

**For discussion on
13 November 2017**

Legislative Council Panel on Welfare Services

**Looking into the Governance Issues of Social Welfare Organisations
in light of the Neighbourhood Advice-Action Council Incident**

Purpose

This paper sets out the information relating to the staff retrenchment incident (the Incident) of the Neighbourhood Advice-Action Council (NAAC) in September 2017 and the governance of social welfare organisations for Members' reference.

Background

Causes of the Incident

2. Based on the information provided by the NAAC, it had a Lump Sum Grant (LSG) reserve of more than \$114 million as at the end of March 2015 and was of the view that with the then financial position, it could introduce some enhanced staff remuneration measures and additional service projects, a summary of which is set out below -

- (a) The NAAC reviewed the remuneration of the entire staff and implemented enhanced measures from 2014-2015 onwards, including continuing to disburse special allowances, enhancing insurance plans, improving the salary scale, and increasing Mandatory Provident Fund contribution, etc.;
- (b) The NAAC launched 21 short-term service projects¹, mostly for a term of two years, during the period between June 2016 and April 2017, with a view to enhancing services and trying out new service approaches. Some of the projects were also meant to strengthen staff training and some were service studies of an exploratory nature (such as the impact of mobile phones / electronic products on family relationship), etc.;

¹ The 21 projects have been implemented in 10 subvented service units and were scheduled to run for a period ranging from one to three years. Most of the projects were set for two years and scheduled to operate until mid-2018 (with individual projects to end by June 2019). A total of 63 staff members were hired.

(c) The NAAC hired additional manpower for different units² beginning from the second half of 2016 for a term of two years to provide support to the existing staff; and

(d) Increased subsidies for staff to further their studies.

3. With the implementation of the above measures, the LSG reserve of the NAAC fell from some \$104 million as at 31 March 2016 to some \$72 million as at 31 March 2017. In a review of its financial position in July and August 2017, the NAAC came to realise that the overall expenditure had been growing faster than expected. If no remedial measure was taken, the NAAC anticipated that -

(a) the LSG reserve would plummet to some \$24 million on 31 March 2018;

(b) the LSG reserve would be exhausted in August 2018; and

(c) a deficit of about \$14 million would be recorded on 31 March 2019.

4. The NAAC revealed that its management³, without seeking the views of its Executive Committee, decided in late August 2017 to prematurely terminate all the 21 short-term projects mentioned above and the employment contracts of the additional temporary staff it had hired. The arrangement, expected to be completed in late December 2017, was announced by the management to the staff concerned from early September 2017 onwards. The Executive Committee of the NAAC, which was informed of the decision by the management only on 7 September, formally resolved in a meeting on 11 September to prematurely terminate the short-term projects and the employment contracts of the additional temporary staff it had hired.

5. The Executive Committee of the NAAC resolved in a meeting on 13 September 2017 to form an Ad Hoc Committee with a view to conducting an in-depth and thorough investigation into the Incident, identifying the crux of the problem and responsibilities involved, and providing recommendations for improvement. The Ad Hoc Committee comprises 11 members, two of whom are independent members from the legal and accounting professions. It has completed an investigation report and convened general staff meetings on 31 October and 6 November to explain the Incident and details of the report. Meanwhile, the Ad Hoc Committee held a press conference on 31 October to elucidate to the media the key points of the report, which was uploaded onto the NAAC's homepage on the same day for public access at the following website -

² The Headquarters and 20 subvented service units are involved, with a total of 54 staff members hired.

³ It comprises the Executive Director, the Deputy Executive Director and the Financial Controller.

Impact of the Incident on Staff and Follow-up Actions

6. After the Incident, the Social Welfare Department (SWD) has been urging the NAAC to handle it properly and made repeated requests that the NAAC should conduct a thorough examination of its financial position and explore the feasibility of extending the employment of all or some of the affected staff until the end of the original contract periods. At the same time, it should review the resources available within the NAAC or job vacancies arising from natural wastage to accommodate the affected staff, so as to reduce the number of affected staff. Nevertheless, the Executive Committee and the Ad Hoc Committee of the NAAC are of the view that the financial position of the NAAC is unsatisfactory, and it is necessary to reduce expenditure as soon as possible, and hence the contracts of the affected staff cannot be maintained, though it is possible to accommodate some of the affected staff by the NAAC's internal job vacancies.

7. According to the information provided by the NAAC, 117 staff members have been involved in the Incident and the present position is as follows -

- (a) 41 of them are not affected, including those on loan, having worked until normal contract maturity, or already left the NAAC before the Incident;
- (b) 23 have been accommodated by the NAAC's internal job vacancies;
- (c) 11 resigned after the Incident for new job positions or further studies; and
- (d) 42 are still in need of work arrangement.

