For information
on 20 April 2012

Legislative Council Panel on Education

Improvement measures to the administration and governance of Direct Subsidy Scheme (DSS) Schools

PURPOSE

This paper aims to brief Members on the measures to improve the administration and governance of DSS schools recommended by the Working Group on DSS (Working Group) which has been set up under the instruction of the Secretary for Education (SED) to study the recommendations put forward in the Report No. 55 of the Public Accounts Committee (PAC Report) of the Legislative Council.

BACKGROUND

2. As reported in the LC Paper No. CB(2)2291/10-11(01) of 11 July 2011, the Working Group, chaired by the Permanent Secretary for Education, had been set up in February 2011. The task is to review and make recommendations for improving the administration of the DSS as well as DSS schools' governance and administration. After almost 10 months of deliberation and extensive and iterative consultations with the DSS schools sector (including the Hong Kong DSS Schools Council, School Management Committee (SMC)/Incorporated Management Committee (IMC) members, school sponsors, parents, principals as well as senior management staff of DSS schools), the Working Group submitted its report to the SED on 30 December 2011. The SED accepted all the recommendations put forward in the report on 17 February 2012.

ISSUES DISSCUSSED AND RECOMMENDATIONS MADE

3. The Working Group holds the view that the policy objective of the DSS, i.e. enhancing parental choice and enriching our education system through increasing the diversity in our school system should continue to be maintained. Therefore, the Working Group has focused its deliberation on enhancing the transparency of schools' operation and enabling DSS schools to strengthen their governance and internal control, thereby ensuring that DSS schools are properly managed by their own SMC/IMC. This approach, in the opinion of the Working Group, suits DSS schools most as it draws a sensible balance between maintaining the flexibility enjoyed by DSS schools and the diversity in the school system on the one hand, and enhancing the management and accountability of DSS schools on the other.

4. In fact, the transparency of schools' operation has been gradually enhanced since the release of the Report No. 55 of the Director of Audit (Audit Report) and PAC Report No. 55. For example, in the annual school fee revision exercise, DSS schools are now required to provide parents, in the consultation process, with appropriate financial information of the schools, including the accumulated surplus, justifications for fee increase and additional resources required, etc. We note Members' request made at the meeting of the Panel on Education held on 11 July 2011 for a sample of the financial information provided by a DSS school to parents in the last school fee revision exercise. Such a sample is enclosed at Annex I.

Recommendations

5. The Working Group's recommendations mainly cover five aspects, namely, fee remission/scholarship schemes, governance and internal control of DSS schools, financial management of DSS schools, training for school personnel of the DSS schools, and measures to ensure compliance of requirements of the DSS by schools. In addition, the Working Group has also made its recommendation on the DSS status of Li Po Chun United World College (LPCUWC). The essence of the

Working Group's recommendations and their rationale are set out in the ensuing paragraphs.

A. Fee Remission/Scholarship Schemes

Enhancing transparency and access of information

6. The Working Group considers that transparency (implying access to updated information on how the fee remission systems of DSS schools operate) is the prerequisite to ensuring a fair chance of admission to DSS schools for students from different socio-economic strata. To this end, the Education Bureau (EDB), upon the Working Group's recommendation and with SED's endorsement, issued a circular in early July 2011 setting out new measures to enhance the accessibility of information of fee remission/scholarship schemes in individual DSS schools[1]. The Working Group has further recommended in its report that the EDB should keep in view the implementation of the improvement measures and, where appropriate, take necessary measures to ensure compliance by DSS schools.

Uncertainties faced by schools with utilization of fee remission/scholarship far exceeding the reserves set aside as required

7. Quite a number of DSS schools admitting a large number of needy students have used more than 100% of the school fee incomes set aside for fee remission/scholarship. Based on the latest information available (i.e. the 2009/10 audited accounts), we have compiled information, as requested at the meeting of the Panel on Education held on 11 July 2011, on the utilization of the fee remission/scholarship schemes of DSS schools at Annex II. It is noteworthy that 30 or 42% of the DSS schools have used more than 100% of the fee remission/scholarship provisions. To avoid creating pressure for tuition fee increase on schools which have fully utilized their fee remission/scholarship provisions, the Working Group has recommended that DSS schools meeting the following criteria be allowed to apply to the

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[1] The new measures have been set out in Education Bureau Circular No. 2/2011 on *Fee Remission/Scholarship Schemes in DSS Schools*.

EDB for exemption from the “no less favourable”[2] requirement:

(a) the utilization rates of their fee remission/scholarship provisions are 100% or more in the past three consecutive years; and

(b) two thirds of their fee remission/scholarship provisions or more have been used for fee remission.

In addition, DSS schools given exemption should ensure that (i) students receiving fee remission before the schools adopt the revised eligibility criteria will not be affected and (ii) sufficient notice will be given to prospective parents/students before implementing the new eligibility criteria. The Working Group believes that this arrangement can help DSS schools admitting a large number of needy students continue to take care of needy students on the one hand and maintain a viable mode of operation in the long run on the other.

