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TO

Joint Secretariat-Civil Service Pay Policy & System.
Attention Task Force.
Room 701 7th. Floor
Tower Two
Lippo Centre, 89 Queensway H.K.

Dear Sirs,

Public Consultation

I attach two copies of my Response to the above public consultation.

In general terms, I believe, that the average member of the community would have difficulty making a cogent response, due to the focus on "systems" and insufficient information on salaries and benefits for comparison purposes.

"Pay systems" overseas have emerged from the implementation of Programmes of Reform of their civil service. They are an end product, and not a starting point.

To be realistic, therefore, it has been necessary to include some basic research information into the Response, and identify some fundamental issues facing the community in terms of modernising the government bureaucracy.

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Civil Service Pay and Policy Response to Public Consultation

Executive Summary

General Observations

1. In the early colonial era an artificially high platform of pay and perks was created in Hong Kong's civil service to attract expats politically loyal to Britain. In the 1970's political correctness demanded that this artificially high platform be also applied "across the board" to local staff. No other colony or protectorate applied this policy for its own citizens after cessation of colony status, and Hong Kong is now paying an excessive price for its history, aggravated by other events, including the use of an unreliable formula for salary reviews. . . . see annex 1.
2. Massive growth in numbers of civil servants together with the artificially high platform of "pay and perks" have created an unsustainable financial burden on the community, not to mention deep resentments within the community. The "hidden" costs of future pensions to retired civil servants will create a financial time-bomb for future generations of tax payers. see annex 2.
3. Public awareness was alerted in mid-2001 when government officials advocated new forms of taxation, at a time when civil servants were awarded a salary increase (upto 5%) and when the private sector was suffering job losses and pay cuts. The resultant

public outcry brought to the surface deep resentments on the excessive salaries and perks of the civil servants; and lack of accountability.

4. Hong Kong now has a massive costly bureaucracy. In the period 1990 to 2000, sample departmental analysis suggests numbers of staff have increased in a range of 22% to 163%, and salaries were increased by 100% "across the board". see annex 3.
5. By comparison, the 1990's was a decade when overseas governments, acting under political and financial mandates, achieved substantial reduction in the size and cost of their civil service (for example UK and Canada each downsized 40% over a 10 years period). also annex 3
6. By comparison with civil servants in overseas government, Hong Kong's civil service, (especially at directorate grades, and higher master pay scale) enjoy excessive salaries and perks. Government officials are unwilling to admit this. More transparency on the amounts of salaries and benefits should have been provided in the public consultation documents. see annex 4.

Hong Kong's Bureaucracy

Hong Kong is in a time warp. Its cumbersome procedure-driven bureaucracy was established when Britain administered many colonies. Since then, overseas governments, including Britain, have modernized, using Programmes of Reform to downsize, outsource, and impose strict financial controls and business management principles. Market testing and regular efficiency programs are the norm. The majority of Hong Kong civil servants (other than the very top) have no awareness of the serious effects of the economic downturn nor any sense of urgency for bringing about a change of culture and pro-active administration.

In terms of "Size and Numbers" it is necessary to revert to the most fundamental principle of government - namely - that the purpose of employing government staff is to achieve an "end product" is a specific public service essential to, and for the benefit, of the community with the requirement that the cost of any particular public service should be visibly accountable including staffing and overhead costs.

Hong Kong has lost sight of this fundamental principle.

The existing internal processes for employing, retaining, promoting, pensioning and managing government staff with intricate "rights of seniority" and inter-department transfers at administrative and executive grades is now so complex and time-consuming, that they have taken on a life-form of their own; de facto, they have become an "end product" instead of a component in the production line of an "end product".

More time appears to be spent on internal staff affairs than on services to the public.

This is evidenced by the size and cost of the Civil Service Bureau which is responsible for staff policies, staff management and related issues. The Bureau itself has some 300 staff, predominantly administrative and executive grades, and including more than 20 directorate level posts. In the period 1990 to 2000, the Bureau expanded 37%. In the year 2001 it cost \$210,000,000 to run (not including the Civil Service Training Institute which employs another 90 staff). The Bureau does not provide an identifiable public service direct to the community. It simply handles internal staffing issues and yet in year 2000, it was 3x' bigger than the Planning and Lands Bureau, 5 times bigger than the Transport Bureau and 1.5 times bigger than the Works Bureau.

