the EDB from May to November 2009 focusing on the related follow-up actions; and

- the other case that had been brought to the Secretary for Education's attention was the one concerning the Hong Kong Chinese Union ("HKCCCU") Logos Academy, which was covered in the Audit Report. From 10 November to 1 December 2010, the case had been covered, among others, in a total of six working meetings with the Secretary over the Audit Report. The Secretary was informed that a warning letter was issued to the school on 12 November 2010 and that the EDB was contemplating the appointment of members to the SMC of the school having regard to its irregularities and malpractices.

54. The Committee noted that the school which had repeatedly failed to set aside adequate provision for fee remission/scholarship scheme purpose in several years was the HKCCCU Logos Academy. As reported in paragraph 3.4 of Chapter 2 of the Audit Report, although the school had been reminded time and again by the EDB since September 2005 to set aside the required amount of school fee income for its fee remission/scholarship scheme, no action had been taken by the school up to June 2010. The Committee also noted that the underprovided amount of this school in 2008-2009 was as high as \$3 million. Given that the EDB had the power to withdraw the subsidy payable to a school with a resultant loss of DSS status, the Committee asked:

- why the EDB had not taken more rigorous actions to demand the school's early rectification of the irregularity; and
- about the actions that had been taken by the EDB since September 2005 to ensure that the school would comply with its advice to make good the shortfall, and the school's response.

55. In Annex A of his letter of 11 December 2010 (in *Appendix 19*), the **Secretary for Education** stated that:

- the school was operated in a DSS through-train mode. Its primary and secondary sections started operation in September 2002 and September 2003 respectively;

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- through checking the school's 2002-2003 audited accounts in the 2004-2005 school year, the EDB started to find out that the school did not set aside the required amount of school fee income for its fee remission/scholarship scheme. The EDB advised the school for rectification on 8 September 2005. However, the EDB found the same malpractice through checking the school's audited accounts in the subsequent four years. Hence, the EDB wrote to the school a number of times in February 2007, October 2007, November 2008, September 2009 and August 2010 to request necessary rectification; and
- the school finally replied in September 2010 saying that it had set aside the required amount of fee remission. Although the school had committed to setting aside the required amount of fee remission, it had not rectified other malpractices identified. Hence, the EDB issued a warning letter to the school on 12 November 2010. In response, the school gave a reply to the EDB dated 23 November 2010. The EDB would continue to liaise closely with the school to follow up the issues.

56. Referring to the remarks of the Principal Assistant Secretary for Education (Finance) that different approaches were adopted by the EDB and Audit for determining whether a school had provided sufficient amount for fee remission/scholarship scheme purpose, the Committee queried:

- why there was such difference and why the EDB had not amended its criteria concerned if it considered that schools should be given flexibility in funding their fee remission/scholarship schemes; and
- about the difference in the criteria adopted by the EDB and Audit.

57. In Annex A of his letter of 11 December 2010 (in *Appendix 19*), the **Secretary for Education** stated that:

- for the purpose of running a fee remission/scholarship scheme, DSS schools are required to set aside:
 - (a) 10% of the school fee income; or

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(b) 50% of the amount of school fee which exceeds two-thirds of the DSS subsidy rate, if the school fee is between the range of two-thirds, and two and one-third of the DSS subsidy rate,

whichever is the higher; and

- in the course of examining the annual audited accounts of DSS schools each year, the EDB would check whether all schools had set aside in the year concerned a provision for fee remission/scholarship scheme not less than the minimum 10% of the school fee income. For those provisions above 10%, the EDB counted on DSS schools' external auditor to check if schools complied with the requirements. If there was any shortfall, the REOs would follow up with the schools concerned and request them to rectify and make good the shortfall. In fact, the EDB had recently conducted a detailed check on the internal records of the 10 schools which satisfied the criteria under item (b) above and were among the 22 schools as identified by Audit to have made inadequate provision for fee remission/scholarship scheme. Out of the 10 schools, only one had not complied with the requirement due to misinterpretation.

58. The **Secretary for Education** further explained in the same letter that:

- the EDB noted that in applying the criteria under item (b) in paragraph 57 above in its calculations, Audit had used the 2008-2009 "projected" DSS subsidy rate and the "snapshot of enrolment figures" as of 30 September 2008 as the basis, whereas the EDB's assessments were made with reference to the 2008-2009 "finalised" DSS subsidy rate and actual enrolment figures adopted by most schools;
- noting that different schools might have adopted different accounting practices having regard to their unique circumstances, the EDB adopted a practical approach to assessing whether the requirement of setting aside sufficient financial provision for the purpose of fee remission/scholarship scheme had been met;
- in so doing, the EDB bore in mind the objective of ensuring adequate provision for needy students. Hence, while ensuring compliance with the requirement, the EDB allowed some reasonable variation in respect of the account to which fee remission/scholarship scheme was charged.

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Specifically, apart from direct deduction of the required provision from the school fee income, it would also allow schools to make alternative arrangements to set aside the required amount from other funding sources, including but not limited to accumulated reserve balance, bursaries as well as scholarship /fee remission expenses paid during the year from the Income and Expenditure Account. In addition, it also accepted schools using actual school fees paid by students (i.e. after fee remission) for setting aside sufficient amount as required under the criteria under item (a) or (b) in paragraph 57 above; and

- the EDB also allowed under-provision of an insignificant amount, say 0.01% (in one case the difference was only \$10 and in another it was around \$1,000 in 2008-2009).

59. Regarding the findings based on the EDB's and Audit's assessments, the **Secretary for Education** stated that:

- according to Audit's findings set out in Table 1 in paragraph 3.3(b) of Chapter 2 of the Audit Report, 22 DSS schools had under-provision for fee remission/scholarship scheme purpose in their 2008-2009 accounts in varying degrees ranging from \$1 to above \$1 million. Upon cross-checking with Audit's findings, the EDB found that 16 out of the said 22 DSS schools were considered to have made adequate provisions for fee remission/scholarship scheme purpose in their 2008-2009 accounts. This difference in assessment was all but one due to the reasons listed in paragraph 58 above;
- for the remaining six schools with under-provision of fee remission/scholarship scheme according to both the EDB's assessment and Audit's observation in its report, the EDB had already informed them and they had all agreed to top up funding in their 2009-2010 accounts to make good the shortfall. Of these six schools, three had not set aside the required amount for fee remission/scholarship scheme in 2006-2007, 2007-2008 and 2008-2009; and
- to avoid misunderstanding arising from different interpretations of the requirements on fee remission/scholarship scheme, the EDB undertook to refine the guidelines with a view to clarifying and standardising the practice.

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60. In respect of the three schools which had not set aside the required amount for fee remission/scholarship scheme in 2006-2007, 2007-2008 and 2008-2009, the **Secretary for Education** provided, in Annex A of his letter of 17 December 2010 (in *Appendix 12*), the actual amounts set aside by the schools and the amounts of under-provision in each of the three years, as well as the latest compliance situation.

61. The Committee also noted the following information, which was provided by the Secretary for Education in Annex A-1 of his letter of 11 December 2010 (in *Appendix 19*), on the 22 schools mentioned in Table 1 in Chapter 2 of the Audit Report:

- (a) the criteria for setting aside amount for fee remission/scholarship scheme purpose;
- (b) the annual school fee income in 2008-2009;
- (c) the actual amount of under-provision in 2008-2009 as per Audit's calculations;
- (d) the actual amount of under-provision in 2008-2009 as per the EDB's calculations;
- (e) the utilisation rate in 2008-2009 as per the EDB's calculations; and
- (f) the reasons for the discrepancies between (c) and (d).

Handling of the draft Audit Report

62. Noting the discrepancies between the findings of Audit and the EDB, the Committee pointed out that the EDB's approach might not be unreasonable. The Committee, however, queried why the EDB had not informed Audit of its usual approach for assessing DSS schools' provision for fee remission/scholarship scheme or its analyses of the problem of under-provision. It appeared to the Committee that if the EDB had clarified the matter and informed Audit of the actual situation when responding to the draft Audit Report, the panic among members of the public which was caused by DSS schools' alleged widespread non-compliance of the requirements on fee remission/scholarship scheme, might have been avoided and the schools would not have been subject to undue pressure. The Committee asked whether the EDB had communicated with Audit over the matter.

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63. The **Director of Audit** and **Mr POON Sui-cheung, Assistant Director of Audit**, responded that:

- Audit had not been informed of the EDB's approach for determining whether a school had met the requirements on fee remission/scholarship scheme. Audit's methodology was based on an EDB circular issued earlier. Audit considered that for budgeting purpose, it would be more appropriate to set aside the required amount based on the "projected" DSS subsidy rate and the enrolment figures at the beginning of a school year; and
- the draft Audit Report was sent to the EDB at the end of August 2010. A meeting was held with the EDB on 6 September 2010 to discuss the draft report. After modifying the draft report in the light of the discussion, the final draft report was sent to the EDB on 13 September 2010 for response by the end of September 2010. The EDB provided its comments to Audit on 12 October 2010.

64. The **Permanent Secretary for Education, Deputy Secretary for Education** and the **Principal Assistant Secretary for Education (Finance)** responded that:

- the EDB understood that Audit had assessed the matter based on its professional knowledge while the EDB had adopted a practical approach, and hence there was inconsistency in the findings. This was not a question of whether Audit and the EDB were right or wrong. The EDB's concern was to ensure that the amount of fee remission/scholarship set aside by the schools for needy students had not been affected;
- the EDB had communicated with Audit over its practice of allowing schools to charge fee remission/scholarship scheme to accounts other than that for school fee income. But there was no specific discussion on the use of "snapshot" figures in calculation because the EDB did not have detailed information at that time. After noting the Audit Report's query about the propriety of the EDB's practice, the EDB requested the schools concerned to provide detailed information. It was only after further checking the information that the EDB identified the reasons for discrepancy; and

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- the EDB was only given a short time for considering the draft Audit Report. As a large number of schools were covered and the draft Audit Report had to be kept confidential, it was impossible for the EDB to verify with individual schools the issues raised. As a matter of fact, the EDB had questions about some of the information contained in the draft Audit Report, and obtained a list of the relevant schools from Audit in September 2010 with a view to conducting analyses of the overall situation. But this was difficult because the issues were reported in different sections in the two chapters of the Audit Report, and time was short. In the end, the EDB focused on the feasibility of Audit's recommendations and the accuracy of Audit's description of the EDB's policies and measures, and provided response to Audit where necessary. Audit had made revisions to its report after considering the EDB's comments. When handling similar reports in future, the EDB would be more alert. However, the principle of confidentiality would still have to be observed.

65. Regarding the explanation that due to the shortage of time, the EDB could not verify the issues with individual schools, the Committee pointed out that the EDB could at least focus its efforts on the four schools visited by Audit and verify if the facts relevant to them were correct. The Committee doubted the propriety of the EDB's way of handling the draft Audit Report.

66. The Committee also asked, as a matter of principle, if the EDB contacted a school which was criticised in the draft Audit Report to verify the relevant facts, such as the composition of the IMC/SMC and the basis for calculating the provision for fee remission/scholarship scheme, whether this would be in breach of the requirement on confidentiality of the draft Audit Report.

67. The **Director of Audit** said that:

- he did not consider it a problem if the EDB verified the facts with the schools concerned. For instance, it was stated in paragraph 4.14(c) of Chapter 1 of the Audit Report that "for the 14 IMCs that did not have alumni manager, the history of the schools was relatively short and hence either their alumni associations had not been formed or their graduates were too young to serve as managers." This piece of

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information was provided by the EDB to Audit after making enquiry with the schools concerned; and

- Audit's observations in respect of DSS schools, other than the four which it had visited, were derived from its examination of the EDB's records. Audit was not in a position to comment whether the EDB should verify the facts with individual schools.