Better utilization of fee remission/scholarship reserves in through-train secondary and primary schools

8. There is a close connection between through-train primary and secondary schools. To facilitate better utilization of fee remission/scholarship reserves in through-train secondary and primary schools, thereby enabling them to admit more needy students overall, the Working Group has recommended that through-train secondary and primary schools be allowed to transfer a maximum of 50% of the fee remission/scholarship reserves of the linked primary school to the linked secondary school or vice versa should they meet the following conditions and obtain prior approval from their SMC/IMC:

(a) the utilization rates of the fee remission/scholarship provisions of the linked secondary/primary school receiving funds are 100% or more as reflected in the audited accounts of the past three consecutive years; and

(b) two thirds of the fee remission/scholarship provisions or

[2] Currently, each DSS school is required to offer to parents a fee remission/scholarship scheme with a set of eligibility benchmarks no less favourable than the government financial assistance schemes for students.

more of the linked secondary school/primary school receiving funds are used for fee remission purposes.

B. Strengthening the Governance and Internal Control of DSS Schools

9. The Working Group believes that proper school governance and internal control mechanisms will facilitate SMC/IMC in managing their DSS schools properly and in complying with the EDB's requirements. Nevertheless, the Audit Commission's and Public Accounts Committee's findings reveal that the EDB can continue to rely on schools' internal governance only if it is able to identify a way to ensure that the internal governance of DSS schools is sound. To this end, the Working Group has proposed a framework comprising three inter-related aspects to help DSS schools strengthen their internal governance. Details are in paragraphs 10 to 12 below.

Completion of a self-evaluation checklist

10. The first aspect of the framework is a self-evaluation checklist. The Working Group considers that through completing a self-evaluation checklist which sets out the processes essential to the integrity of schools' various management systems, DSS schools will increase their awareness of the need, and be guided, to put in place checks and balances for self improvement. The Working Group has therefore recommended that DSS schools be required to conduct self-assessment by completing regularly a self-evaluation checklist covering four important areas of school operations, namely general administration of school governing body, operation of school fee remission/scholarship schemes, human resources management matters and financial management matters.

Mechanism under the SMC/IMC to conduct governance review on a regular basis

11. The second aspect of the framework is to set up a governance review sub-committee accountable to the SMC/IMC. Given the potential liability of an SMC/IMC for possible mishaps in its DSS school that is fee-charging and granted with greater operational flexibility and

autonomy, the Working Group sees the merits of setting up, under the SMC/IMC, a governance review sub-committee for conducting *system review* of various key management and financial control systems and processes including whether the various checks and balances are working as intended. Different stakeholders of the DSS schools sector have different views on the proposed governance review sub-committee. While some school sponsors, SMC/IMC and principals welcome it, some DSS school principals have reservations. They consider the proposed set-up unnecessary and detrimental to the mutual trust between the SMC/IMC and the Executive led by the principal. After iterative discussions with the DSS schools sector and careful deliberation of their views, the Working Group remains of the view that such a set-up is necessary to provide the SMC/IMC with an instrument to better ensure that the management and financial control systems and processes are working as intended and as reported. Nonetheless, the Working Group has suitably modified the original proposal and clarified areas of concern about the positioning, functions and composition of the governance review sub-committee. In sum, all DSS schools are required to set up by the 2013/14 school year a governance review sub-committee (or any other name that the SMC/IMC sees fit) to assist the SMC/IMC in reviewing the integrity of various management and financial systems and processes.

Essential items to be discussed at SMC/IMC meetings

12. The third aspect of the improved governance framework is to devise a list of essential items to be discussed at SMC/IMC meetings. The list, in the view of the Working Group, can enhance the accountability and governance of the SMC/IMC by helping to forestall the inadvertent oversight of essential administrative and management issues. These essential matters include human resource policies for senior teaching and administrative posts, annual school budgets, large-scale capital works (if any), procurement of services/goods through tendering with significant financial implications (if any), operation of the fee remission/scholarship scheme, fee revision proposals, investment policy and update, advisory letter(s) and/or warning letter(s) from the EDB (if any), and self-evaluation on schools' academic as well as non-academic performance under the School Development and

Accountability Framework.

Management and financial audit

13. In the opinion of the Working Group, internal governance by DSS schools and macro external oversight by the EDB as a regulator are complementary measures. Alongside the recommended measures to help DSS schools strengthen their internal governance as set out in paragraphs 9 to 12 above, the Working Group has recommended that the existing audit inspections conducted by the EDB of DSS schools should be strengthened and replaced by a management and financial audit, which will cover management aspects as well as the use of resources including funds and other forms of resources such as human resources. The Working Group has also recommended that the management and financial audit should commence as from the 2014/15 school year.

Enhancing the transparency of school governance bodies

14. The community especially parents of both prospective and current students of a school have a legitimate interest in knowing who serve on the SMC/IMC. DSS schools with an IMC are already obliged to disclose the composition of the IMC under the Education Ordinance. However, having regard to the provisions of the Personal Data (Privacy) Ordinance, the consent of the school managers of SMC needs to be sought. The Working Group has therefore recommended that (a) consent of managers of DSS schools governed by an SMC be sought of the EDB's disclosure of their information including the name, tenure of office/date of registration and category of school manager; and (b) for schools with managers who refuse to give consent to the proposed disclosure, a remark indicating the number and categories, if applicable, of managers who have not given such consent be posted on the relevant part of the EDB's homepage.

C. Strengthening the Financial Management of DSS Schools

15. The onus of prudent resource deployment of DSS schools is greater than that of their aided counterparts because they may also collect

school fees and enjoy greater flexibility in the use of funds. The Working Group considers it important to set a few basic guidelines on DSS schools' internal financial management which can help enhance transparency and facilitate the IMC/SMC's proper oversight of the school's use of resources. These guidelines are outlined in paragraphs 16 to 22 below.

