

ITEM FOR FINANCE COMMITTEE

**HEAD 156 – GOVERNMENT SECRETARIAT :
EDUCATION AND MANPOWER BUREAU
Subhead 000 Operational Expenses**

Members are invited to approve –

- (a) a departure from the approved annual adjustment mechanism for the Operating Expenses Block Grant for aided schools in the 2003/04 school year, by
 - (i) applying the outstanding 1.65% reduction deferred from the 2002/03 school year with effect from September 2003; and
 - (ii) after the revision in (i) above, deferring from September 2003 to January 2004 the regular annual adjustment based on the movement of the Composite Consumer Price Index between June 2002 and June 2003; and
- (b) in respect of the Capacity Enhancement Grant¹, a revised schedule of rates for government and subvented schools² with effect from the 2003/04 school year.

/PROBLEM

¹ The Capacity Enhancement Grant is a constituent grant of the Operating Expenses Block Grant for aided schools and the Subject and Curriculum Block Grant for government schools.

² For the purpose of disbursement of the Capacity Enhancement Grant, “subvented schools” means aided schools, caput schools and schools in receipt of government subsidies for running the full-time initiation programme for newly arrived children. Any additional provision to aided schools will also lead to increased subsidies to schools under the Direct Subsidy Scheme according to an approved formula.

PROBLEM

We need to decide how the current rates of the Operating Expenses Block Grant (OEBG) for aided schools should be price-adjusted for implementation in the 2003/04 school year. Separately, the present two-tier rate structure for the Capacity Enhancement Grant (CEG) does not encourage effective use of public money.

PROPOSAL

2. For the OEBG, we propose to –
 - (a) apply the outstanding 1.65% reduction deferred from the 2002/03 school year with effect from September 2003, instead of offsetting the reduction against upward adjustments in future years (as approved by this Committee in November 2002);
 - (b) price-adjust the rates as revised in (a) above for application in the 2003/04 school year in accordance with the movement of the Composite Consumer Price Index (CCPI) between June 2002 and June 2003; and
 - (c) defer the application of the price-adjusted rates in (b) above from September 2003 to January 2004, in order to reduce the impact of the aggregate adjustment in (a) and (b) above on aided schools.

3. For the CEG, we propose to refine the existing schedule of rates, with effect from the 2003/04 school year, by –
 - (a) introducing a separate set of rates for special schools, on top of the existing ones for primary and secondary schools;
 - (b) setting a basic rate for schools with number of classes below a threshold (i.e. primary schools with six classes or less, secondary schools with 12 classes or less and special schools with five classes or less); and
 - (c) setting a per-class rate for each class beyond the threshold in (b) above, with the total amount of grant subject to a maximum rate which is equivalent to the provision for 24 classes for primary and secondary schools, and for 19 classes for special schools.

Encl. Details are shown in the Enclosure.

/JUSTIFICATION

JUSTIFICATION**Price adjustment of the OEBG**

4. In May 2000, Members approved the consolidation of various non-salary recurrent grants for aided schools to become the OEBG which would be adjusted annually in accordance with the movement of the CCPI.

5. In November 2002, Members approved a departure from the above annual adjustment mechanism when determining the OEBG for the 2002/03 school year. The departure entails a downward adjustment of the rates of the OEBG by 1.65%, instead of by 3.3% reflecting the CCPI movement between June 2001 and June 2002, and the deferment of the remaining 1.65% downward adjustment to later years by not making any upward adjustments in the grant rates until the outstanding reduction is fully offset. On the same occasion, the Administration undertook to examine the accounts and expenditure patterns of aided schools and study whether the CCPI was an appropriate reference for the OEBG adjustments.

Effecting the outstanding reduction deferred from the 2002/03 school year

6. With the special relief measure in paragraph 5 above, there is now a discrepancy between the rates of constituent grants under the OEBG for aided schools and the rates of similar grants under the Subject and Curriculum Block Grant (SCBG) for government schools. This is because the rates of the SCBG in the 2002/03 school year have reflected the full downward adjustment of 3.3% in accordance with the CCPI movement. Given the deflationary environment, it is unlikely that the discrepancy between the rates for similar grants under the two block grants will be bridged in the short term. Prolonged discrepancy would cause unnecessary misconception that we adopt disparity treatment for government and aided schools and have different requirements on schools in the two sectors. We have therefore reviewed whether it is possible to effect the deferred 1.65% reduction of the OEBG as soon as possible, having regard to the accounts and expenditure patterns of aided schools.

7. According to audited accounts received from aided schools for the 2000/01 and the 2001/02 school years, over 70% of the schools had accumulated a surplus ranging from more than \$0.2 million to \$3.6 million under the General Domain³ and over 99% of the schools had a surplus in their Special Domain³, of which about 50% had a surplus ranging from more than \$0.2 million to \$3.6 million.