68. The **Secretary for Education** responded that:

- it was unfortunate that the EDB had not set out in writing its basis for assessing whether a school had met the requirements on fee remission/scholarship scheme. He agreed that in future the EDB should provide clearer response to draft Audit Reports;
- the auditee in the current audit was the EDB, not individual schools. The aim of the audit review was to identify room for improvement in the EDB's monitoring of DSS schools, and the draft Audit Report commented that there were inadequacies in the EDB's monitoring. Under the circumstances, it would not be appropriate for the EDB to make enquiries with each school to ascertain if the inadequacies identified in the report really existed; and
- while only 22 schools were involved in Audit's observations on fee remission/scholarship scheme, a large number of other issues had also been raised in the Audit Report. As Audit had obtained information on the schools through scrutinising the relevant files and records kept by the EDB and integrating it with the school information gathered from other sources, the EDB was not sure whether Audit had a comprehensive understanding of the actual situation. Due to lack of time and information, it was impossible for the EDB to verify all the relevant facts with the schools and respond to Audit's observations in the draft Audit Report.

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Publicity of fee remission/scholarship schemes

69. As revealed in paragraph 3.14 of Chapter 2 of the Audit Report, although under the DSS, schools were required to provide full details of the fee remission/scholarship schemes in their prospectuses, only two of the four schools visited by Audit had mentioned the schemes in their prospectuses. However, full details of the schemes (e.g. the eligibility criteria and the maximum percentage of fee remission) were not provided. Given that 50% of the schools visited by Audit did not comply with the EDB's requirement, the Committee queried whether the EDB had put in place any mechanism for checking the schools' compliance with its guidelines and requirements.

70. The **Permanent Secretary for Education** and **Miss WU Po-ling, Principal Assistant Secretary for Education (School Administration and Support)**, said that the administration of a fee remission/scholarship scheme was an important condition for admission to the DSS. The EDB considered that it was the schools' responsibility to provide full details of the fee remission/ scholarship schemes in their prospectuses and they had the ability to do so. The EDB would not require the schools to submit their prospectuses for its checking.

71. The Committee pointed out that it was very important for DSS schools to make public the full details of their fee remission/scholarship schemes so that parents who wished to choose such schools for their children could take the schemes into consideration when assessing their ability to pay the school fees. If such information was not provided to the public, some needy parents might be discouraged from applying for their children's admission to DSS schools. The Committee asked how the EDB would improve the situation and enhance the transparency of the fee remission/scholarship schemes run by DSS schools, so as to safeguard the interest of parents and students in need.

72. The **Permanent Secretary for Education** said at the public hearings and the **Secretary for Education** in Annex B of his letter of 17 December 2010 (in *Appendix 20*) that:

- in the EDB Circular No. 12/2010 issued on 5 November 2010, the EDB had set out more clearly the requirement for DSS schools as regards the provision of fee remission/scholarship schemes. The schools were required, among other things, to draw up clear and transparent criteria

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for awarding needy students fee remission and sufficient financial assistance (e.g. the eligibility criteria and the maximum percentage of fee remission);

- it had all along been the EDB's requirement that DSS schools should provide full details of the fee remission/ scholarship schemes in their prospectuses, which would be given out to any person upon request. The EDB would follow up with those schools which had not complied with such requirement. The EDB also agreed that it was desirable for schools to upload details of the schemes onto their websites, so as to facilitate parents in assessing the amount of fee remission that would be granted to them before applying for their children's admission to DSS schools. The EDB had requested schools to do so in the EDB Circular No. 12/2010; and
- in the Working Group set up to address the issues raised by the Committee and Audit, the EDB would further study possible measures to enhance the transparency (including ensuring that parents could have sufficient information on the fee remission/scholarship schemes and how schools might make effective use of any accumulated surplus of the schemes) and efficacy of the fee remission/scholarship schemes in DSS schools, in order to help ensure that students from low-income families would not be deprived of access to DSS schools due to inadequate means.

73. The Committee further asked whether the EDB had issued any guidelines on how a DSS school with excessive reserve for the purpose of fee remission/scholarship scheme should deploy the reserve and on the proper use of the reserve. The **Secretary for Education** replied in the same letter that:

- the EDB had set out the guidelines on the arrangements for DSS schools to handle reserve for the fee remission/scholarship schemes in the EDB Circular No. 12/2010; and
- the acceptable uses of the reserve included: extending the scholarships/fee assistance schemes by relaxing the awarding criteria; reducing the school fees; subsidising eligible students in their purchase of textbooks/reference books/stationery; and funding students' extra-curricular activities, including the expenses for their joining overseas educational visits and exchange study programmes, etc.

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Eligibility criteria of fee remission/scholarship schemes

74. The Committee noted from paragraph 3.16 of Chapter 2 of the Audit Report that of the 23 DSS schools which had provided details of their fee remission schemes on the schools' websites, the eligibility criteria adopted by two of them were less favourable than the government financial assistance schemes to students.

75. The Committee also referred to the eligibility criteria of the fee remission scheme of Good Hope School ("GHS") for 2010-2011 (provided in Annex A-8 in the Secretary for Education's letter of 11 December 2010 in *Appendix 19*). The Committee noted that in assessing the eligibility of students, the school adopted a point system under which points would be awarded on two aspects, i.e. family income and dependants. It was stated in the relevant Guidelines that "Dependents in receipt of Comprehensive Social Security Assistance ('CSSA') (excluding Old Age Allowance and Disability Allowance) are not eligible for any point score". The Committee further noted that apart from granting scholarships to students in need of financial assistance, GHS also set aside a number of scholarships to students who had outstanding performance in different aspects.

76. Against the above background, the Committee queried whether:

- GHS had discriminated against students from families in receipt of CSSA ("CSSA students") in administering its fee remission scheme; and
- the EDB had issued any guidelines to schools requiring them to set aside a larger proportion of their scholarships to assist students in need of financial assistance, instead of rewarding outstanding students.

77. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (School Administration and Support)** replied that:

- under the DSS, the eligibility criteria of the fee remission/scholarship schemes offered by DSS schools should not be less favourable than the government financial assistance schemes to students. As the fee remission reckoner adopted by GHS in assessing the eligibility of its students was very different from the basis of assessment for government schemes, it was difficult to make a direct comparison of the two. The EDB considered it very important that the fee remission scheme

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adopted by a DSS school should be clear and comprehensible. Hence, the EDB would discuss with GHS to see how it could improve and simplify its scheme so that parents would easily understand the scheme and the eligibility criteria; and

- as long as the schools fulfilled the EDB's requirements on the minimum amount of school fee income to be set aside for fee remission/scholarship scheme purpose and their eligibility criteria were not less favourable than government schemes, the EDB allowed the schools great flexibility in designing their fee remission/scholarship schemes having regard to the schools' history and the background of their students.

78. In response to the Committee's further questions about the fee remission scheme administered by GHS, the **Secretary for Education** informed the Committee in Annex G of his letter of 17 December 2010 (in *Appendix 20*) that:

- GHS explained that under the current system, students receiving CSSA payments that already included school fees would not be eligible for receiving school fee remission. However, if the CSSA payments did not cover school fees, the students could always apply for fee remission administered by the school and fee remission would always be granted. The school also clarified that the reference to CSSA recipients in the Guidelines for applying for school fee remission was included to avoid a situation where students would receive double subsidies from the CSSA and the school fee remission scheme. GHS indicated that it would revise the Guidelines as soon as possible to make the eligibility criteria clearer;
- two CSSA students from Secondary 2 and Secondary 4 respectively had been granted full fee remission in 2010-2011 school year; and
- GHS advised that it had never turned down the application for fee remission from CSSA students. Also, it had not provided assistance to students in applying for school fee remission from the Social Welfare Department ("SWD") as the school was always ready to grant full fee remission to CSSA students if schools fees were not covered under their CSSA payments.

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79. To ascertain whether CSSA students were discriminated by DSS schools, the Committee asked about the schools' policy towards the admission of and granting of fee remission to CSSA students. According to the information provided by the **Secretary for Education** in Annex E of the same letter and by the EDB at the end of January 2011:

- GHS adopted the same admission policy in respect of CSSA students and non-CSSA students. The school would not require applicants to state if they were CSSA recipients. All students were eligible for its fee remission/scholarship scheme; and
- in the remaining 71 DSS schools, all CSSA students were eligible for the schools' fee remission/scholarship schemes. Besides, all the schools adopted the same admission policy in respect of CSSA students and non-CSSA students.

80. Regarding the government policy towards remission of school fees in respect of CSSA students in DSS schools, the **Secretary for Education** advised in Annex F of the same letter that, according to the information provided by the SWD:

- the CSSA Scheme was a safety net of last resort for those who could not support themselves financially to meet their basic needs;
- under the existing CSSA policy, a student under the age of 22 and receiving education up to secondary level in a grammar school, vocational or technical training school could be assisted with a special grant to cover the school fees and other educational expenses. As free education was provided by the Government for students receiving primary and secondary education in government or aided schools, normally, no special grant for school fees would be given under the CSSA Scheme to students who choose to attend DSS schools; and
- where the students had been attending DSS schools before resorting to CSSA, the SWD would give them sufficient time to make suitable arrangements. Normally, they would be given a special grant for school fees up to the current school year, and in the interim, they could apply for fee remission from school or apply to change to a government or aided school. A special grant for school fees could be given to students attending Primary 5 and 6 to complete the Primary course; and also to those attending Secondary 5 and 6 to complete the Secondary course.

E. Revision of school fees

Approval for revision of school fees and consultation with parents

81. According to paragraphs 4.4 to 4.6 of Chapter 2 of the Audit Report, in 2009-2010, a DSS school intending to apply for school fee increase was required to obtain consent from the majority of the parents if: (a) it applied for a fee increase exceeding 7%; or (b) its accumulated operating reserve exceeded its annual operating expenses. Audit's examination of the records of the 18 approved school fee increase applications for 2009-2010 revealed that, in one of the six applications that required consent from the majority of the parents, supporting documents were not provided to the EDB. In the remaining five applications, relevant financial information of the schools was not provided to the parents.

82. The Committee asked whether the EDB had imposed any requirements on the type of financial information (e.g. the schools' financial status) that should be provided by DSS schools when they consulted parents on the proposals to apply for school fee increase.

83. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (School Development)** replied that:

- the EDB required schools applying for fee increase to obtain consent from the majority of the parents, and the school supervisors would sign off the application documents declaring that this had been done. However, currently the schools were not required to furnish the supporting documents to the EDB to prove that they had obtained the required consent; and
- while the EDB agreed that schools should provide sufficient information to parents during the consultation process for school fee increase, it had not specified the type of financial information that should be provided. The EDB would further consider the type of financial information that should be provided by schools during their consultation with parents.

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84. The Committee noted from paragraph 4.3 of Chapter 2 of the Audit Report that for 2008-2009 and 2009-2010, the EDB approved 30 and 18 applications respectively for school fee increases. For these two years, the approved school fee increases ranged from \$500 to \$17,500 and from \$100 to \$12,000 respectively. In response to the Committee's enquiry, the **Director of Audit** advised that for the two schools with the highest levels of fee increases, the increases were from \$4,500 to \$22,000 and from \$48,000 to \$60,000 respectively. The Committee asked whether the EDB had taken into consideration parents' affordability in approving such high levels of school fee increases.