Clear delineation between the operating reserve and the designated reserves

16. To facilitate proper resource management and enhance transparency of the financial situation of the schools, the Working Group has recommended that DSS schools' reserves should be classified into two categories, namely the operating reserve and the designated reserves. Accumulated surplus [3] arising from both government and non-government funds (except those in the designated reserves) of DSS schools will be classified as the operating reserve of DSS schools. Designated reserves, on the other hand, may include (i) fee remission/scholarship reserve, (ii) long service payment reserve, (iii) donations with specific purposes and (iv) a new reserve for constructing, maintaining and upgrading above-standard facilities. Such delineation of reserves is also necessary for the implementation of other improvement measures as set out in paragraphs 17 to 22 below.

Setting a ceiling for schools' operating reserve

17. In accordance with the requirement to set a reserve ceiling for surplus funds for other subvented organizations, the Working Group has recommended that the ceiling on the operating reserve of DSS schools should be set at an amount equal to 100% of the annual total expenditure, i.e. 12 months' operating expenditure. In determining the appropriate level at which the ceiling should be set, due consideration has been given to the principle that the proposed ceiling should allow ample room for DSS schools to cater for teachers' promotion in the years to come, additional teachers' salary increase, as well as routine repairs and maintenance expenses for standard facilities.

[3] "Accumulated surplus" is the excess of income over expenditure over the years concerned which is retained in the form of assets net of liabilities. Assets include fixed assets, accounts receivable and cash, among others.

18. For schools with accumulated operating reserve exceeding the ceiling, it is recommended that they should be allowed to rectify the situation through either reducing school fees, receiving less DSS subsidy, returning the excess surplus to the Government or transferring the excess surplus to the fee remission/scholarship reserve subject to the fee remission/scholarship reserve being exhausted and the utilization rate of the fee remission/scholarship provisions in the past three years being 100% or more.

Special one-off arrangement

19. Given that DSS schools have all along been allowed to keep, without ceiling, all the accumulated surpluses from both government and non-government funds, the Working Group considers that it may not be fair to apply the new measures in paragraph 18 above to DSS schools right after the new measure of reserve ceiling is introduced. The Working Group has therefore recommended that DSS schools be allowed to grandfather the reserve in excess of the reserve ceiling accumulated before the implementation of the recommendation concerning reserve ceiling subject to the EDB's approval of schools' plans with detailed accounts of their reserves including their types, proposed usage and, where necessary, timeframe for deployment endorsed at SMC/IMC meetings. Nevertheless, the accumulated reserves will be a factor that EDB would consider in assessing proposals for tuition fee increases.

Setting aside school fee income for construction, maintenance and upgrading of above-standard facilities

20. The Working Group acknowledges that maintaining DSS schools' flexibility in using non-government funds to finance above-standard capital works for developing their own characteristics is in the interest of both DSS schools and the diversity of the school system. Nevertheless, the Working Group also holds the view that such hardware enhancement must be pursued prudently to forestall creating an undue pressure for upward adjustment of tuition fees. It has therefore recommended that DSS schools with genuine needs for constructing, maintaining or upgrading above-standard facilities be allowed to set up a

designated reserve for the purpose. To forestall abuse of this flexibility, DSS schools have to meet the following conditions for transferring funds to this reserve:

(a) concrete plans have to be approved by the SMC/IMC;

(b) Parent-Teacher Associations have to be consulted (all parents have to be consulted if the reserve is used for new above-standard capital works);

(c) the amount to be transferred to the reserve for above-standard facilities should be no more than 10% of the school fee income of each school year;

(d) there is no need to consult the EDB beforehand if after the proposed transfer, there remains cash in the operating reserve equivalent in amount to at least six months' the school's expenses; and

(e) the EDB's prior approval should however be sought if the school intends to transfer more than 10% of the annual school fee income or if after the transfer, the cashflow in the operating reserve account falls below six months' expenses of the school. In any case, the cashflow in the operating reserve account should not fall below three months' expenses after the proposed transfer.

Strengthening the prevailing guidelines on investment

21. The Working Group members agree unanimously that DSS schools should focus their effort and resources on enhancing learning and teaching quality instead of indulging in making investment. However, to address the needs of some DSS schools that find themselves fully justified to make certain investments by using their own funds, the Working Group has recommended that permissible investment products should be clearly specified with corresponding guidelines drawn up. These comprise:

(a) the SMC/IMC's approval should be sought before investment decisions are made;

(b) the only funds that may be used for investment are the long service payment reserve, donations with specific purposes and the reserve for construction, maintenance and upgrading of above-standard facilities; and

(c) DSS schools should only be allowed to invest in (i) Hong Kong dollar bonds; and (ii) Hong Kong dollar certificates of deposits.

Strengthening the prevailing guidelines on purchase of properties

22. Currently, the purchase of properties by DSS schools is not encouraged. This notwithstanding, DSS schools can still do so if they have strong justifications and have sought approval from the SMC/IMC and consulted parents. Given the liquidity constraints of and the high risk level associated with properties, the Working Group has great reservations about allowing DSS schools to purchase properties for investment purposes. Nevertheless, respecting the DSS policy intention of promoting diversity, the Working Group has deliberately refrained from making prescriptive recommendations as far as possible. To balance the need to forestall the purchase of property from affecting the proper functioning of a school and the need to respect a school's flexibility to use its non-government funds, the Working Group has recommended that the following two requirements be added to the existing requirements on the purchase of properties by DSS schools:

(a) DSS schools should be allowed to acquire property only if they still have cash in their operating reserve account an amount equivalent to at least six months' operating expenditure after the purchase of properties; and

(b) DSS schools should not be allowed to purchase properties through mortgages or any other borrowing arrangements.