This type of centralized and costly bureaucracy has been phased out of modern government.

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Over the past decade, there has been little or no attempt to control the expansion of the civil service, in spite of world-wide trends towards downsizing. The Civil Service Bureau should accept at least some of the responsibility for this squandering of public finance.

Similarly, it is not unreasonable to suggest that the Standing Commission on Civil Service Salaries has paid too little attention to its obligation to safeguard the wider financial and economic interest of the community. The Commission has misguidedly placed its faith in a bureaucratic formula which uses tenuous criteria, which has received intense public criticism in its failure to make adequate adjustments for longer working hours, lack of job security and other disadvantages of private sector employment. In doing so, especially in periods of economic downturn, the Commission has allowed an upward salaries spiral to occur, placing an additional financial burden on the public purse. The work of the Commission should be more transparent to the public, who after all pay the salaries of the Commission. . . . see annex 1

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Footnote.

It is particularly noticeable that the lower paid "frontline" staff who face the general public on a daily basis are wonderful in their jobs and responsive to the public (post offices, libraries, district offices etc). It is the "ivory tower" inhabitants that most frequently cause frustration to the community and it is at this middle management and higher management levels that a Program of Reform should be focused. (Disciplined Services are not included in this response paper).

ARTIFICIALLY HIGH PLATFORM.

~~2~~ UPWARD SPIRAL.

- i) From the outset as a colony, British expats with political loyalty to Britain formed the basis of the civil service. They were paid high salaries and provided with housing passages, children's overseas education, medical and travel, and a generous (non-contributory) pension. This created an artificially high platform of pay and perks for expats. Local recruits were paid according to the local market.
- ii) By the 1970's, with the professional and administrative skills available locally, political correctness demanded that local staff be paid the same as expats. Substantial upgrading of pay and perks followed "across the board", so that the whole of the civil service was upgraded to this artificially high platform of pay and perks; this inevitably increases the costs of public services to the community.
- iii) Subsequently, (1990) government decided to get rid of its housing obligation to civil servants by offering a cash allowance for home-purchase. The intention was to reduce the enormous public cost of housing staff. Nevertheless, the cash allowances are now an added perk of \$15,000 to \$30,000 (guesstimate) in cash paid monthly for a period of 10 years (50% of this is accountable to be paid against a mortgage). By this means, staff were persuaded to move out a government quarter, but benefited from the additional monthly cash allowance.
- iv) The artificially high platform of pay and perks has, for many years, been used as a guideline by statutory bodies, university administrative and corporations such as MRTD, KCB many of which have actually recruited staff directly from the civil service; the escalation of costs has therefore spread to other sectors of the community.
- v) Inevitably private sector companies have to compete by offering a competitive pay package particularly for their key posts at managerial levels, thus further perpetuating the "artificially platform" scenario though not necessarily for lower grade staff.
- vi) The upward spiral has been perpetuated by a bureaucratic mechanism known as the "pay trend survey" and the application of pre-determined criteria. Even in economic downturns, civil service salaries have never followed private sector salaries down over a period of 30 years.

UPWARD SPIRAL —

Pay Trend Survey and Salary Review

The Standing Commission on Civil Service Salaries and Conditions of Service is appointed by the Chief Executive. The salaries are paid out of public funds and it costs the community some \$12 million per year.

The Commission is required to advise the Chief Executive on a range of matters relating to "pay and perks" including

1. c) whether ^{overall} ~~oversee~~ reviews of pay scales should continue to be based on the "pay trend survey".
1. d) the methodology for such survey.

Under Clause (3) the Commission shall give due weight to any wider community interests, including financial and economic considerations".

It is perfectly legitimate, therefore, at the time of a salary review, for the Commission to consider that in the wider community financial interests, a pay cut is desirable during an economic downturn, notwithstanding that the technical results of the pay trend survey may suggest otherwise (the pay review formula is a tenuous mechanism at best).