85. The **Secretary for Education** and the **Permanent Secretary for Education** said that:

- in approving an application for school fee increase, the EDB would take into account the circumstances of the school concerned. For example, a school might change to small-class teaching and need to employ more teachers, or might need to expand the school premises; and
- the EDB would also require the school to seek the consent of the majority of parents if it applied for a fee increase exceeding 7%, which meant that parents' affordability would be taken into consideration in the proposed fee increase. The EDB would also assess if the school had properly addressed the concerns raised by the parents.

86. As requested by the Committee, the **Secretary for Education** provided a copy of the letters issued by the two schools with the highest levels of fee increases to obtain consent from parents for increasing the school fees (in Annex B of the Secretary's letter of 11 December 2010 in *Appendix 19*). The Committee noted that in Document 2 issued by the school with an increase from \$48,000 to \$60,000, it was stated that "Our financial projections indicate that the School will be operating at a deficit from 2009/10 onwards if the school fees are maintained at the current level." The Committee asked whether the financial projections had been provided to the parents, and whether the two schools had consulted parents by holding parents' meetings.

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87. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (School Development)** replied that:

- the EDB did not have record showing if the school had provided information about the operating deficit to parents because currently the EDB did not require the school to provide the EDB with such record. The EDB would request DSS schools to improve the transparency of their financial status when consulting parents on proposed school fee increases in future; and
- both of the two schools had discussed the fee increase proposals at the meetings of their parent-teacher associations, but they had not held meetings to consult all parents of the schools.

88. On the reasons for allowing the school to increase its fees from \$48,000 to \$60,000 from 2009-2010, the **Principal Assistant Secretary for Education (School Development)** explained that the EDB had considered the following factors in deciding to approve the fee increase:

- the school had not increased its fees in the past seven years since its conversion to a DSS school;
- the school had recently moved to a new campus, which was four times bigger than the old one, and hence there would be a significant increase in the maintenance cost; and
- if the school fees were not adjusted, the school's operating reserves would not be sufficient to meet at least two months' operating expenses of the school, which was a requirement of the EDB.

89. In order to understand the EDB's work in assessing DSS schools' applications for revision of school fees, the Committee enquired about:

- the criteria for approving or rejecting DSS schools' applications for increasing school fees; and
- the mechanism in place to ensure that the financial projections made by DSS schools in their fee increase applications were fair and reasonable.

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90. The **Principal Assistant Secretary for Education (School Development)** said at the public hearings and the **Secretary for Education** stated in Annex B of his letter of 11 December 2010 (in *Appendix 19*) that:

- apart from parents' consent, the EDB would also take into account other factors when considering schools' applications for increasing school fees. The major considerations for assessing the fee revision applications were:
 - (a) the financial situation of the school (e.g. the amount of operating reserve available and the budget for the coming year);
 - (b) the reasons and justifications for the fee revision; and
 - (c) the due process with regard to the consultation with parents;
- to ensure consistency in vetting applications for fee revision, a set of internal guidelines with criteria for vetting fee revision applications had been devised, details of which were summarised in the letter; and
- after the REO's initial vetting, all the fee applications were passed to the EDB's Finance Division for its professional comments. Based on the REO's initial vetting and the scrutiny of the schools' audited accounts, the Finance Division would spot out irregular items such as high bonus payments for follow-up by the REO.

91. As requested by the Committee, the **Secretary for Education** provided in the same letter the respective numbers of DSS schools with fee increase applications wholly/partially rejected and those for which approval was granted subject to a reduced level of increase, during the 2008-2009 to 2010-2011 school years. He also set out the main reasons for rejection, as follows:

- the school failed to provide the relevant audited account for the EDB to review its financial situation;
- the school possessed sufficient accumulated surplus and failed to provide strong justifications for fee increase; and
- the school failed to provide concrete evidence showing that parents had full understanding of the reasons for fee increase.

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92. The **Secretary for Education** also set out the main reasons for requiring schools to reduce the level of fee increase, as follows:

- taking into account the school's accumulated surplus and justifications, reduction of fee increase was necessary; and
- the school was requested to take into consideration parent's affordability for the proposed increase of fees.

Financial projections in applications

93. The Committee noted that financial viability was one of the justifications that would be accepted by the EDB for approving an application for school fee increase. Paragraphs 4.10 and 4.11 of Chapter 2 of the Audit Report revealed that underestimation of accumulated operating reserves was found in 26 of the 30 approved school fee increase applications in 2008-2009. As reported in Table 4 in paragraph 4.10(a), in eight schools, the actual accumulated operating reserves turned out to have exceeded their projected reserves by more than 100%. The Committee asked about the reasons for the significant variances between the projected and actual operating reserves of the eight schools.

94. The **Secretary for Education** said that:

- the EDB required schools to maintain operating reserves sufficient to meet at least two months' operating expenses all the time, which was about \$10 million for a secondary school. The EDB also considered that an operating reserve between two and 12 months of a school's operating expenses was reasonable; and
- as reported in Table 4, there was a school with a projected reserve of \$0.3 million and its actual reserve turned out to be \$1.8 million, meaning that there was a variance of \$1.5 million (500%). Although it appeared that a variance of 500% was substantial, the actual sum was not huge and was less than two months' operating expenses of the school as required by the EDB. Given the difficulties in making accurate projections and that the amounts of difference, which were in the region of three to four months of the schools' operating expenses, were relatively not substantial, he considered the variances acceptable.

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95. As requested by the Committee, the **Secretary for Education** provided an analysis of the reasons for the variances between the projected and actual operating reserves of the eight schools, in Annex B of his letter of 11 December 2010 (in *Appendix 19*). In gist, he stated that:

- for a school which applied for fee increase in 2008-2009, it had to submit, among other information, the following financial information around May 2008:
 - (a) the audited accounts of 2006-2007;
 - (b) the revised estimate of 2007-2008; and
 - (c) the budget for 2008-2009 taking into account the impact of the proposed fee increase;
- the 2008-2009 projected reserve of a school would be made in May 2008, about 16 months before the actual operating reserve of 2008-2009 was concluded as at 31 August 2009 for most schools. In other words, there was a time gap of about 16 months between the projected and actual result in income and expenditure items. Difference between the projected income or expenditure and the actual income or expenditure would result in variance between the projected reserve and the actual reserve as highlighted by Audit; and
- when the school prepared the budget for 2008-2009 in May 2008, it had to make reference to the 2007-2008 projected DSS unit subsidy rates which were the latest data available at that juncture (the 2007-2008 and 2008-2009 finalised rates would only be available in October of 2008 and 2009 respectively). The 2008-2009 finalised rates were higher than the 2007-2008 projected rates by 6% to 16%, resulting in higher DSS subsidy income and hence a higher actual operating reserve than estimated.

96. The **Secretary for Education** also stated in the same letter that two of the eight schools had substantial under-spending in various areas, as follows:

- one school had incurred less expenditure than estimated by 22% for several reasons (including the delay of a school self-financed extension

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construction project, lower-than-expected expenses on major repairs and teachers' salary, etc); and

- the other school had included a provision in the 2008-2009 budget for large-scale repair works/self-financed construction works. However, about \$1.4 million was not used in that school year.

97. The Committee further referred to paragraph 4.12 of Chapter 2 of the Audit Report which revealed that a DSS school, in its fee increase application, grossly overestimated its operating deficit by adopting a policy to depreciate its new school building over just five years, resulting in a depreciation expense of 22% of the estimated cost of the new school building. Such practice was not in line with the normal practice of providing for the depreciation over a longer period of say, 50 years, and the consequent depreciation expenses of only 2% of the estimated cost of the new building. The Committee questioned whether the EDB was aware that the school had adopted such an uncommon depreciation policy when approving its fee increase application.

98. The **Principal Assistant Secretary for Education (Finance)** said that the problem was identified by the Finance Division and referred to the REO for follow-up.

99. The **Principal Assistant Secretary for Education (School Development)** said that the REO did not accept a depreciation rate of 22%. Following the REO staff's discussion with the SSB of the school, it had changed its depreciation policy in the following year and depreciated the school building over 40 years, thereby significantly reducing the depreciation expense. In assessing the school's fee increase application, the EDB had not considered the depreciation expenses. Approval was given for the school to increase the fees of its junior secondary classes only, having regard to the rise of teachers' salary and the expenses arising from the commissioning of the new school building.

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Using operating reserves to finance capital works

100. The Committee noted from the Secretary for Education's reply that some schools had included provisions for large-scale repair works or construction works in their operating reserves accumulated from school fee income. It appeared to the Committee that if a school charged expenditure on major capital works, such as construction of a new school building, to its operating reserves, the school could have a strong justification for applying for substantial school fee increase, which would in turn create heavy financial burden on the parents. This was particularly so if the school intended to raise funds for the capital works over a short period of time, say five years. The Committee asked about the EDB's policy in this regard and how it safeguarded the interest of parents.

101. The **Secretary for Education** said that the EDB required DSS schools to submit development plans when their accumulated operating reserves exceeded an amount equivalent to a full year's operating expenses. The plans should set out how their accumulated operating reserves would be used, such as construction of new school premises. If a school applied for school fee increase to finance major capital works, it had to explain its plan to parents during the consultation process and obtain the parents' consent. The EDB would also ensure that the financial projections made by schools in the applications for school fee increases were properly justified and reasonable. For those schools with large amounts of accumulated operating reserves at the time of application for fee increases, the EDB would take into consideration the intended use of their reserves.

102. The Committee further asked, in respect of the eight schools mentioned in Table 4 in paragraph 4.10(a) of Chapter 2, the percentage of their operating reserves which had been used to fund the expenses of non-recurrent capital works.

103. The **Secretary for Education** replied in Annex I of his letter of 17 December 2010 (in *Appendix 12*) that based on the 2008-2009 audited accounts and information provided by the schools concerned, six out of the eight schools did not have non-recurrent capital works expenses charged to their income and expenditure accounts or accumulated operating reserves in the year. The remaining two schools had charged non-recurrent capital works expenses to the accounts which amounted to 2.4% and 15.1% of their operating reserves respectively.

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104. In Annex H of his letter of 17 December 2010 (in *Appendix 12*), the **Secretary for Education** stated that:

- DSS schools were given flexibility in using their operating reserves of non-government funds to finance capital works and maintenance works of above-standard facilities, such as construction of additional floors and swimming pools, which would benefit the students. Apart from the operating reserves accumulated from fee incomes, some DSS schools raised funds separately for large-scale capital projects;
- to facilitate future monitoring of the operating reserves, the EDB would discuss with DSS schools the need for setting aside separate reserves with designated account for large-scale capital works and their related maintenance, as well as the rules of setting aside separate reserves. Moreover, the EDB would make it more explicit that DSS schools should consider the following factors when planning large-scale capital works:
 - (a) the capital works should meet educational and school needs, and were in the interests of students; and
 - (b) there should be due regard to parents' affordability and appropriate measures should be adopted to ease out the increase, which might include spreading out the expenses of the works over a longer period of time; and
- the EDB would also request that DSS schools, when planning to carry out large-scale capital works, should consult parents, and that during the process, they should provide parents with sufficient information, including the possible impact of the capital works on school fees and the schools' financial information.

F. Financial management

Audited accounts

105. According to paragraph 5.27 of Chapter 2 of the Audit Report, under the DSS, a school is required to ensure that its external auditor's report on the school's accounts will include a statement that the school has used the government subsidies in accordance with the rules promulgated by the EDB for the DSS. However, Audit noted that for the 2008-2009 audited accounts submitted by 67 DSS schools, the external auditors of 18 schools did not comply with the requirement on the auditor's reports.