8. Since the early stage of the Incident, the NAAC has set up a support group to coordinate internal job vacancies, support the management by writing to other organisations in the sector for assistance, and liaise with other welfare organisations to look for job opportunities for the affected staff. According to the NAAC, the support group is still assisting the 42 affected staff members in need of work arrangement to look for jobs. As at the end of October 2017, about 40 welfare organisations have offered some 160 comparable job vacancies for the affected staff to apply for under the established procedures of individual organisations. Meanwhile, the NAAC expressed that they would continue to try to accommodate more affected staff by internal job vacancies. As recommended by the Ad Hoc Committee of the NAAC,

the Executive Committee of the NAAC has started to put in all efforts in assisting the work of the support group so as to lessen the impact on the staff concerned.

Impact of the Incident on Services and Service Users

9. As reported by the NAAC, regular services governed by the Funding and Service Agreements (FSAs) are not affected by the Incident. The NAAC expressed that it had been making effort in handing over the services upon termination of the short-term projects and in continuing the provision of services on a need basis, with a view to minimising the impact on service users. Measures include extending the projects as far as practicable, adjusting the scale or schedule of the projects, and arranging the permanent staff of regular services to follow up on the projects. The management of the NAAC has planned to visit the relevant service units later to explain to service users the Incident and relevant arrangements to extend the services.

10. Although, according to the NAAC, regular services governed by the FSAs are not affected by the Incident, some services under the short-term projects will be scaled down, or their individual needy users will be followed up by existing staff. The SWD has requested the NAAC to set up communication channels with the service users for them to express their opinions on service arrangements. The SWD has also drawn the NAAC's attention to the fact that the workload of permanent staff might increase correspondingly, and suggested the NAAC to strengthen its supervisory support and discuss relevant work arrangements with its staff. The SWD will continue to keep in view the service level of the NAAC and monitor its subvented services through the Service Performance Monitoring System, so as to ensure that the requirements under the FSAs are met.

Issues Revealed by the Incident

11. Based on the findings in the report of the Ad Hoc Committee set up by the NAAC, the following issues about the NAAC have been identified from the Incident -

- (a) It failed to make comprehensive and accurate forecasts in financial planning, and commenced new service projects and hired temporary staff in the absence of comprehensive financial forecasts;
- (b) The management lacked the awareness and capacity in risk management;
- (c) It failed to examine its financial expenditure carefully or have it closely monitored upon the implementation of measures;

- (d) It lacked internal supervision. The management and the Executive Committee failed to communicate effectively on the important decision to terminate service projects and contracts of temporary staff prematurely. It was inappropriate for the management to notify the Executive Committee of the NAAC only after the decision was made and executed;
- (e) It underestimated the impact of the decision on staff and service users; and
- (f) An effective management and control mechanism among the Executive Committee, subcommittees and the management are lacking, which calls for improvement.

Observations and Recommendations of the Ad Hoc Committee set up by the NAAC

12. The Ad Hoc Committee set up by the NAAC is of the view that the acute financial situation should be handled seriously and future expenditure should be closely monitored to ensure financial integrity. To summarise the findings, the Ad Hoc Committee recommended that improvement measures should be adopted in the following four aspects -

- (a) **Governance:** The management structure and functions of the senior personnel of the NAAC should be revamped with an enhanced capacity for supervision and risk management; the Executive Committee and other subcommittees of the NAAC should play a proper role in management and supervision;
- (b) **Financial management:** The NAAC should appoint personnel with appropriate professional qualifications and experience to manage its finances; review its financial management structure and its monitoring and control processes; refine the monitoring processes for budgeting and management; raise the awareness of the management personnel in financial management; and adopt suitable measures to restore a robust LSG reserve;
- (c) **Manpower planning and staff communication:** The authority and responsibilities for different levels of the management should be specified; the management should step up communication with subordinate management teams; the staff should be consulted extensively; and

- (d) **Service planning:** The SWD should be consulted before introducing any FSA-related services; service continuity should be considered.

Follow-up Actions by the SWD

13. Upon learning the Incident on 7 September 2017, the SWD took immediate actions to enquire with the NAAC, and held urgent meetings with its Executive Committee and its management on 8 and 13 September to listen to the NAAC's report and explanation on the details and causes of the Incident, solutions and service arrangements, etc. The NAAC was also urged to convene a general staff meeting as soon as possible for providing their staff with clear explanations, and submit a detailed Incident Report and other relevant information. The SWD also met with the Executive Committee and the management of the NAAC on 24 and 30 October to learn about the progress, findings and recommendations of the Ad Hoc Committee set up by the NAAC. In response to the requests of the affected staff, service users and union representatives, the SWD also held a meeting with them on 25 October to listen to their views and demands.