D. Training for DSS Schools

Training for DSS schools

23. To prepare DSS schools to take forward the new proposed improvement measures for enhancing the governance, management and

administration of DSS schools, the Working Group has recommended that suitable and relevant training programmes be provided for them. To ensure that the training programmes meet the practical needs of DSS schools, the Working Group has also recommended that a steering committee on training for DSS schools comprising representatives from the Hong Kong DSS Schools Council, non-school sector professionals and colleagues from different EDB Divisions should be set up.

Training for managers of DSS schools

24. The EDB has been organizing structured training programmes for school managers of aided schools. The Working Group agrees that training sessions with topics relevant to DSS schools should also be open to participation by school managers of DSS schools. We also intend to add an optional module on deployment of resources specifically for DSS school managers to cater for the special needs of managers of DSS schools.

E. Measures to Ensure Compliance of Requirements of the DSS by Schools

25. Taking into account the interests of students, the EDB has always exercised restraint and refrained from drastic measures such as withdrawing DSS subsidies from schools in handling malpractice or non-compliance. However, past experience indicates that reliance on advisory letters to the schools may not be efficacious in addressing identified malpractices. To fortify the existing mechanism to address non-compliance, the Working Group finds it necessary to enhance deterrence, as follows:

(a) escalation of advisory letters to supervisors at the earliest opportunity;

(b) if (a) does not work, escalation of warning letters to SMC/IMC members at the earliest opportunity;

(c) disclosure of the non-compliance or malpractice with the school concerned named on the EDB's website after exhaustion of the steps in (a) and (b) above and if the malpractice remains to be rectified; and

(d) suspension of part of the DSS subsidy if a school fails to comply with an important requirement or rectify serious malpractice after exhaustion of the steps mentioned in (a) and (b) above until rectification is made. In order to ensure that the interests of students are not unduly affected, the EDB will assess the financial situation of the school before withholding the school's DSS subsidy. The EDB may decide to take the measure in (c) prior to, or in addition to, withholding part of the DSS subsidy.

F. Status of Li Po Chun United World College of Hong Kong in the DSS

26. Having reviewed the justifications put forward by the then Education Department (ED) and Education and Manpower Bureau (EMB) for allowing LPCUWC to remain in the DSS in 1999 and 2002, the Working Group fully concurs with the views of the then ED and EMB that LPCUWC is unique in nature and takes the view that the reasons put forward by the then ED and EMB remain valid.

27. The Working Group considers that LPCUWC, being one of the United World Colleges[4] (UWC), is unique in nature. First, it has been offering two-year pre-university education, and hence not in direct competition with other international schools or local schools in Hong Kong. Second, LPCUWC's students come from different parts of the world and are supported by various scholarships. The school's culturally diversified environment enables local students in Hong Kong to enjoy an invaluable opportunity to acquire an international perspective while still being physically in Hong Kong. Besides, the sponsoring body of the school is running various colleges in the world with reciprocal arrangements in the admission of students and scholarship arrangements. Students in Hong Kong enjoy the benefits of attending

[4] As of today, UWC has 13 colleges and schools (including LPCUWC) across five continents all with distinctive characters but sharing the same mission, ethos and values. At most schools and colleges, an average of 70 different nationalities are represented at any one time, and embracing the many nationalities present is an important feature of UWC life, helping students to explore and develop an international appreciation. Academic achievements are put into perspective with a demanding mix of community engagement, international affairs, physical activities and creative pursuits.

various colleges in other education systems world-wide, which will undoubtedly help them broaden their horizon, explore and develop an international appreciation.

28. The Working Group concludes that LPCUWC is an education institute that Hong Kong should value in consideration of the College's culturally diversified school environment and membership in a world league of UWC network, and should continue to receive funding support from the Government. Among the two basic funding modes for schools in Hong Kong, i.e. aided or DSS, the DSS is considered the more appropriate one for LPCUWC as it enables the Government to provide per capita financial support only for local students of the school. With recurrent government subsidies, local students in Hong Kong can enjoy all the benefits brought about by LPCUWC at lower school fees. Any change in the existing funding mode for LPCUWC, in the view of the Working Group, will not be in the interests of local students in Hong Kong. The Working Group has therefore recommended the continuation of the status quo, i.e. that LPCUWC be allowed to continue to remain in the DSS.

29. A summary of the Working Group's recommendations is at Annex III. The full report of the Working Group is available on EDB's website at http://www.edb.gov.hk/index.aspx?nodeID=173&langno=1.

Way Forward

30. Upon the endorsement of the Working Group's Report by the SED, the EDB has immediately started discussions with the DSS school sector with a view to drawing up an implementation schedule for taking forward the Working Group's recommendations. Consultation with the frontline school personnel on the operational details is underway. Some progress has been made in these two months, for example, the steering committee on training for DSS schools is being formed, and we have started the exercise of seeking consent of managers of DSS schools governed by an SMC regarding the disclosure of their information on EDB's homepage. Hopefully the self-evaluation checklist and the list of essential items to be discussed at SMC/IMC meetings could be put to trial

use in the coming school year. In sum, the recommendations would be put in place progressively as from 2012/13 school year, and we anticipate that by the 2014/15 school year, there will be full implementation of all the recommendations.