106. The Committee asked whether the EDB:

- would check if the external auditor's reports submitted by the schools were in compliance with its requirements and what actions it would take in case of non-compliance;
- had provided any standard audit engagement letter and standard format of the auditor's report for DSS schools to follow so as to help ensure compliance; and
- would consider devising a self-assessment system for DSS schools to declare if they had complied with the EDB's various requirements and requesting the schools to document the justifications in case of non-compliance.

107. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (Finance)** responded at the public hearings, and the **Secretary for Education** in Annex J of his letter of 17 December 2010 (in *Appendix 20*) that:

- upon receipt of the external auditor's report on the school's accounts submitted by DSS schools, the EDB normally would not check its contents and hence was not aware of the non-compliance highlighted by Audit. At present, if the EDB spotted that the external auditors had not stated in their reports that the schools had used government subsidies in accordance with the rules promulgated by the EDB for the DSS schools, the EDB would not return the report to the school for submission of

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another external auditor's report that complied with the bureau's requirement. Nevertheless, since the matter had been raised by Audit, the EDB agreed that it should step up the relevant requirement and request a school to submit another external auditor's report in similar situation;

- it was individual DSS schools that appointed their own auditors. The EDB had provided the schools with an outline of an audit engagement letter in the EDB Circular No. 17/2008 for their reference. As regards external auditors' report, the EDB had set out its requirements in the "Reference Notes for Auditors of Schools which received subsidies under the Direct Subsidy Scheme" sent to all DSS schools. The EDB would consider requiring all DSS schools to adopt the same audit engagement letter; and
- the EDB was considering devising a list of important issues and requiring schools to declare their compliance with those issues. The suggestion of putting in place a self-assessment mechanism for DSS schools was in line with the EDB's thinking and it would carefully study the idea.

Interest income from government funds

108. The Committee noted from paragraph 5.31 of Chapter 2 of the Audit Report that a school had understated its interest income from government funds for three years by about \$448,000. Responding to the Committee's enquiries, **Mr Tony NG, Senior Auditor, Audit**, said that the school had explained that the mistake was caused by its misunderstanding of the accounting arrangements of DSS schools. The **Principal Assistant Secretary for Education (Finance)** said that after the irregularity was spotted by Audit, the EDB had taken follow-up action.

109. In Annex K of his letter of 17 December 2010 (in *Appendix 20*), the **Secretary for Education** added that the school confirmed on 14 December 2010 that the \$447,726.35, being the interest income from government funds for the 2006-2007 to 2008-2009 school years, would be transferred from the non-government fund accounts back to the government fund accounts within December 2010.

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Use of government funds

110. The Committee referred to paragraph 5.35 of the Chapter 2 of the Audit Report which revealed that some DSS schools had charged non-approved expenditure items to their government fund accounts for 2008-2009 and 2009-2010. Such expenditure items included: (a) travelling expenses of \$8,400 incurred by three teachers in an exchange visit; (b) an expenditure of about \$29,000 incurred for holding an annual dinner for staff; (c) an expenditure of \$42,000 for renting a piece of land for a kennel to keep dogs to guard against illegal immigrants entering the school premises; and (d) a tax payment of \$4.1 million and a donation payment of \$5.1 million.

111. It appeared to the Committee that except for the tax and donation payments mentioned in (d) above, there were well-justified reasons for incurring the expenses mentioned in (a), (b) and (c) above, and the sums involved were reasonable. The Committee therefore asked why Audit and the EDB considered the expenditure items improper.

112. The **Director of Audit** and the **Senior Auditor** explained that the EDB had issued a circular informing DSS schools that only approved expenditure items of educational nature could be charged to the schools' government fund accounts. Although the amounts of the expenses mentioned in paragraph 5.35 of Chapter 2 of the Audit Report might not be unreasonable, they were not approved items specified in the circular and should be charged to the schools' non-government fund accounts.

113. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (School Administration and Support)** responded that:

- the EDB agreed with Audit that the above expenditure items should not be charged to the government fund accounts. According to the EDB's policy, government funds could only be used for educational purpose and for the benefits of students. Other expenditures, like entertainment expenses for staff, should be charged to the schools' non-government fund accounts;
- in deciding whether an expenditure item should be charged to the government fund accounts, the EDB would consider the schools'

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circumstances and the nature of the relevant functions. For instance, if a school had established a proper procedure or mechanism for holding staff exchange programme or staff entertainment functions, the EDB might allow the school to charge the costs so incurred to its government fund accounts. In the present cases, the schools concerned did not have such procedure or mechanism; and

- when the EDB followed up with the DSS Schools Council on the recommendations of Audit and the Committee in future, it would discuss with the Council to see how improvements could be made to the EDB's guidelines.

Use of non-government funds

Purchase of properties

114. The Committee noted from paragraph 5.41 of Chapter 2 of the Audit Report that the HKCCCU Logos Academy had used non-government funds to purchase three properties during the period from 2006 to 2009. The properties were held under a purported trust arrangement, which was considered improper by the EDB. The Committee also noted that the EDB only discovered the problem through the school audit carried out in March 2009. The Committee asked:

- about the details of the malpractice;
- why the EDB had not been able to detect the purchase of properties by the HKCCCU Logos Academy from the school's financial statements submitted to the bureau before 2009, but could only identify the malpractice after carrying out the school audit in March 2009; and whether and how the purchase had been reported in the school's audited accounts in the relevant years; and
- about the follow-up actions taken by the EDB.

115. The **Secretary for Education** provided the information in Annex C of his letter of 11 December 2010 (in *Appendix 19*) and in Annex A of his letter of 30 December 2010 (in *Appendix 21*). In gist, he stated that:

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- the EDB scrutinised the audited accounts of schools every year and wrote to request schools to rectify the malpractices and irregularities identified. The purchase of a property in August 2006 was recorded by the HKCCCU Logos Academy as "Additions" under "School Premises" in the 2005-2006 audited accounts. No other details were provided in the audited accounts, including any indication that those additions were for the purchase of properties. As it was not uncommon for schools to have additions to school premises such as minor construction work and renovation work, the EDB did not categorically follow the matter up with the school;
- the purchase of properties and trust arrangement were first identified by the EDB in the school audit inspection in March 2009, and since then the EDB had followed up with the school. The EDB issued a management letter to the school in February 2010 requesting, among other things, justification/rectification of the arrangement and other financial irregularities. In the absence of any response from the school, written reminders were issued in March and August 2010 respectively. As there was still no response, a warning letter was issued to the school in November 2010 requiring it to provide, among other irregularities detected, detailed information and concrete actions to be taken in respect of the trust arrangement, including proper documentation of and justifications for the purchase of the properties, as well as the approval of the SMC for the purchase and making of the trust arrangement. A reply dated 23 November 2010 was finally received from the school, in which it undertook to take rectification actions promptly; and
- the EDB would request DSS schools to provide detailed disclosure on purchase of properties in their accounts from 2009-2010 onwards.

116. The Committee further asked about the latest progress made by the school in transferring the three properties back to the SMC. The **Permanent Secretary for Education** said at the public hearings and the **Secretary for Education** stated, in Annex B of his letter of 30 December 2010 (in *Appendix 21*) and his letter of 24 January 2011 (in *Appendix 22*), that:

- the school had appointed a solicitor firm to follow up the matter. According to the Supervisor of the HKCCCU Logos Academy, the Declaration of Trust of the three properties stated that the trustees would hold the properties for the IMC of the HKCCCU Logos Academy.

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Since the School had no IMC and the school sponsor had no plan to establish one in the near future, legal advice was that it would be necessary to seek a vesting order from the court to vest the three properties to the SMC, i.e. the HKCCCU Logos Academy Management Committee Limited. The SMC had accepted the legal advice to apply to court for a vesting order. To this end, the solicitor retained by the school had in turn instructed a barrister to apply for the requisite vesting order; and

- the EDB would monitor the development closely with a view to ensuring that the vesting process was not unduly delayed.

Training programme for principals from the Mainland

117. The Committee noted from paragraph 5.42 of Chapter 2 of the Audit Report that the HKCCCU Logos Academy had organised a training programme for school principals from the Mainland. Up to May 2010, expenses of about \$151,000 had been incurred for the programme and charged to the school's non-government funds. The Committee asked whether the EDB considered the arrangement appropriate.

118. The **Permanent Secretary for Education** said that it was the EDB's requirement that the expenses incurred by DSS schools should benefit the students of the schools. The EDB did not consider the arrangement appropriate as the training programme benefited Mainland school principals instead of the school's students directly. Hence, in the warning letter issued by the EDB, the school was also required to provide justifications for organising the training programme.

Investment of surplus funds

119. According to EDB Circular No. 2/2003, surplus funds which are not immediately required for use by schools (including DSS schools) may be placed in time deposits or savings accounts with banks licensed under the Banking Ordinance (Cap. 155). Any other forms of speculative investment (e.g. in local equities) are not recommended because of the risk of financial loss. Paragraph 5.47 of Chapter 2, however, revealed that contrary to the EDB's guidelines, one of the four schools visited by Audit, i.e. GHS, invested part of its surplus funds in financial instruments (e.g. local equities and investment funds) instead of placing them in time deposits or savings accounts.

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120. The Committee asked about the details of the malpractice and the EDB's follow-up actions, as well as the EDB's guidelines in this regard. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (Finance)** replied that:

- the investment was discovered by the EDB during the school audit inspection in December 2007, before Audit's review. The EDB found that the school had obtained approval from its SMC before making the investment. The EDB had issued a management letter to the school reminding it that such speculative investment was not recommended. The school had also been informed that the liability for any financial loss arising from the investment would strictly fall on the school management and that it would not be allowed to charge any financial loss to any of the school's accounts;
- in response to the management letter, GHS had committed to placing its surplus funds in low-risk investment and disposing of the local equities and investment funds gradually;
- as reported by the press, there was discrepancy between the English and Chinese versions of EDB Circular No. 2/2003. In the English version, it was stated that speculative investment was "not recommended". But in the Chinese version, this was phrased as schools "cannot" make speculative investment. The EDB had recently revised the Chinese version so that it would be consistent with the English version. In fact, it had all along been the EDB's stance that speculative investment was "not recommended"; and
- in the EDB Circular No. 12/2010 issued in November 2010, the EDB had provided guidelines to DSS schools on devising a school-based mechanism on investment by using non-government funds. Schools were required, among other things, to consult their key stakeholders and seek prior approval of their SSBs as well as their SMC/IMC if they had compelling and well-justified reasons to invest by using non-government funds.

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121. In response to the Committee's other enquiries, the **Secretary for Education** stated in Annex C of his letter of 30 December 2010 (in *Appendix 21*) that according to the information provided by GHS, the school was the registered owner of all the investments reported in the audited accounts, and all dividend income/additional units of funds generated from the investments were reported as interest income/profit on disposal of investment in the school's audited accounts.

Fund raising activities

122. The Committee referred to the fund raising activity undertaken by a school as mentioned in paragraph 5.56 of Chapter 2 of the Audit Report, and asked:

- why the EDB was not able to detect the irregularities until they were identified by Audit;
- how the funds raised had been disclosed in the school's audited accounts since the launching of the activity by the school in June 2008; and
- about the follow-up actions taken by the EDB.