14. The SWD has referred complaints arising from the Incident to the Lump Sum Grant Independent Complaints Handling Committee (ICHC) for investigation and the complaints investigation is in progress.

15. According to the information provided by the NAAC, the NAAC has room for improvement in aspects such as decision-making of the management, financial management, human resources arrangement, communication with staff and service users and crisis management, etc. The SWD will assess carefully what responsibilities the NAAC has in the Incident, after examining the report submitted by the NAAC and the findings of the ICHC. If the NAAC is found not complying with the requirements, the SWD will consider submitting the case to the Lump Sum Grant Steering Committee (LSGSC) for discussion, and penalties including warning letters or ban on bidding for new subvented services for a certain period of time, etc. may be imposed on the NAAC.

16. Meanwhile, the SWD has required the NAAC to carry out follow-up actions as follows -

- (a) to implement the recommendations in the report of the Ad Hoc Committee and submit quarterly reports;
- (b) to update its financial projections (including estimates for the next two years) in order to ensure that it is in a reasonable financial position to provide various subvented services;

- (c) to evaluate the support rendered to the affected staff and the impact of taking over the services from the termination of the short-term projects and the employment of temporary staff, and submit quarterly reports;
- (d) as required in the LSG Manual, the NAAC must consult the SWD as to what constitutes “FSA-related” activities before rolling out new service projects in the future; and
- (e) as stipulated in the Best Practice Manual, regarding the use of the LSG reserve, the NAAC’s governing board/management committee is required to discuss in their meeting(s), at least once a year, how to manage and utilise the reserve, and to consider during the discussion how to maximise the use of the reserve for the NAACs’ development. The discussion has to be put on record. The NAAC is required to have documents setting out the policies and procedures on managing and monitoring their LSG reserve, and to make known to staff such procedures. The NAAC is required to, through appropriate channels, disseminate information about the utilisation of the LSG reserve in the past year to the public. Such information should include briefly a plan on how the reserve will be used in the future. The NAAC has to submit documents and records to prove that these requirements are being complied with.

17. In a related discussion in the 43rd Meeting of the LSGSC in October 2017, it was stated that all NGOs should examine and strengthen their measures relating to corporate governance, internal control and staff communication, make sound financial projections, adopt good risk and crisis management practices and inform the SWD early of any drastic change to their financial positions or large-scale retrenchment⁴. NGOs were also suggested to step up financial management training and consider engaging consultants to conduct actuarial studies, with a view to ensuring that NGOs maintain a robust financial position. The SWD will take into account the recommendations when the review on the enhancement of the LSG Subvention System is carried out.

⁴ According to paragraphs 3.20 of the LSG Manual, if the NGOs anticipate financial difficulty, their Board should have thorough deliberation and inform SWD in advance.

The SWD's Support for NGOs Receiving LSG Subvention

18. Since the implementation of the LSG Subvention System in 2001, the SWD has been reviewing the system and introducing enhancement measures from time to time with a view to assisting NGOs to further enhance corporate governance. Regarding the provision of additional resources, the Government has provided on various occasions an additional one-off funding of over \$4.3 billion and an additional recurrent funding of over \$800 million (please refer to **Annex** for details) including -

- (a) the provision of a one-off funding of \$200 million in 2008-09 for NGOs to implement various measures to enhance human resources and financial management;
- (b) the provision of an additional recurrent funding of \$200 million in 2008-09 to enhance NGOs' administrative capacity;
- (c) the provision of \$1 billion starting from 2010-11 for the establishment of the Social Welfare Development Fund to subsidise NGOs' staff training, system upgrade and service studies; and
- (d) the provision of an additional recurrent funding of around \$470 million in 2014-15 to enhance central administrative and supervisory support, etc.