ADVICE SOUGHT

31. Members are invited to note the content of this paper.

Education Bureau
13 April 2012

Annex I

A sample of the financial information provided by DSS Schools to parents when proposing for school fee revisions

As from the 2011/12 fee revision exercise, DSS schools are required to provide essential information on school's financial situation for parents when conducting parent consultation about their school fee revision proposals. The essential information required which is clearly listed in a template attached to the letter to DSS schools calling for applications for school fee revision includes the following:

(a) services/facilities that will lead to fee increase;

(b) additional funds required for the services/facilities;

(c) projected deficit/surplus in the budget of the school year concerned if the school fee is kept unchanged;

(d) projected deficit/surplus in the budget of the school year concerned after the proposed fee increase; and

(e) operating reserves as reflected in the latest audited accounts.

A sample of the financial information provided by a DSS school to its parents during parent consultation in the 2011/12 fee revision exercise is appended below.

School Fee Application for 2011/2012

Breakdowns of Estimates on Additional Services and Facilities in 2011/2012 (in million dollars)

(Renovations costs not included)

5 Additional Teaching Posts**	1.890	1.890
Library Enahncement		
Additional Technical Assistant**	0.200	
Library Collections	0.350	
Computer and Software	0.380	
AV Equipments	0.030	0.960
PE Enhancement		
Equipments and Consumables	0.320	
Coaches**	0.150	0.470
Art Enhancement and Fashion Design		
Equipments	0.048	
Workshop Assistant**	0.100	
Learning Materials and Consumables	0.030	
Instructors**	0.030	0.208
Band Room		
Musical Instruments	0.300	
AV Equipments	0.060	
Instructors**	0.020	0.380

Out-door Learning Zone		
Facilities	0.130	0.130
English Drama Enhancement**	0.200	0.200
Recurrent Expenses of the New Annex**	1.573	1.573
		5.811

***These items will become recurrent expenses if the services and programmes are to be continued after 2011/2012*

Additional information about related financial situation of the school (for reference)

Total school fee to be collected in 2010/2011	12.440	
Proposed total school fee to be collected in 2011/2012	16.007	
Projected additional school fee to be collected in 2011/2012	3.567	
Estimated Surplus if school fee kept unchanged in 2011/2012	0.371	
Estimated Surplus after school fee increase in 2011/2012	3.938	
Total Expenditure according to Audited Account 2009/2010	37.115	
Average expenditure for each month in 2009/2010	3.093	(a)
Accumulative surplus accoring to Audited Account 2009/201(	16.600	(b)
Total operating reserves in terms of number of month	5.37 months	(a)/(b)

Annex II

Updated information on the eligibility for and utilization of fee remission/scholarship schemes of DSS schools

As set out in the Education Bureau Circular No. 2/2011 on *Fee Remission/Scholarship Schemes in DSS Schools*, DSS schools are required to offer to parents a fee remission/scholarship scheme with a set of eligibility benchmarks no less favourable than the government financial assistance schemes. DSS schools are also required to provide details of their fee remission/scholarship schemes via various channels such as posting such information on their school websites, including such information in application forms for student admission, etc. This will help parents understand the fee remission/scholarship schemes and facilitate an informed assessment of their children's eligibility for remission/scholarship.

According to the latest available audited accounts submitted by DSS schools, i.e. the audited accounts for the 2009/10 school year, the utilization of the fee remission/scholarship provision of DSS schools is summarized as follows:

Utilization rate of fee remission/scholarship provision	Number of Schools / Percentage of Schools
Greater than 100%	30 / 42%
Between 50% and 100%	23 / 32%
Less than 50%	19 / 26%

It is noteworthy that the figures above reflect the situation in the 2009/10 school year, i.e. before the release of the Report No. 55 of the Director of Audit in October 2010 and the Report No. 55 of the Legislative Council Public Accounts Committee in February 2011. In other words, the possible effort made by DSS schools to improve the utilization of their fee remission/scholarship provision has yet to be revealed. With the increased awareness of the need to better utilize fee remission/scholarship reserves among DSS schools, as well as DSS schools' generally positive response to the improvement measures in the Education Bureau Circular No. 2/2011 on *Fee Remission/Scholarship Schemes in DSS Schools*, we expect the utilization rate of fee remission/scholarship provision in DSS schools will improve in the next few years. In fact, we note that those schools with the utilization of the fee remission/scholarship provision below 50% have been stepping up efforts to improve the utilization of their fee remission/scholarship provision through various means. These means include relaxation of the eligibility criteria of their fee remission schemes, provision of additional financial assistance on top of school fee remission, organizing structured promotion activities to primary schools in respect of their remission schemes for needy students, etc. Besides, with the special measure facilitating better utilization of fee remission reserves in through-train DSS schools recommended by the Working Group on DSS, the fee remission utilization can be further stepped up. The Education Bureau will keep in view the development.

Annex III

Summary of Working Group's Recommendations

No.	Recommendation
Improvement Measures for the Fee Remission/Scholarship Schemes	
1	Paragraph 3.5 The Working Group recommends that the EDB should keep in view the implementation of the improvement measures of enhancing the transparency and accessibility of information on fee remission/scholarship schemes in individual DSS schools and provide advice or intervention to schools concerned where necessary.
2	Paragraph 3.8 The Working Group recommends that DSS schools should continue to be given the flexibility to devise their school-based arrangements to offer financial assistance to needy students over and above the current requirements.
3	Paragraph 3.12 The Working Group recommends that: (a) DSS schools be encouraged to continue to explore ways to better utilize their fee remission/scholarship reserve; and (b) the proposal of setting up a centralized fund for fee remission/scholarship purposes be shelved and only be revisited if the situation of under-utilization of fee remission/scholarship reserve by DSS schools persists.
4	Paragraph 3.15 The Working Group does not recommend setting a cap for scholarship.
5	Paragraph 3.18 The Working Group does not recommend mandating DSS schools to surrender a percentage of their school places for central allocation by the EDB.