8. We have also taken a more detailed look at the utilisation of two of the constituent grants under the General Domain of the OEBG, the Administration Grant (AG, available to secondary, primary and special schools) and the Revised Administration Grant (RAG, available to primary and special schools which do not opt for AG), used for the employment of janitors/clerks and the engagement of related services. According to the 2001/02 expenditure of aided schools, the AG or the RAG constituted, on average, about 50% of the OEBG provision. The proportion in respect of aided primary, secondary and special schools was around 40%, 60% and 50% respectively. An analysis of the 2000/01 and the 2001/02 audited accounts from aided schools showed that the overall utilisation rate of the AG/RAG was 93.5% in 2000/01 and 93.8% in 2001/02, i.e. not all allocated funds were exhausted. In fact, about 50% of the schools had accumulated a surplus up to \$0.2 million while another 20% of the schools a surplus ranging from more than \$0.2 million to \$1.4 million. If some aided schools find that they do not have sufficient funds in the AG/RAG for the engagement of janitors/clerks or related services, they can make use of the flexibility for virement of funds between constituent grants under the General Domain to top up the difference. Furthermore, noting that the majority of aided schools had surpluses in their Special Domain, and to provide additional flexibility, we will, through administrative means, allow those aided schools that have difficulty in fulfilling the contractual commitments they have made in the engagement of janitors/clerks to transfer their Special Domain surpluses to top up the AG/RAG items. To prevent abusive transfer of surpluses out of the Special Domain, such arrangement will be allowed as an exception rather than a rule and is confined to covering the costs to be incurred in the continued employment of janitor/clerical staff already committed by the concerned schools.

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³ The OEBG comprises two domains, a General Domain and a Special Domain. Schools are free to set flexibly the allocations for each constituent grant under the General Domain. If surpluses within this domain are available, schools may use them to top up expenditure on items under the Special Domain or use the money on items chargeable to other government subsidies outside the OEBG. The Special Domain contains funds which can only be used for specified purposes. Each grant within the Special Domain is separate and no virement will be allowed among the grants. Furthermore, funds in the Special Domain cannot be transferred out of the domain.

9. In summary, we are satisfied that the vast majority of aided schools should not have cashflow difficulty if the Government is to effect, in the 2003/04 school year, the outstanding 1.65% downward adjustment deferred from the 2002/03 school year. As an indication, adjustment by -1.65% would mean reduction in the OEBG for a bi-sessional primary school operating 24 classes in each of the two sessions and a 30-class secondary school by \$65,000 and \$75,000 respectively. For individual aided schools which may encounter problems, we will follow up with them case by case. We will assess, for instance, the nature and extent of their particular problem and help them better plan their budget for various activities.

Price-adjusting the OEBG for implementation in the 2003/04 school year

10. In our review of the accounts and the expenditure pattern of aided schools, we have considered the suggestion for the Government to compile a school-specific CCPI by focusing only on expenditure items relevant to schools. However, compilation of a school-specific CCPI will involve a separate school operating expenses survey with dubious benefits. We have concluded that we should continue to price-adjust the OEBG in accordance with the movement of the CCPI, as approved by this Committee in May 2000.

11. Accordingly, the OEBG rates restored as per paragraph 2(a) above should be price-adjusted according to the CCPI movement between June 2002 and June 2003. The said CCPI movement will not be available until the latter part of July this year. Assuming a CCPI movement of -1.5%, which is the forecast of the CCPI for 2003 as a whole, aided schools will receive an OEBG reflecting an estimated aggregate price adjustment of about -3.15%, i.e. after effecting the outstanding -1.65% adjustment deferred from the 2002/03 school year and enforcing the 2003/04 adjustment at the provisional rate of -1.5% (the latter is subject to revision according to the CCPI movement between June 2002 and June 2003). To reduce the impact of the aggregate effect on aided schools, we propose to defer the latter price adjustment to January 2004. With this proposal, the rates for the constituent grants under the OEBG for aided schools and those for similar grants under the SCBG for government schools will be fully aligned starting from January 2004.

12. We are meanwhile conducting a fundamental review of grants to aided schools with a view to merging the grants and allowing more flexibility in their usage. Our aim is to implement the new arrangements in the 2004/05 school year.

CEG

13. The existing schedule of the CEG rates consists of two tiers only, one for schools with 19 or more classes and the other for schools with less than 19 classes. However, given the wide range in the size of schools, the CEG rates may be excessive for small-sized schools with number of classes well below 19. We note, for example, that the CEG utilisation rates of primary schools with six classes or less were 58% and 65% in the school years 2000/01 and 2001/02 respectively, compared to 63% and 76% for schools with 13 to 18 classes in these two school years respectively. For secondary schools with six classes or less, the utilisation rates were 58% and 53% in the two school years respectively, compared to 69% and 76% for schools with 13 to 18 classes in the same two school years respectively. The Audit Commission, in a recent value for money audit on primary education, also pointed out that it would not be necessary for schools with a small number of classes to be given the full amount of grant currently set for schools with less than 19 classes. It recommended the introduction of more funding levels for CEG for different number of operating classes in schools. We agree with the Audit Commission's observations and recommendation.