19. With regard to training, the Government has commissioned universities, consultants and social service agencies to conduct a number of training programmes and studies for enhancing the corporate governance of NGOs, with the publication of relevant articles. These include -

- (a) various seminars and workshops from 2001 to 2007 for directors and senior management of NGOs;
- (b) a commissioned survey conducted by a university in 2001 on NGOs' boards of directors for collection of their information and analysis of the training needs of the directors;
- (c) a best management practice handbook and reference guidelines for NGOs' boards of directors compiled from 2001 to 2003;
- (d) the Envisioning Programme on the Best Practice Manual (BPM) held from 2015 to 2016 for the senior management and the boards of directors of NGOs. It comprised a symposium and

workshops, providing opportunities to share experience and good practices. Relevant keynote speeches and learning points have been compiled as a special supplement and uploaded onto the SWD website;

- (e) the Director of Social Welfare invited the directors (or representatives) of all the 165 NGOs receiving LSG subvention to participate in a total of 8 meetings from June to October 2016 to exchange ideas on the proper use of the LSG, enhancement of corporate governance, financial and human resources management, etc., with a view to enhancing the management capacity of NGOs and encouraging them to implement best practices; and
- (f) the allocation of over \$9.7 million from the Lotteries Fund to the Hong Kong Council of Social Service in early 2016 to implement the NGO Governance Platform Project for a period of four years. Through collaboration with different professional sectors such as the Hong Kong Institute of Certified Public Accountants, the Project aims at providing more training opportunities for the boards of directors/executive committees of NGOs, building a more robust network and database, facilitating research studies and further enhancing the overall corporate governance of NGOs, etc.

20. In addition, the Government provides the following reference materials and practice guidelines for enhancement of corporate governance of NGOs -

- (a) the information about good corporate governance issued by the Independent Commission Against Corruption and the Efficiency Unit as included in the LSG Manual; and
- (b) the BPM jointly produced by the SWD and the welfare sector in 2014 covering the areas of human resources management, financial management, corporate governance and accountability of NGOs, aiming to provide a common framework for the welfare sector to step up management of LSG matters and encourage NGOs to enhance transparency and disclose information to stakeholders, etc.

Continuous Enhancement of the LSG Subvention System

21. The Government reviews the implementation of the LSG Subvention System and introduces suitable measures from time to time to assist NGOs in maintaining good corporate governance. However, as mentioned above, the Incident showed from the outset that there is room for improvement for the NGOs' management in aspects such as decision-making, financial management, human resources arrangement, communication with staff and service users and crisis management, etc. For continuous enhancement of the LSG Subvention System, it is announced in the Policy Agenda of the Chief Executive's 2017 Policy Address that the Government will discuss with the social welfare sector how to optimise the LSG Subvention System. To this end, the Secretary for Labour and Welfare has assigned the SWD to set up a Task Force with members comprising representatives from the Labour and Welfare Bureau, the SWD, NGOs' management, staff, service users and individual members of the public. The SWD has started discussion with the welfare sector and the review is expected to be completed within two years after the scope of review is established.

**Labour and Welfare Bureau
Social Welfare Department
November 2017**

**Lump Sum Grant Subvention System
Additional Funding**

Additional recurrent funding			
Year	Item	Amount	Remarks
2008-09	Enhancing NGOs' administrative capacity	\$200 million	
2011-12 2013-14 2015-16 2017-18	Additional recurrent funding for the subvented welfare service units affected by the implementation of the statutory minimum wage	\$63 million	A total of four additional funding allocations.
2012-13	The adjustment of allocation to Other Charges (OC) at a rate of +4.5%, with reference to the composite consumer price index (CCPI) for the year	\$69 million	The \$69 million only accounted for the upward adjustment by 4.5% in 2012-13. The subsequent annual additional funding required was excluded.
2014-15	Strengthening central administrative and supervisory support, making additional allocation to OC and assisting NGOs to recruit and retain paramedical staff more effectively or to hire paramedical services	\$470 million	In addition, all new service units were provided with additional recurrent funding for supervisory support and paramedical support.
2017-18	Additional allocation to OC for the provision of air-conditioning in all subsidised residential care service units	\$42 million	
Total:		\$844 million	The additional recurrent funding required for the enhancement of individual services was excluded.
One-off funding			
Year	Item	Amount	
2001-02	Business Improvement Project (BIP) Scheme	\$105 million	
2001-02	Five-year Tide-over Grant (TOG)	\$1,473 million	
2006-07	Special One-off Grant (SOG)	\$912 million	

2008-09	One-off subsidy for NGOs to implement various measures for enhancing human resources and financial management	\$200 million
2009-10	One-off block grant from the Lotteries Fund	\$80 million
2009-10	Additional resources for NGOs in need of hire of paramedical staff or related services	\$277 million
2009-10	Funding for small NGOs	\$24 million
2012-13 to 2013-14	More additional resources for NGOs in need of hire of paramedical staff or related services	\$229 million
2010-11 to 2018-19	Social Welfare Development Fund (SWDF)	\$1,000 million
Total:		\$4,300 million