No.	Recommendation
6	<u>Paragraph 3.24</u> The Working Group recommends the adoption of the measures set out below: (a) DSS schools meeting the following criteria should be allowed to apply to the EDB for exemption from the requirement of adopting eligibility criteria no less favourable than those of the government financial assistance schemes to needy students: (i) the utilization rates of their fee remission/scholarship provisions are 100% or more as reflected in the audited accounts of the past three consecutive years; and (ii) in overall terms, during the three years in question, two thirds of their fee remission/scholarship provisions or more have been used for fee remission purposes as confirmed by the schools. (b) DSS schools given exemption should ensure that: (i) students receiving fee remission before the schools adopt the revised eligibility criteria will not be affected, i.e. they will continue to receive fee remission under the previous eligibility criteria until they graduate from the schools; and (ii) sufficient notice must be given to prospective parents/students before implementing the new eligibility criteria; and in any case, the revision must be made available for public consumption; (c) the exemption to DSS schools would be cancelled once: (i) the average utilization rate of their fee remission/scholarship provisions under the revised eligibility criteria in the past three years is less than 80%; or (ii) in the past three years, on average, less than two thirds of their fee remission/scholarship provisions under the revised eligibility criteria are used for fee remission

No.	Recommendation
	purposes.
7	Paragraphs 3.27 & 3.28 The Working Group recommends that through-train secondary and primary schools be allowed to transfer a maximum of 50% of the fee remission/scholarship reserves of the linked primary school to the linked secondary school should they meet the following conditions and obtain prior approval from the SMC/IMC: (a) the utilization rates of the fee remission/scholarship provisions of the linked secondary school are 100% or more as reflected in the audited accounts of the past three consecutive years; and (b) two thirds of the fee remission/scholarship provisions or more of the linked secondary school are used for fee remission purposes as confirmed by the schools. Following the same logic, the Working Group also recommends that similar flexibility under identical terms be allowed for the transfer of fee remission/scholarship reserves of the secondary school to the linked primary school.
Strengthening the Governance and Internal Control of DSS Schools	
8	Paragraph 4.7 In respect of DSS schools governed by SMC/MC, the Working Group recommends the following: (a) at school level, the EDB to consult schools on disclosure of their composition on the EDB's homepage; (b) at individual school manager level, the EDB to add a checkbox to the application form for registration as a manager with a view to seeking his/her consent of the EDB's disclosure of his/her information including the name, tenure of office/date of registration and category of school manager. As for serving managers of SMC/MC, the EDB should seek their consent to similar disclosure through an ad hoc exercise; and (c) for schools with managers who refuse to give consent to the

No.	Recommendation
	proposed disclosure, the EDB to add a remark indicating the number and categories, if applicable, of managers who have not given such consent on the relevant part of the EDB's homepage.
9	<u>Paragraph 4.11</u> The Working Group recommends that: (a) all DSS schools be required to conduct self-assessment by completing the Checklist regularly; (b) while the EDB would collaborate with the Hong Kong DSS Schools Council in the development of the Checklist, individual DSS schools should be given flexibility in adapting or modifying the Checklist to suit their own needs given that their needs do vary; and (c) relevant training be provided to DSS schools to facilitate the effective use of the Checklist with a view to promoting over time the internalization of a self-evaluation culture in DSS schools.
10	<u>Paragraph 4.17</u> The Working Group recommends that all DSS schools be required to set up a governance review sub-committee (or any name the SMC/IMC sees fit) to assist the SMC/IMC in reviewing the system integrity of various management and financial control processes with regard to the requirements below: (a) A governance review sub-committee (or any other name the SMC/IMC sees fit) responsible for conducting regular system reviews of various key management and financial control systems and processes has to be set up by DSS schools by the 2013/14 school year; (b) Specifically, the governance review sub-committee should review school-based policies and processes in respect of the following aspects: (i) human resources management matters including staff

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	recruitment, promotion, remuneration, etc; (ii) financial management matters including school budgeting, financial reporting, procurement, investment, transfer of funds from the operating reserve to designated reserves, etc; (iii) operation of school fee remission/scholarship schemes; Other management functions can be assigned to the governance review sub-committee as individual SMC/IMC deems appropriate; (c) Having regard to the sub-committee's operational needs in terms of a viable quorum for a meeting and for the sake of continuity, the governance review sub-committee should have a minimum of three members, with one member preferably with experience and qualification in accounting/financial management and one member being a manager of the school. To avoid conflict of interests, parents of students studying in the school should not be invited as a member of the sub-committee. In addition, all the members should not be among the paid staff of the school; (d) In principle, the governance review sub-committee is required to complete a comprehensive review of the school-based policies and processes as set out in (b) (i), (ii) and (iii) and submit a comprehensive report to the SMC/IMC within a three-year cycle. Within the three-year cycle, the SMC/IMC should determine the focus of its annual review each year and the governance review sub-committee should then submit a focused review report to the SMC/IMC annually; and (e) While paid staff of a DSS school including the principal and senior teachers/heads of functional committees of the school should not serve as member(s) of the governance review sub-committee, they may, at the discretion of the governance review sub-committee, attend meetings or serve as resource persons to facilitate the internal review. Nevertheless, at the review sub-committee meeting(s) where the annual focused