123. In Annex D of his letter of 30 December 2010 (in *Appendix 21*), the **Secretary for Education** stated that:

- according to the 2007-2008 audited accounts of the school concerned, a receipt and an expenditure entry of the same amount of \$508,408 with the description of “膠椅捐贈四川地震災區” were recorded in the notes to the accounts under Other Operating Expenses;
- as regards Audit's findings in paragraph 5.56(c) of Chapter 2 that there was a sum of about \$160,000 from the fund raising activity recorded as retained surplus in the school's accounts, EDB had checked the 2007-2008 and 2008-2009 audited accounts again and found that the said sum of surplus had not been separately disclosed in the accounts;
- subsequently, the EDB noted from the 2008-2009 audited account that the above-mentioned fund raising activity had been completed but the EDB had not yet received the school's application for approval of the activity. The EDB therefore wrote to the school on 31 August 2010 requesting it to seek covering approval from the bureau. In its reply of

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14 September 2010, the school informed the EDB that the activity was organised solely by the Parents Association ("PA") with parents as the target donors, and hence the school did not consider the EDB's approval necessary;

- in response to the EDB's further enquiries, the SMC of the school wrote to the EDB on 23 December 2010, confirming that the fund raising activity was organised by the PA and assisted by the school. As the EDB's prior approval was still required for any fund raising activity organised by other organisations in schools, the SMC had also committed to seeking covering approval from the EDB; and
- in order to avoid the misunderstanding that the school could use the surplus for other purposes, the school had further committed to transferring the surplus back to the PA. The PA had already made known to the parents the relevant financial statement of the fund raising activity on 22 November 2010.

124. The **Permanent Secretary for Education** added that it was the school's responsibility to follow the EDB's guidelines to prepare a separate financial statement for each fund raising activity, instead of reporting the activity in the school's other accounts. The school was also required to display such statement for a reasonable period of time for the information of the stakeholders, including teachers, parents and students.

G. Admission process

Assessment of track record

125. According to paragraphs 2.2 to 2.5 of Chapter 1 of the Audit Report, in processing applications from aided schools for admission to the DSS, the Task Force on DSS assesses an applicant school's track record of performance. Audit's examination of the records of 10 applications for admission to the DSS in 2008-2009 and 2009-2010, however, revealed that in one case, the score awarded by the Quality Assurance Division ("QAD") was based on an inspection carried out a decade ago; and in four other cases, the applicant schools had not been subject to any External School Review ("ESR") or quality assurance inspection, and therefore no score was awarded by the QAD.

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126. The Committee asked why the EDB had not assessed the applicant schools' track records of performance based on up-to-date and relevant information, and in the absence of such information, what the basis of the EDB's decision was.

127. The **Deputy Secretary for Education** responded that:

- the Task Force on DSS schools would take into consideration a basket of factors when processing a school's application for admission to the DSS, and the school's performance in previous ESR was one of the factors. For those applicant schools which had not been subject to any previous ESR or quality assurance inspection, if there was sufficient information about the track record of the school to enable the Task Force to make a professional judgement, the Task Force might not find it necessary to carry out a school inspection; and
- the EDB agreed with Audit's recommendation and when assessing applicant schools' track record of performance in future, a new school inspection would be carried out by the QAD for assessment purpose where necessary.

128. In response to the Committee's enquiry, the **Assistant Director of Audit**, said that the application mentioned in paragraph 2.5(a) of Chapter 1 of the Audit Report had been rejected by the EDB. The four cases mentioned in paragraph 2.5(b) had been approved by the EDB after considering other relevant factors, which were documented.

Compliance with admission conditions

Non-profit-making status

129. According to paragraphs 2.9 to 2.12 of Chapter 1 of the Audit Report, starting from 1999-2000, profit-making schools are no longer eligible to join the DSS. Five profit-making schools (four admitted to the DSS in 1999-2000 and one in 2000-2001) were required to complete the procedures for acquiring a non-profit-making status within one year after admission. However, up to June 2010, their profit-making status remained unchanged. Noting the EDB's response in paragraph 2.12 that efforts were made during the period from January 2006 to

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June 2010 to sort out the proper procedures to take forward the proposal, the Committee questioned:

- how the five schools had used their operating surpluses in the past five years; and
- the reasons for the long time taken since January 2006 to sort out the issues and procedures relating to the schools' change to a non-profit-making status.

130. In Annex A of his letter of 25 November 2010 (in *Appendix 17*), the **Secretary for Education** advised that although the SSBs of the five schools had not acquired a non-profit-making status legally, they had been operating on a non-profit-making basis. All the surpluses accumulated would be retained in the school for use relating to the benefit of students, such as major repair and upgrading of school facilities, purchase of furniture and equipment, and hiring additional teachers, etc. In fact, the schools seldom applied for fee increase, and their school fees, which were uniform among the five schools within the group, were comparatively low.

131. Regarding the reasons for taking a long period of time to sort out the procedural matters, the **Deputy Secretary for Education** said at the public hearings and the **Secretary for Education** stated in Annex A of his letter of 8 December 2010 (in *Appendix 14*) that:

- the five schools were ex-Bought Place Scheme ("BPS") schools operated by two profit-making companies limited respectively. The two school operators borrowed BPS loan from the Government at a total amount of HK\$247 million for purchasing the five school premises in the 1990s, and in this connection five Loan Agreements and Legal Charges were signed and registered with the Lands Department. As the two school operators were registered under Company Limited by Shares, they set up five companies with non-profit-making status to serve as the SSBs of the schools and suggested to process the change of operation right from the existing school operators to the new SSBs by way of signing a "novation agreement";

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- due to the uniqueness and complexity of the case, which involved not only the transfer of school operation right, but also the transfer of property ownership (Legal Charge) and the liability under the Loan Agreement, the EDB had adopted a prudent approach. It had sought legal advice from the DoJ and the Legal Advisory and Conveyancing Office ("LACO") from time to time, so as to ensure that the interest of the Government was properly protected;
- in early 2007, the EDB started a review of the standard clauses and articles of the M&AA for the SSBs under the Company Registration. At the same time, the EDB was preparing a Procedural Guide on Transfer of SSB of Aided Schools ("Procedural Guide") for internal reference. It was considered that in handling the five cases in question, the EDB should take the former into consideration and make reference to the latter to ensure consistency. Relevant Standard Clauses and Articles of M&AA were updated and made available for school use in 2007. The compilation of the Procedural Guide was completed in 2008;
- in 2009, the EDB devised a workflow for processing the transfer of operation right between the old and new SSBs of the five schools with reference to the Procedural Guide. At the same time, the EDB requested the new SSBs to provide their existing M&AA for its checking. The EDB received the M&AA in January 2010. The new SSBs were requested in June 2010 to revise their M&AA in order to meet the latest requirements. The schools submitted the revised M&AA to the EDB for comment in September 2010. Subject to further amendments by the SSBs, they would submit the amended M&AA to the Companies Registry and the Inland Revenue Department for endorsement; and
- this case, which involved complex legal issues, was unprecedented. As the DSS was a comparatively new system and some of the implementation details had to be fine tuned in the process to cater for different scenarios in practice, the EDB had taken much time to resolve the matter. The EDB admitted that the progress had not been satisfactory. Once the Deed of Novation and Assignment were agreed by the schools, the DoJ, the LACO and the EDB, the EDB would proceed with the task according to the relevant procedure.

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Self-owned school premises

132. As reported in paragraphs 2.13 and 2.14 of Chapter 1 of the Audit Report, one of the conditions for admission to the DSS is that the schools must have their self-owned school premises. Schools operating in leased premises are required to secure their own premises within 10 years after admission, or any other period as specified by the EDB. Two schools conditionally admitted to the DSS in 1999-2000 were required to secure their own school premises by the end of 2004-2005. However, up to June 2010, they were still operating in leased premises.

133. In response to the Committee's question, the **Secretary for Education** replied in Annex A of his letter of 25 November 2010 (in *Appendix 17*) that according to the Rating and Valuation Department, the two schools, which were operating in leased premises, were paying rents at the market level.

H. Monitoring school performance

Issuance of school audit reports and follow-up audits

134. The Committee noted that the EDB carried out audits of DSS schools to ascertain whether their financial and accounting operations complied with the relevant requirements. As reported in paragraphs 5.9 and 5.12 of Chapter 1 of the Audit Report, Audit's examination of the records of 20 DSS school audits found that there were delays in issuing audit reports to 11 (55%) schools, ranging from 6 to 240 days. Moreover, no follow-up school audit had been carried out by the EDB even though glaring malpractices had been identified during school audits. In three of the four schools visited by Audit, some issues identified as glaring malpractices by the EDB had not yet been rectified.

135. The Committee queried whether the above audit findings reflected that the EDB's supervision of DSS schools had been lax.

136. The **Secretary for Education** admitted that there had been negligence on the part of the EDB in issuing audit reports to schools, and improvement would be made to ensure timely issuance of such reports. He also said that the glaring malpractices were committed by a few individual schools only and serious non-compliance was not a general phenomenon among all DSS schools.

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137. In response to the Committee's questions, the **Secretary for Education** informed the Committee vide Annex C of his letter of 11 December 2010 (in *Appendix 19*) that the three schools which were found to have glaring malpractices, as set out in Table 4 in paragraph 5.12 of Chapter 1 of the Audit Report, were Tak Sun Secondary School, HKCCCU Logos Academy and GHS. In the same letter, he set out the reason why the glaring malpractices of the three schools had not been rectified after a long time, the actions that had been taken by the EDB and the present position of the malpractices.

School audits on DSS schools

138. The Committee further referred to paragraph 5.6 of Chapter 1 which reported that up to 30 June 2010, the EDB had only completed school audits on 28 (39%) of the 72 DSS schools. Given that school audits served the important function of ascertaining whether the schools' financial and accounting operations complied with the relevant requirements, the Committee was concerned about the small number of audits carried out on DSS schools. The Committee therefore enquired:

- about the manpower deployed for conducting audits on DSS schools and following up the issues identified in the audits, and whether the EDB considered the manpower sufficient; and
- whether there had been any changes in the manpower in the past five years from 2005 to 2010.

139. The **Permanent Secretary for Education**, the **Principal Assistant Secretary for Education (School Administration and Support)** and the **Principal Assistant Secretary for Education (Finance)** said that:

- the EDB understood that as DSS schools were relatively a new feature and were given a lot of flexibility in their financial management, there was a need to deploy more resources to conduct school audits on them. In fact, the EDB had allocated more resources for such work and had progressively conducted more audits on DSS schools, from two in 2006 to eight in 2009. At its own initiative, the EDB also planned to increase the number of school audits to 12 in 2010-2011; and

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- the EDB would review if the current manpower was sufficient for school audits and the follow-up work. The EDB also agreed with Audit's recommendation that it should establish a systematic risk analysis mechanism for the selection of schools for audits.

140. Regarding the manpower deployed for carrying out audits on DSS schools, the **Secretary for Education** advised in Annex C of his letter of 11 December 2010 (in *Appendix 19*) that:

- the Finance Division and the REOs of the EDB took up a range of duties in respect of school education services. Currently, there were around 4,000 schools including aided, government, DSS, caput and private schools as well as kindergartens in Hong Kong. The 15 District School Development Sections under four REOs were responsible for providing support to the administration and development of schools. There was no designated post specifically created for school audits of DSS schools and the follow-up work required;
- the School Audit Section of the Finance Division would conduct audit of DSS schools. After conducting field audit inspections, the School Audit Section would continue to follow up with the schools in respect of any outstanding documents/information/clarifications which could not be provided by the schools on-site. Management letters would be issued to the schools concerned after seeking comments from the policy division. In addition, the Finance Division also deployed staff to examine the audited accounts and fee revision application of DSS schools; and
- schools were required to respond to the management letters and the REOs would take appropriate follow-up actions where necessary. Other than follow-up on audit inspections, with regard to DSS schools, the REOs were also responsible for handling major repairs exceeding \$2 million, fee revision, complaints handling, renewal of service agreement, enhancement of school facilities and other school administrative work (e.g. crisis management, appointment of school head, and trading operation). For optimisation of resources, there was no post in the REOs designated solely for handling DSS schools.