14. Special schools in general have fewer classes than ordinary schools. If we are to modify the schedule of rates for primary and secondary schools to better address the needs of schools with different numbers of operating classes, we consider it justified to introduce a separate set of rates for special schools to cater for their special circumstances.

15. To improve the schedule of CEG rates, we propose to set a lower level of grant rate in each of the cases of primary, secondary and special schools to address the circumstances of small-sized schools within each category. This new set of rates, to be called the "basic rates", ensures that small-sized schools can still receive an amount sufficient for hiring one or two additional staff, or procuring equivalent service, throughout the year. The basic rates will apply to schools with the following class size –

Secondary schools	12 classes or less
Primary schools	6 classes or less
Special schools	5 classes or less

The proposed thresholds take into account the most common number of classes in what would be regarded as small-sized schools within each school category. In the case of secondary schools, the basic rate is calculated on the basis of the cost of two full-time teaching assistants. In the case of primary and special schools, the basic rate is calculated on the basis of one full-time and one part-time teaching assistants. In all cases, reference is made to the packages for non-civil service contract staff employed by the Government to comparable jobs.

16. For each class beyond the threshold covered by the basic rate, we propose a per class rate of CEG to ensure that the amount of grant received by the schools would better correspond to their operational needs, which depend largely on the number of operating classes.

17. We further propose to cap the amount of grant received by schools under the revised schedule because large-sized schools may benefit from the economy of scale, and thus have more room for redeployment to meet their operational needs. The cap is proposed to be equivalent to the provision for 24 classes for primary and secondary schools, and 19 classes for special schools. The ceilings are equivalent to the maximum rates permissible under the existing two-tier system of CEG rates.

18. The proposed schedule of rates drawn up on the basis of considerations in paragraphs 14 to 17 above are set out in the Enclosure. Apart from our proposed refinement to the schedule of CEG rates, all other aspects of the CEG will remain unchanged.

19. The CEG is one of the constituent grants under the OEBG for aided schools and under the SCBG for government schools. The proposed rates set out in the Enclosure is at the price level of the 2002/03 school year. The proposed rates will still be subject to price adjustment (in accordance with the movement of the CCPI between June 2002 and June 2003) for implementation in the 2003/04 school year. In the case of aided schools, this price adjustment will be deferred to January 2004 as proposed in paragraph 2(c) above.

FINANCIAL IMPLICATIONS

20. We estimate that the proposal to effect the outstanding 2002/03 downward adjustment of 1.65% in the 2003/04 school year in respect of the OEBG will achieve savings of about \$52 million in the 2003/04 school year (or \$36 million in the 2003-04 financial year). As for the proposed deferment of the adjustment of OEBG rates for the 2003/04 school year to January 2004, assuming that the movement of CCPI from June 2002 to June 2003 is -1.5%, the Government will have to incur an estimated additional expenditure, in terms of savings foregone, of about \$15 million in the 2003/04 school year and in the 2003-04 financial year.

21. As regards the proposed refinements to the schedule of CEG rates, we estimate that the proposal will achieve savings of about \$60 million in the 2003/04 school year (or \$59 million in the 2003-04 financial year).

BACKGROUND INFORMATION

22. Representatives from schools councils, major school sponsors, unions of school heads, teachers' unions and clerical and janitor unions were consulted on our OEBG proposals on 15 and 16 April 2003. They generally did not raise any objection. For our CEG proposals, we consulted schools councils, unions of school heads and other educational associations on 7 March 2003, and they accepted our proposals. We subsequently consulted the Legislative Council Panel on Education on the OEBG and the CEG proposals on 28 April 2003 and 17 March 2003 respectively. The Panel did not raise any objection.

Education and Manpower Bureau
May 2003

Schedule of Proposed Rates of Capacity Enhancement Grant

The proposed rates of the Capacity Enhancement Grant at the price level of the 2002/03 school year are set out below⁴ –

	Secondary (per annum)	Primary (per annum)	Special (per annum)
Basic rate	\$240,067 (first 12 classes)	\$151,600 (first 6 classes)	\$151,600 (first 5 classes)
Maximum provision	\$430,363 (24 or more classes)	\$526,000 (24 or more classes)	\$526,000 (19 or more classes)
Rate per class for classes in addition to the threshold number	\$15,858	\$20,800	\$26,743

The existing schedule of CEG rates at the price level of the 2002/03 school year are set out below for reference –

	Secondary (per school per annum)	Primary (per school per annum)
Less than 19 classes	\$358,636	\$430,363
19 classes or more	\$430,363	\$526,000

⁴ These proposed rates have assumed that the 1.65% outstanding reduction not reflected in the 2002/03 school year for the subvented schools has been fully effected. The rates are still subject to price adjustment in the 2003/04 school year according to the movement of the Composite Consumer Price Index between June 2002 and June 2003.