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	report or the comprehensive report is to be finalized before submission to the SMC/IMC, attendance should be confined to official members of the governance review sub-committee only.
11	<u>Paragraph 4.19</u> The Working Group recommends making it a mandatory requirement for DSS schools to put up essential matters as set out below for discussion and approval at SMC/IMC meetings: (a) the human resource policies for senior teaching and administrative posts such as the recruitment, appointment, promotion and remuneration packages of senior teaching and administrative staff; (b) annual school budgets and financial report/audited account including acceptance of donations and fund raising activities; (c) large-scale capital works (including the SMC/IMC's determination of what constitutes "large-scale" works); (d) procurement of services or goods through tendering with significant financial implications (including the SMC/IMC's determination of the thresholds for different modes of procurement); (e) operation of the fee remission/scholarship scheme including an annual operational summary and criteria for the schemes; (f) fee revision proposals; (g) investment policy and update; (h) advisory letter(s) specifying for the attention of the SMC/IMC and/or any warning letter(s) (e.g. the management letter from EDB's School Audit Section); and (i) self-evaluation on schools' academic as well as non-academic performance under the School Development and Accountability Framework, including the endorsement of School Development Plan, Annual School Plan and School Report.
12	<u>Paragraph 4.21</u>

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	The Working Group recommends that: (a) the existing audit inspection of DSS schools should be replaced by a management and financial audit; (b) relevant training be provided for DSS schools before the commencement of the management and financial audit from the 2014/15 school year to allow DSS schools to acquire sufficient know-how and have ample time to prepare for the enhanced audit; and (c) a review be conducted upon the completion of the first round of the management and financial audit of DSS schools to determine whether the management and financial audit should become an on-going measure; and if so, how.
Strengthening the Financial Management of DSS Schools	
13	<u>Paragraph 5.13</u> To enable DSS schools to put in place longer-term development strategies, the Working Group recommends that the following measures in respect of the ceiling on accumulated operating reserve be adopted: (a) the ceiling on the operating reserve which may contain both government funds and non-government funds should be set at an amount equal to 100% of the annual total expenditure, i.e. 12 months' operating expenditure as reflected in the audited accounts of the same school year; (b) only the balance in the operating reserve should be used to assess whether the schools' operating reserve exceeds the ceiling, taking into account the fact that funds in the designated reserves have specific purposes; (c) schools with accumulated operating reserve exceeding the ceiling as reflected in the latest audited accounts should be given the following options to rectify the situation and they should be required to indicate the option they choose in their submission of the audited accounts: (i) schools may choose to submit a plan on how to reduce

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	school fees in the forthcoming school year so that the accumulated operating reserve will drop to below the ceiling taking into account their own long-term financial considerations; (ii) schools may choose to receive less DSS subsidy in the forthcoming school year - the amount exceeding the ceiling will be deducted from the DSS subsidy to be paid to the school in the next payment; (iii) schools may choose to return the surplus in excess of the ceiling to the Government in a specified timeframe; or (iv) schools may choose to transfer the surplus in excess of the ceiling to the fee remission/scholarship reserve subject to the following conditions being met: – there is no surplus in the fee remission/scholarship reserve as reflected in the latest audited accounts; – the utilization rates of the fee remission/scholarship provisions are 100% or more in the past three consecutive years; and – the amount that can be transferred to the fee remission/scholarship reserve is subject to EDB's approval.
14	Paragraphs 5.15 & 5.16 The Working Group recommends that DSS schools be allowed to grandfather the reserve including assets in excess of the reserve ceiling accumulated before the implementation of the recommendation concerning reserve ceiling. This notwithstanding, the grandfather arrangement is subject to the following conditions being complied with: (a) schools submit to the EDB plans with detailed accounts of their reserves including their types, proposed usage and, where necessary, timeframe for deployment endorsed at SMC/IMC meetings within a specified timeframe to be set by the EDB; and

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	(b) the plans are approved by the EDB. The Working Group also recommends that the EDB should take into account schools' grandfathered reserve when processing any applications from schools for tuition fee increase or for setting up a designated reserve for construction, maintenance and upgrading of above-standard facilities.
15	<u>Paragraph 5.23</u> The Working Group recommends that DSS schools with genuine needs for constructing, maintaining or upgrading above-standard facilities be allowed to set up a reserve for the purpose subject to the following conditions being met: (a) concrete plans with purposes, timeframe/cashflow and funds required have to be deliberated and approved by the SMC/IMC; (b) Parent-Teacher Associations have to be consulted about the plans (all parents have to be consulted if the reserve is used for new above-standard capital works); (c) the amount to be transferred to the reserve for above-standard facilities should be no more than 10% of the school fee incomes of each school year; (d) there is no need to consult the EDB beforehand if after the proposed transfer, there remains cash in the operating reserve equivalent in amount to at least six months' the school's expenses. Instead, such a transfer should be detailed in the audited accounts to be submitted to the EDB; (e) the EDB's *prior* approval should however be sought if the school intends to transfer more than 10% of the annual school fee income or if after the transfer, cashflow in the operating reserve account falls below six months' expenses of the school; and (f) the EDB should not give approval to the application should the cashflow in the operating reserve account fall below three