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141. On the question of manpower changes in the past five years, the **Secretary for Education** provided the following two tables in the same letter. He also stated that the manpower as indicated in the tables below referred to: (a) the number of School Audit Section's staff deployed for undertaking duties relating to audits of DSS schools and the related follow-up work; and (b) the apportionment of staff resources devoted to the overall administration and support of DSS schools and was worked out based on the relative workload of DSS schools as compared to other types of schools.

	Year					
	2005	2006	2007	2008	2009	2010 (Planned)
No. of audit inspections on DSS schools	4	2	6	6	8	12
No. of School Audit Section's staff involved in audit inspections on DSS schools	0.9	0.4	1.3	1.3	1.7	2.5

	Year					
	2005	2006	2007	2008	2009	2010
No. of REO staff devoted to the overall administration and support of DSS	3.2	3.8	4.2	4.9	5.3	5.4

I. Direct subsidy scheme subsidy

142. According to paragraphs 6.13 and 6.14 of Chapter 1 of the Audit Report, the then Education and Manpower Bureau did not inform the Finance Committee ("FC") of the LegCo that exception had been given to a school to ensure that it would continue to receive the old DSS subsidy rate after the two-tier system was introduced. The Committee asked why the bureau had not informed the FC.

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143. The **Permanent Secretary for Education** said that both the then Education and Manpower Bureau and the then Finance Bureau were of the view that the FC's approval was not required for the change in the calculation of subsidy rate under the two-tier system because the two-tier system did not deviate from the funding principle approved by the FC. The FC's approval was therefore not sought for the introduction of the two-tier system. The special approval given to a school to continue to receive the DSS subsidy at the old rate when the two-tier system was introduced, was in fact not relevant to the justification for the new measure. Hence, the FC was not informed.

144. The Committee further asked whether the EDB agreed that transparency would have been enhanced if the FC had been informed of the special approval granted to the school.

145. The **Permanent Secretary for Education** said that he had no reason to query the judgement of the then Education and Manpower Bureau and the then Finance Bureau, which had been made after thorough consideration. However, as a general principle, he agreed that complete information should always be provided to the LegCo.

146. **Ms Alice LAU, Deputy Secretary for Financial Services and the Treasury (Treasury)**, said that the Financial Services and the Treasury Bureau also agreed with the general principle that complete and accurate information should always be provided to the FC.

J. International schools in the direct subsidy scheme

147. According to paragraph 7.2 of Chapter 1 of the Audit Report, when the DSS was introduced in 1991-1992, international schools were eligible to join the scheme. In October 1995, the Government decided to gradually phase out international schools from the DSS. Up to 2009-2010, one international school (School I — Li Po Chun United World College) remained in the DSS.

148. Paragraphs 7.9 and 7.10 revealed that when the Executive Council ("ExCo")'s decision was sought in October 1995 to phase out international schools from the DSS, there were five international DSS schools. However, in the

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Memorandum submitted to the ExCo by the Administration, the then Education and Manpower Branch³ did not include School I in the list of international schools to be phased out. The Committee asked whether the EDB agreed that School I had been treated more favourably than the other international schools which were phased out, and about the reasons for allowing School I to remain in the DSS.

149. The **Secretary for Education** responded that:

- the decision to allow School I to remain in the DSS was made in 1999 by staff of the then Education and Manpower Bureau. As stated in the Audit Report, the decision had been reviewed several times by the relevant bureau and department over the years. The justifications recorded by the then Education Department in 2002 were that School I was offering the International Baccalaureate Diploma Programme which was recognised by universities both in Hong Kong and overseas for admission purpose, and about 40% of School I's enrolment were local students; and
- after reviewing the reasons recorded by his predecessors for allowing School I to remain in the DSS, he thought that probably his decision might be the same if he were to make the decision at that time.

150. The **Permanent Secretary for Education** said that the EDB agreed with Audit's recommendation that it should critically review the justifications for continuing to allow School I to remain in the DSS. In Annex E of his letter of 30 December 2010 (in *Appendix 21*), the **Secretary for Education** supplemented that the Working Group set up by the EDB would revisit the justifications based on which a decision was made for continuing to allow School I to remain in the DSS. It would take into account the then and current prevailing circumstances, including the operating mode, quality of education provided by School I and legal advice, etc.

151. In response to the Committee's question, the **Secretary for Education** stated in Annex D of his letter of 8 December 2010 (in *Appendix 14*) that the Secretary for Education and Manpower who was involved in dealing with the matter of allowing School I to remain in the DSS in 1999 was Mr WONG Wing-ping.

³ In July 1997, the Education and Manpower Branch was renamed the Education and Manpower Bureau.

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152. According to paragraphs 7.3 to 7.7 of Chapter 1, in June 1991, in seeking funding approval from the FC for building and equipping the new school premises for School I, the FC was informed that no recurrent subsidy would be provided to the School. Yet, the then Education and Manpower Branch did not inform the FC that School I would be given recurrent subsidy upon its admission to the DSS in 1994. The Committee also noted that there had been discussions between the then Education and Manpower Branch and the then Finance Branch on the need to inform the FC of the change. The Committee asked why the FC was not informed in the end.

153. The **Deputy Secretary for Financial Services and the Treasury (Treasury)** said that both the Education and Manpower Branch and the Finance Branch agreed that there was no need to seek the FC's approval for admitting School I to the DSS and for it to receive recurrent DSS subsidy. The Finance Branch only considered that it would be desirable to submit an information note to the FC to inform Members of the change. After discussion, the Education and Manpower Branch did not submit an information note to the FC.

K. Human resource management

154. The Committee noted from paragraphs 6.7 to 6.9 of Chapter 2 of the Audit Report that of the four DSS schools visited by Audit, three did not carry out open recruitment for some staff recruited in 2007-2008 to 2009-2010. The staff recruited included a senior post that was equivalent to the rank of vice-principal, a principal, and 36 other staff, etc. The Committee asked whether the EDB was aware of the situation before it was raised by Audit.

155. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (School Development)** responded that:

- there was an established procedure for the appointment of a school principal and the EDB's approval was also required. As the school concerned had not complied with the procedure, the EDB did not approve the appointment of the new principal. The EDB's approval was not required for the appointment of the other staff and hence it was not aware that open recruitment had not been conducted for their appointment. The appointment of staff was basically a school-based decision;

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- DSS schools were given great freedom in different areas, including human resource management. A school could appoint suitable teachers and give them appropriate salaries in the light of its development and curriculum. The EDB had issued a number of guidelines to advise DSS schools of the best practices in human resource management. The basic principles were that recruitment should be carried out in a fair and open manner, proper mechanisms should be put in place to ensure that the remuneration packages for individual staff were fair and justifiable, and performance management should be handled properly, etc. The EDB also required the schools to follow the guidelines issued by the Independent Commission Against Corruption ("ICAC") in devising their human resource systems;
- notwithstanding the guidelines, the EDB would not specify the details of the mechanisms to be established for compliance by the schools. This was the responsibility of the SMCs/IMCs of the schools; and
- the Working Group set up by the EDB would consider how to assist DSS schools in improving their human resource management practices.

L. General administration and other governance issues

156. According to paragraph 7.22 of Chapter 2 of the Audit Report, two of the four DSS schools visited by Audit had accepted donations from trading operators without any documented compelling reasons, and no disclosure was made in the school reports. The Committee asked whether the schools concerned had obtained approval from the school governing bodies for accepting donations and about the EDB's requirements in this respect.

157. The **Permanent Secretary for Education** and the **Principal Assistant Secretary for Education (Finance)** said that:

- the schools concerned had obtained approval from their school governing bodies for accepting donations from the lunch box suppliers. However, it was not sufficient to have the approval. According to the EDB's requirement, the schools should only consider accepting donations or advantages from the trading operators/suppliers in very exceptional circumstances with justification of compelling reasons as well as approval from the school governing body; and

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- schools had to comply with some guiding principles in accepting donations or advantages, including that all donations to the school should be expended on the school and for educational purposes only, the school's reputation and students' benefits must not be affected, and in no circumstances might a school suggest to the suppliers and contractors that the school would provide an advantage in return for their donations, etc. Schools were also required to establish a mechanism to handle donations with reference to the ICAC's guidelines on corruption prevention and the EDB's guidelines.

158. The Committee noted from paragraph 7.18 of Chapter 2 that the profit of some of the items sold by three of the four schools visited by Audit had exceeded the 15% profit ceiling set by the EDB. The profit rates ranged from 20% to 150%. The Committee asked what the items were.

159. The **Director of Audit** replied that the item with the highest profit was school pins. The cost of a school pin was \$4 and the selling price was \$10, giving a profit rate of 150%.

M. Conclusions and recommendations

160. The Committee:

- notes that:
 - (a) the Audit Commission ("Audit")'s value for money audit is on the Direct Subsidy Scheme ("DSS") administered by the Education Bureau ("EDB") and not on individual DSS schools *per se*;
 - (b) the audit is confined to the EDB's administration and supervision of the DSS and the governance and administrative matters of DSS schools, which do not include the quality of education provided by DSS schools; and
 - (c) in the early stage of the DSS, in order to encourage more schools to join the scheme, the Administration allowed some schools to join the DSS before they had been able to complete all the admission requirements, making it difficult for the EDB to deal with the

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problems that surfaced subsequently in requiring the schools to comply with certain admission conditions;

- considers that although the objective of the DSS is to inject diversity to Hong Kong's school system through the growth of a strong subsidised private school sector so that parents would have more choices, and DSS schools are allowed to have greater flexibility in various areas, the EDB has to perform a monitoring role to ensure that the schools comply with its requirements, and that their governance, accountability and transparency are up to the required standard and public expectation;
- expresses grave dismay and finds it unacceptable that the Secretary for Education has not been made aware of the widespread compliance problems in DSS schools and there is no dedicated high-level body in the EDB to oversee the administration of the DSS and the schools' compliance with the DSS requirements;
- expresses disappointment that:
 - (a) the EDB has failed to discharge its monitoring role over DSS schools effectively, as reflected by some serious cases of non-compliance with the EDB's guiding principles or requirements and its failure to take effective actions to ensure timely rectification of those problems. Details of the non-compliance are set out in the ensuing parts;
 - (b) the EDB has failed to attach sufficient importance to the gravity of the problems in the administration of DSS schools in that they were simply dealt with as operational issues without adequate appreciation of the need to bring them to the attention of the Secretary for Education for policy review; and
 - (c) before allowing some schools to join the DSS prior to completing all the admission requirements, the Administration had failed to consider the circumstances of individual schools which would make compliance with all the admission conditions difficult to achieve within a reasonable time;
- is surprised at and does not accept the Secretary for Education's statement that the EDB was toothless towards non-compliant DSS

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schools, given the administrative and punitive measures that EDB may take against them;

- expresses dismay that some DSS schools have not:
 - (a) set aside the required amounts of school fee income for the purpose of their fee remission/scholarship schemes; and
 - (b) clearly set out the eligibility criteria or adequately publicised the schemes, which might have discouraged needy parents from applying for their children's admission to DSS schools due to lack of information;
- acknowledges that for the purpose of enhancing and stepping up efforts to improve the governance of DSS schools, the Secretary for Education has tasked the Permanent Secretary for Education to consider a review of the governance framework, internal control and enforcement mechanism and financial management of DSS schools. A Working Group has been set up under the EDB with inputs from DSS schools and the academic sector as well as from relevant professionals experienced in governance, financial management and related areas to take forward the review and address the issues raised by the Committee and the Director of Audit;
- strongly urges the Secretary for Education to:
 - (a) enhance his supervision of the DSS and ensure that the EDB will perform its monitoring role over DSS schools more effectively;
 - (b) establish a dedicated high-level body in the EDB to oversee the administration of the DSS as well as its control and monitoring of DSS schools. Its duties should include conducting regular reviews of the EDB's control and monitoring mechanism, so as to enhance the governance and administration of DSS schools;
 - (c) put in place a system that requires the EDB staff to report, in appropriate cases, DSS schools' non-compliance and malpractices to sufficiently high-level staff, including the Permanent Secretary for Education and the Secretary for Education, for follow-up actions;

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- (d) require the Working Group to accord top priority to reviewing the EDB's control and monitoring mechanism instituted for DSS schools to ensure that it is sound and effective, so that non-compliance with the EDB's requirements and malpractices will be detected in a timely manner, rigorous actions will be taken to enforce compliance and rectification, and appropriate punitive measures commensurate with the gravity of the problems will be taken against the schools concerned. The Working Group should consult various stakeholders and the Panel on Education in the review; and
- (e) apart from requiring DSS schools to improve their fee remission/scholarship schemes, conduct a comprehensive review to explore effective measures to ensure that students from grassroots families will have a fair chance of studying in DSS schools, such as providing sufficient financial subsidy to needy students for meeting the necessary expenses of studying in such schools other than school fees, and consult the Panel on Education in the review;

Service agreement with school sponsoring body ("SSB")

- notes that up to mid-December 2010, the SSBs of Schools C, D and E that were required to enter into SSB Service Agreements with the EDB have still not entered into such agreements because they consider the school governance structure required under the draft SSB Service Agreement not consistent with that in their incorporation ordinances, and Schools C and E are also concerned about the clause in the School Management Committee ("SMC") Service Agreement that requires the transfer of government-funded assets to the Government upon termination of the SMC Service Agreement;
- expresses concern that some DSS schools which have entered into SSB Service Agreements have not complied with the terms of the agreements, as follows:
 - (a) although a DSS school should form an SMC before it commences operation, 18 DSS schools formed their SMCs after commencing operation. The delays ranged from two days to about nine years, with an average of three years;

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- (b) up to early June 2010, three DSS schools, which commenced operation in 2004-2005 to 2008-2009, had not incorporated their school governing bodies, and the requirement to acquire tax exemption status under the Inland Revenue Ordinance (Cap. 112) had also not been complied with;
 - (c) in three of the four DSS schools visited by Audit, no service agreement between the SSBs and the SMCs/Incorporated Management Committees ("IMCs") was signed, contrary to the requirement of the SSB Service Agreements;
 - (d) up to June 2010, one of the 15 schools examined by Audit, which commenced operation under the DSS in 2003-2004, had not submitted its school development plan to the EDB as required under the SSB Service Agreement signed;
 - (e) school development plans submitted by some DSS schools did not contain all the required information (e.g. school budget, academic goals for students, and criteria for student admission);
 - (f) two DSS schools had not obtained the EDB's prior approval for the improvement works carried out at their school premises, as required by the SSB Service Agreements; and
 - (g) of the 52 SSB Service Agreements signed, only 34 included a clause to provide the Director of Audit with the right of access to the records and accounts of the DSS schools;
- expresses concern that no record was kept by the EDB on the signing of service agreements between the SSBs and the SMCs/IMCs. Hence, the EDB was not able to ascertain if this requirement has been complied with;
 - acknowledges that:
 - (a) the Secretary for Education has agreed with the audit recommendations in paragraphs 3.13, 3.29 and 3.33 of Chapter 1 of the Director of Audit's Report ("Audit Report");

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- (b) the EDB has agreed to revise the draft SSB Service Agreement for Schools C, D and E to allow them to be managed and operated under their original governing framework. The EDB also intends to refine the clause in the SMC Service Agreement for Schools C and E on the transfer of assets to the Government upon the termination of the SMC Service Agreement;
 - (c) as at the end of November 2010, of the three school governing bodies that had not yet acquired tax exemption status, two had acquired the status with effect from 7 June 2010 and 9 November 2010 respectively, and the remaining one was in the process of acquiring the status; and
 - (d) in the EDB Circular No. 12/2010 issued in November 2010, the EDB has required all DSS schools to keep proper administrative and financial records and provide them for examination by the Director of Audit when required;
- urges the Secretary for Education to:
- (a) resolve the conflicts with Schools C, D and E over the terms and conditions of the draft SSB Service Agreement and the SMC Service Agreement as soon as possible to ensure that they will duly enter into the SSB Service Agreements; and
 - (b) take effective measures to ensure early rectification of the non-compliance with the terms of the SSB Service Agreements identified by Audit;

Service agreement with incorporated school governing body

- expresses concern that:
- (a) although 53 DSS schools were required to enter into SMC/IMC Service Agreements with the EDB by June 2010, as at 30 June 2010, 13 of them had not signed the agreements (with three signed in July and August 2010);
 - (b) the composition of some IMCs and SMCs do not comply with the requirements stipulated in the Education Ordinance (Cap. 279) and the SMC Service Agreements respectively; and

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- (c) as at 30 June 2010, eight DSS schools had not signed tenancy agreements with the EDB, although they had been outstanding for about four to 10 years (with one signed in July 2010);
- notes that for the 14 IMCs that do not have an alumni manager (referred to in paragraph 4.13(a)(v) of Chapter 1 of the Audit Report), the history of the schools is relatively short and hence either their alumni associations have not been formed or their graduates are too young to serve as managers;
 - acknowledges that the Secretary for Education has agreed with the audit recommendations in paragraphs 4.7, 4.15 and 4.22 of Chapter 1 of the Audit Report;
 - urges the Secretary for Education to accord a high priority to implementing the above audit recommendations, taking into consideration the special circumstances of the schools concerned;

School fee remission/scholarship schemes

- notes that DSS schools are required to adopt a fee remission/scholarship scheme in order that students will not be deprived of the chance to study at DSS schools solely because of their inability to pay school fees;
- finds it totally unacceptable that the EDB has failed to discharge its duty to monitor DSS schools' compliance with its requirements on the amounts of school fee income that should be set aside for the purpose of their fee remission/scholarship schemes, as well as those on the publicity, implementation and eligibility criteria of the schemes, and that the Secretary for Education and the Permanent Secretary for Education are not aware of the non-compliance, as set out below:
 - (a) contrary to the EDB's requirement, the fee remission/scholarship schemes of five DSS schools were not funded from school fee income. According to Audit's assessment, the amounts of school fees set aside by 22 DSS schools for the purpose of their fee remission/scholarship schemes were less than the levels required;
 - (b) even by applying the EDB's practical approach, six schools are still found to have under-provision under the fee remission/scholarship schemes. Of these six schools, three did not set aside the required

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amounts for three consecutive years in 2006-2007, 2007-2008 and 2008-2009, and one of them has not heeded the EDB's repeated advice since September 2005 for rectification;

- (c) according to the EDB's practice, the above cases of non-compliance, which were discovered by the EDB's Finance Division through checking of the schools' audited accounts, were only referred to the EDB's regional education offices for follow-up without bringing up to attention of the Permanent Secretary for Education and the Secretary for Education;
 - (d) contrary to the EDB's requirement, two of the four DSS schools visited by Audit have not mentioned their fee remission/scholarship schemes in their prospectuses. Two other DSS schools have not provided full details of their schemes (e.g. the eligibility criteria and the maximum percentage of fee remission) in their prospectuses. As such, some parents may be unaware of the schools' fee remission/scholarship schemes; and
 - (e) only 23 DSS schools have provided details of their fee remission schemes on their school websites. The eligibility criteria adopted by two of these 23 DSS schools for their fee remission schemes are less favourable than the government financial assistance schemes to students;
- expresses dismay that in 14 DSS schools, the utilisation of their fee remission/scholarship schemes was 50% or less;
 - expresses dismay that under the existing policy of the Comprehensive Social Security Assistance ("CSSA") Scheme, no special grant for school fees would normally be given under the CSSA Scheme to students who choose to attend DSS schools, and this may deprive students from families in receipt of CSSA ("CSSA students") of the chance to study at DSS schools;
 - acknowledges that:
 - (a) the Secretary for Education has agreed with the audit recommendations in paragraphs 3.9 and 3.17 of Chapter 2 of the Audit Report;

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- (b) to avoid misunderstanding arising from different interpretations of the requirements for fee remission/scholarship scheme, the EDB has undertaken to refine the guidelines with a view to clarifying and standardising the practice;
 - (c) the Working Group set up by the EDB will also study possible measures to enhance the transparency and efficacy of the fee remission/scholarship schemes in DSS schools in order to help ensure that students from low-income families will not be deprived of access to DSS schools due to inadequate means; and
 - (d) in all DSS schools, CSSA students are eligible for the schools' fee remission/scholarship schemes, and all the schools adopt the same admission policy in respect of CSSA students and non-CSSA students;
- strongly urges the Secretary for Education to:
 - (a) step up the EDB's monitoring of DSS schools' compliance with its requirements on fee remission/scholarship schemes and to enhance public awareness of the schemes, so that parents can take them into account when considering whether to apply for their children's admission to DSS schools; and
 - (b) take measures to ensure that DSS schools will not discriminate against CSSA students in administering their fee remission/scholarship schemes;
 - strongly urges the Secretary for Labour and Welfare to revise the existing CSSA policy so that special grant for school fees will be given under the CSSA Scheme to students who choose to attend DSS schools;

Revision of school fees

- is surprised and expresses serious concern that:
 - (a) in one of the six approved applications for school fee increase in 2009-2010, supporting documents were not provided by the school to show that it had obtained the required consent from the majority of the parents;

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- (b) of the 30 approved applications for fee increases in 2008-2009, 26 DSS schools had underestimated their projected accumulated operating reserves by the end of 2008-2009; and
 - (c) DSS schools are given flexibility in using their operating reserves of non-government funds to finance large-scale capital works and maintenance works of above-standard facilities, such as construction of additional floors and swimming pools. The charging of such expenditure to the schools' operating reserves may be a justification for applying for substantial school fee increase, which in turn may create additional financial burden on parents;
- acknowledges that:
- (a) the Secretary for Education has agreed with the audit recommendations in paragraphs 4.7 and 4.14 of Chapter 2 of the Audit Report; and
 - (b) the EDB will discuss with DSS schools the need for setting aside separate reserves with designated account for large-scale capital works and their related maintenance, and set out the factors that the schools should consider when planning large-scale capital works, including parents' affordability;
- urges the Secretary for Education to:
- (a) require DSS schools to provide all parents with information on the schools' financial status when they consult parents on their proposal to apply for school fee increase;
 - (b) take effective measures to ensure that the financial projections made by DSS schools in their applications for increasing school fees are fair and reasonable; and
 - (c) accord a high priority to exploring measures to ensure that the planning and undertaking of large-scale capital works by DSS schools will not cause undue impact on their level of school fee and parents' affordability;