<table>
<tr><th>No.</th><th>Recommendation</th></tr>
<tr><td></td><td>months' expenses after the proposed transfer.</td></tr>
<tr><td>16</td><td><u>Paragraph 5.26</u>
The Working Group recommends that the following measures be adopted with a view to enhancing the regulation of investment activities that DSS schools may conduct and ensuring that the financial situation of DSS schools remains sound and healthy after the investment:

(a) under no circumstances should DSS schools be allowed to use the funds in the operating reserve or the fee remission/scholarship reserve for investment;

(b) DSS schools should seek their SMC/IMC's approval before making investment decisions and such approval and factors for consideration must be clearly documented;

(c) the only funds that may be used for investment are the long service payment reserve, donations with specific purposes and the reserve for construction, maintenance and upgrading of above-standard facilities;

(d) DSS schools should only be allowed to invest in (i) HK dollar bonds; and (ii) HK dollar certificates of deposits according to the prescribed criteria/conditions; and

<table>
<tr><th>Type of Investment</th><th>Investment Criteria/Conditions</th></tr>
<tr><td>HK dollar bonds or certificates of deposits (CD):
✧ short to medium term with a maturity period of one to five years</td><td>✧ The credit rating of the issuer must not be lower than the rating of A3 given by Moody's Investors Service Inc. or A- given by Standard & Poor's Corporation.

✧ The bank must be licensed under the Banking Ordinance, Cap. 155.</td></tr>
</table>

(e) DSS schools should be alerted to the liquidity constraints of the certificates of deposits and corporate bonds in the</td></tr>
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	secondary markets and be advised to make allowance for contingencies in projecting the use of their designated reserves.
17	Paragraph 5.28 The Working Group recommends that two requirements be added to existing requirements for the purchase of properties by DSS schools: (a) DSS schools should be required to keep at least an amount equivalent to six months' operating expenditure in cash after the purchase of properties; and (b) DSS schools should not be allowed to purchase properties through mortgages or any other borrowing arrangements.
18	Paragraph 5.31 To strike a balance between meeting the public expectation for increased transparency of the use of school funding and addressing the practicality at school end, the Working Group recommends that the following measures be implemented: (a) DSS schools are required to disclose annually their major expenditures (including staff remuneration; repair & maintenance; fee remission/scholarship; learning and teaching resources; and miscellaneous expenditures) in terms of percentages of their annual overall expenditures; (b) DSS schools are required to disclose annually the cumulative operating reserve in terms of equivalent months of operating expenditure as well; and (c) to ensure meaningful disclosure and comprehensibility of the data, a template for enhancing the transparency of school's financial management should be developed. To further ensure that the disclosure will be fit-for-purpose and not over-burdensome, EDB should develop the template in consultation with the Hong Kong DSS Schools Council.
Training for School Personnel of the DSS Schools	

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19	<u>Paragraph 6.4</u> To prepare DSS schools to take forward the new proposed improvement measures for enhancing the governance, management and administration of DSS schools and to tackle the non-compliance problems, the Working Group recommends that training programmes be provided for DSS schools and a steering committee be set up to oversee the design and implementation of the training programmes.
20	<u>Paragraph 6.14</u> The Working Group recommends that the existing practice of inviting school managers of DSS schools to the structured training programmes for school managers should continue. To cater for the special needs of managers of DSS schools, the Working Group has also recommended that an optional module on deployment of resources specifically for DSS school managers be added to the existing programmes.
Measures to Ensure Compliance of Requirements of the Direct Subsidy Scheme by Schools	
21	<u>Paragraph 7.5</u> The Working Group recommends that on top of the existing measures, the following new measures be put in place: (a) escalation of advisory letters to supervisors at the earliest opportunity – if a school, without any reasonable justification, fails to comply with a rule/guideline or rectify the malpractice within a given time-frame after the principal of the school is served with an advisory/warning letter, follow-up advisory/warning letters will be issued to the supervisor of the school, copied to the school principal; (b) escalation of warning letters to SMC/IMC members at the earliest opportunity – if a school, without any reasonable justification, fails to comply with a rule/guideline or rectify the malpractice within a given time-frame after a advisory/warning letter has been written to the supervisor of the school, follow-up advisory/warning letters will be sent to the supervisor again but this time, the letter will be copied to

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	all the SMC/IMC members of the school as well; (c) disclosure of the non-compliance or malpractice – after exhaustion of the steps in paragraphs (a) and (b) above and if the malpractice remains to be rectified, the regional Principal Education Officers of the EDB may put up the case for discussion by the Task Force on DSS. With the Task Force's endorsement, the EDB will post the non-compliance (including a description of the malpractice) with the school concerned named on the EDB's website; and (d) suspension of DSS subsidy – if a school fails to comply with an important requirement or rectify serious malpractice after exhaustion of the steps mentioned in paragraphs (a) and (b) above, the Task Force on DSS may decide to take the measure in paragraph (c) prior to, or in addition to, withholding part of the DSS subsidy of the school until rectification is made. In order to ensure that the interests of students are not unduly affected, the EDB will assess the financial situation of the school before withholding the school's DSS subsidy.
Status of Li Po Chun United World College of Hong Kong in the Direct Subsidy Scheme	
22	Paragraph 8.14 Having reviewed the justifications put forward by the then ED and EMB for allowing Li Po Chun United World College of Hong Kong (LPCUWC) to remain in the DSS in 1999 and 2002, and taken into account the uniqueness of LPCUWC, the benefits it brings to students in Hong Kong and the downside of changing the funding mode of LPCUWC, the Working Group recommends the continuation of the status quo, i.e. that LPCUWC be allowed to continue to remain in the DSS.