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Financial management

- expresses astonishment that, of the four DSS schools visited by Audit:
 - (a) one school used non-government funds to purchase three properties. The properties were held under a purported trust arrangement which was considered improper by the EDB; and
 - (b) contrary to the EDB's guidelines, another school invested part of its surplus funds in financial instruments (e.g. local equities and investment funds) instead of placing them in time deposits and savings accounts;
- expresses serious concern over the following cases of non-compliance with the EDB's rules on the financial management of DSS schools, and that the EDB has failed to detect the non-compliance and, in some cases, to take effective actions to ensure rectification of the non-compliance:
 - (a) the EDB has not set a reserve ceiling for DSS schools, contrary to the requirement stipulated in Financial Circular No. 9/2004;
 - (b) as at 31 August 2008, the accumulated operating reserves of 13 DSS schools exceeded the level equivalent to a full year's operating expenses. However, one of them has refused to submit a development plan, setting out how its accumulated operating reserve would be used for school development, to the EDB as required;
 - (c) the 2007-2008 audited accounts of DSS schools indicated that six schools had not followed the EDB's requirement on maintaining accumulated operating reserves sufficient to meet at least two months' operating expenses. As at 31 August 2009, the accumulated operating reserves of two of the schools were still below the required level;
 - (d) as at 30 September 2008, 162 non-local students were admitted by 17 DSS schools. Given that local and non-local students at these schools paid the same level of school fees, and the schools maintained no separate accounts for the non-local students, it is possible that their non-local students had been cross-subsidised by the DSS subsidy for the local students; and

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- (e) the external auditors of 18 DSS schools did not state in their reports on the schools' accounts that the schools had used government subsidies in accordance with the rules promulgated by the EDB for the DSS;
- acknowledges that:
 - (a) the Secretary for Education has agreed with the audit recommendations in paragraphs 5.8, 5.13, 5.17, 5.22, 5.28, 5.32, 5.36, 5.44, 5.48, 5.52 and 5.60 of Chapter 2 of the Audit Report;
 - (b) the Secretary for Financial Services and the Treasury has agreed with the audit recommendations in paragraphs 5.8, 5.17 and 5.22 of Chapter 2 of the Audit Report;
 - (c) the Supervisor of the school which had used non-government funds to purchase three properties has informed the EDB that the SMC had accepted the legal advice to apply to court for a vesting order to transfer the three properties to the SMC;
 - (d) the EDB will request DSS schools to make detailed disclosure on purchase of properties in their accounts from 2009-2010 onwards; and
 - (e) in the EDB Circular No. 12/2010 issued in November 2010, the EDB has provided guidelines to DSS schools on devising a school-based mechanism on investment by using non-government funds;
- urges the Secretary for Education to:
 - (a) closely monitor the progress made by the school concerned in transferring the three properties to the SMC to ensure that the transfer would be completed without delay;
 - (b) put in place measures to enhance the internal control of DSS schools and take effective intervention measures to ensure timely rectification of identified cases of non-compliance;
 - (c) consider devising a self-assessment system for DSS schools to declare if they have complied with the various financial

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management requirements of the EDB and request the schools to document the justifications for not complying with the requirements; and

- (d) provide more training for staff of DSS schools to familiarise them with the EDB's various requirements in financial management to help ensure compliance;

Admission process

- expresses serious concern that:
 - (a) in five admission cases, the assessment on the applicant schools' track records of performance was not based on up-to-date and relevant information;
 - (b) as at June 2010, the profit-making status of five DSS schools (four admitted to the DSS in 1999-2000 and one in 2000-2001) still remained unchanged, although they were required to complete the procedures in acquiring a non-profit-making status within one year after admission; and
 - (c) as at June 2010, two schools (conditionally admitted to the DSS in 1999-2000) that were required to secure their own school premises by the end of 2004-2005 were still operating in leased premises;
- acknowledges that:
 - (a) the Secretary for Education has agreed with the audit recommendations in paragraphs 2.6 and 2.15 of Chapter 1 of the Audit Report; and
 - (b) all schools joining the DSS from 2007 onwards are required to meet all the DSS admission conditions upon admission to the DSS;
- urges the Secretary for Education to:
 - (a) sort out immediately the remaining issues concerning the Deed of Novation and Assignment with the five DSS schools to facilitate their completion of the procedures for acquiring non-profit-making status; and

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- (b) strictly enforce the rule to require all schools joining the DSS to meet all the relevant requirements immediately upon their admission to the DSS;

Monitoring school performance

- expresses concern at the following:
 - (a) the paucity of audits carried out on DSS schools each year, which ranged from two to eight during 2005 to 2009, and of the School Audit Section's staff deployed for undertaking duties relating to audits of DSS schools and follow-up work, which ranged from 0.4 to 1.7 in the same period;
 - (b) the EDB's selection of schools for audit has not been based on a systematic risk analysis mechanism;
 - (c) there has been delay in issuing school audit reports to 11 schools, with two schools over 200 days;
 - (d) no follow-up school audit has been carried out even though glaring malpractices have been identified during school audits;
 - (e) only five (25%) of the 20 DSS schools examined by Audit have uploaded their school plans and reports to their websites as required by the EDB;
 - (f) some school reports uploaded by DSS schools to their websites do not provide the required information (such as financial summary, student performance and feedback on future planning); and
 - (g) two DSS schools have been excluded from the External School Review simply because they were either offering a non-local curriculum or only sixth form classes;
- acknowledges that:
 - (a) the Secretary for Education has agreed with the audit recommendations in paragraphs 5.13, 5.23 and 5.29 of Chapter 1 of the Audit Report; and

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- (b) the EDB plans to increase the number of school audits to 12 in 2010-2011;
- urges the Secretary for Education to deploy sufficient manpower resources to carry out more audits on DSS schools, so as to ensure that the schools use government and school funds properly;

Direct Subsidy Scheme subsidy

- expresses dissatisfaction and finds it unacceptable that:
 - (a) the then Education and Manpower Bureau did not always provide the Legislative Council ("LegCo") with full and accurate information about the changes in measures introduced to the DSS;
 - (b) the then Education and Manpower Bureau did not seek approval from the LegCo's Finance Committee ("FC") for the introduction of the two-tier system, although it had financial implication to the Government; and
 - (c) the then Education and Manpower Bureau did not inform the FC that exception had been given to a school to ensure that it would continue to receive the old DSS subsidy rate after the two-tier system was introduced;
- acknowledges that the Secretary for Financial Services and the Treasury has agreed with the general principles in the audit recommendations in paragraph 6.15 of Chapter 1 of the Audit Report;
- urges the Secretary for Education to ensure that accurate and complete information is always provided to the LegCo;

International schools in the Direct Subsidy Scheme

- expresses dissatisfaction and finds it unacceptable that:
 - (a) the then Education and Manpower Branch did not inform the FC that School I, which had agreed in 1991 to meet its full operating cost, would be given recurrent subsidy upon its admission to the DSS in 1994; and

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- (b) despite the decision of the Executive Council ("ExCo") that international schools should no longer be eligible for admission to the DSS and those already in the scheme should be phased out gradually, in the Memorandum submitted by the Administration to the ExCo, the then Education and Manpower Branch did not include School I in the list of international schools to be phased out and the records of the then Education Department could not explain why School I should not be phased out;
- acknowledges that the Working Group set up by the EDB will critically review the justifications for continuing to allow School I to remain in the DSS;
- urges the Secretary for Education to:
 - (a) proactively keep the LegCo informed when there are major changes to the information previously provided to the LegCo;
 - (b) ensure that complete information is always provided to the ExCo; and
 - (c) having regard to the results of the Working Group's review on the justifications for continuing to allow School I to remain in the DSS, take appropriate measures to address the matter as necessary;

Human resource management

- expresses serious concern that, of the four DSS schools visited by Audit:
 - (a) three schools did not carry out open recruitment for some staff recruited in 2007-2008 to 2009-2010;
 - (b) two schools did not follow the EDB's requirements of reporting the results of their staff recruitments to their governing bodies in 2008-2009 and 2009-2010;
 - (c) one school has not set up a mechanism for determining the remuneration packages for its non-teaching staff as required by the EDB;

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- (d) one school did not have a formal staff performance management system in place. In another school, performance appraisal was carried out only for some staff. In the third school, six staff appraisal reports were not available for examination by Audit. In the remaining school, the appraisers were not required to record the justifications of their assessments; and
- (e) in one school, the decisions of the SMC on contract renewal of staff members were not based on performance appraisals;
- acknowledges that the Secretary for Education has agreed with the audit recommendations in paragraphs 6.12, 6.17, 6.21 and 6.25 of Chapter 2 of the Audit Report;
- urges the Secretary for Education to:
 - (a) provide more training for staff of DSS schools to familiarise them with the EDB's various requirements in human resource management to help strengthen the schools' internal control mechanism; and
 - (b) consider requiring DSS schools to declare if they have complied with the EDB's requirements in human resource management matters and document the justifications for not following the requirements;

General administration

- expresses serious concern that, of the four DSS schools visited by Audit:
 - (a) three schools have not sought prior approval from the EDB for some trading operations carried out by them; and
 - (b) two schools have accepted donations from trading operators without any documented compelling reasons, and made no disclosure in the school reports;
- expresses concern that, of the four DSS schools visited by Audit:
 - (a) one school has not laid down any formal procurement policy and procedure. In another school, the procurement procedures for

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making procurement with non-government funds are less stringent than those of the EDB's guidelines for aided school. No record is available showing that the adoption of the less stringent procedures has been approved by the SMC and made known to the stakeholders of the school;

- (b) in three schools, no record is available showing that the staff involved in purchasing and supplies duties has signed the required undertaking that they would declare to the school governing body any current or future connections they or their immediate families have/will have with the suppliers;
 - (c) the profit of some of the items sold by three schools has exceeded the 15% profit ceiling set by the EDB; and
 - (d) no tender/quotation exercise has been carried out by one school for the selection of the tuckshop operator, and by another school for the selection of operators/suppliers for operating the school tuckshop, the provision of school bus service and the supply of lunch boxes;
- acknowledges that the Secretary for Education has agreed with the audit recommendations in paragraphs 7.12 and 7.23 of Chapter 2 of the Audit Report;
 - urges the Secretary for Education to expeditiously implement the above audit recommendations;

Other governance issues

- expresses concern that:
 - (a) the composition of the school governing bodies of six DSS schools (incorporated under their respective incorporation ordinances) does not include representatives of parents and teachers as school managers, which is not in line with modern corporate governance practices;
 - (b) there is no requirement to disclose to the public the particulars of school managers (name, tenure of office and category of each manager) of SSBs other than the IMCs; and

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- (c) of the four DSS schools visited by Audit:
- (i) the attendance rates of some school managers at the school governing body meetings held by two schools were low;
 - (ii) a quorum was not present at some school governing body meetings held by two schools; and
 - (iii) all the four schools did not comply fully with the requirements stipulated in the EDB's guidelines and the Education Ordinance on managing conflict of interests;
- acknowledges that the Secretary for Education has agreed with the audit recommendations in paragraphs 2.8, 2.15, 2.23 and 2.28 of Chapter 2 of the Audit Report;
 - urges the Secretary for Education to expeditiously implement the above audit recommendations; and

Follow-up actions

- wishes to be kept informed of:
 - (a) the progress made by the Working Group in reviewing the governance framework, internal control and enforcement mechanism and financial management of DSS schools; and
 - (b) the progress made in implementing the various recommendations made by the Committee and Audit.