Not only would this be a legitimate decision for the Commission to make, the Terms of Reference suggest that this "balancing rational" is mandatory under Clause (3).

Any experienced professional - in any discipline - knows that a formula, methodology or mechanism which relies on the application of variables and ~~alterables~~ variables is capable of producing extensive variations and different conclusions.

The reports of the Commission have never been available for public scrutiny, but over a period of 20 to 30 years, there has never been a pay cut for civil servants in spite of several serious economic downturns. There is every indication, therefore, that the Commission paid for out of community funds, has not fairly represented the wider interests of the community and has adopted too narrow an application of its powers. Announcements by senior government officials (Chief Secretary and Secretary of Civil Service) have openly stated that the pay trend survey alone must be the basis for salary adjustment and that "economic downturns a budget deficits are not a reason for government pay cuts". These statements are clearly contrary to the terms of reference of the Commission and raise considerable doubts on the alleged independence of the Commission (which is unlikely to "rock the boat" when faced with such dictates).

More transparency is surely required on the work of the Commission.

Upward spiral.

In times of economic downturn private sector pay cuts and job losses occur. If at such time the Commission allows government salaries to remain static, or decides to award an increase, an immediate salary gap is created or widened. Later, with economic recovery, the private sector salaries try to catch up. These increases are then used to justify further government increases. An upward spiral is created following each economic downturn. It is a win-win situation for civil servants. Government give assurance that their salaries "follow" in reality, they never followed the private sector down. They only follow the private sector up. And historically government has always driven salaries upwards first by retaining the artificial platform of pay and perks, and thereafter by subsequent events. No other colony, territory or protectorate has used the artificial platform (expat) perks as an arrest the board employment basis for its citizens after cessation of colony status.

FUTURE TIME-BOMB from pensions.

Future generations of taxpayers will face a financial time-bomb, and higher tax structures.

The pension of a civil servant is based on 60% of his highest annual salary after 30 years service (53% for recruits after 1997) so that an employee could retire at age 55 years and have a life expectancy of say a further 25 years. Thus just one D4 directorate grade staff (Administrative Officer B and equivalent level) could receive a pension of \$90,000 per month, which would cost the community \$1,080,000 per year after retirement for 25 years (say \$27 million). There are 1,400(?) directorate grade staff. The total pensionable staff on other grades is not known, but the majority are career civil servants. The future financial commitments are enormous, and are a burden in perpetuity, unless pensionable terms are phased out of the government system.

An approximate indication of the community's escalating financial commitments on pensions paid to existing retired personnel is shown in Table B. These figures may substantially increase when existing staff on updated salaries begin to retire.

The financial future of Hong Kong ^{is} at risk. Contrary to upbeat comments made by Senior government officials from time to time, it is very doubtful whether Hong Kong will ever reach its former glory-days.

A Programme of Reform to cut down the size and cost of the bureaucracy is necessary.

In overseas countries, a pension equivalent to HK\$20,000 p.m. would be considered generous, and overseas governments have already downsized and drastically reduced the number of career civil servants.

Table B below illustrates the escalating financial commitment from pensions.

Table B
Escalating annual pension costs

<u>Year</u>	<u>HK\$</u>	<u>Year</u>	<u>HK\$</u>
1990	1,944,000,000	1996	7,466,000,000
1991	2,544,000,000	1997	8,703,000,000
1992	3,393,000,000	1998	9,250,000,000
1993	4,413,000,000	1999	7,362,000,000
1994	5,612,000,000	2000	8,226,000,000
1995	6,240,000,000	2001	9,381,000,000

Other "hidden" costs arising from staff benefits include various home purchase and housing allowances, paid passages and education etc estimated to cost the community \$1.5 billion p.a.

The continually increasing salary levels also have serious long term effects since the resultant pensions are calculated on the highest annual salary.

The Public Consultation document (Part III - Q5) raises the question of government affordability but only in the limited context of "pay adjustments" and "pay systems".

In reality, however, there are two staffing factors which impose a huge cost burden on the community - namely "numbers of civil servants" & "pay and perks of civil servants".

On the subject of numbers of civil servants, it is quite alarming that, at the time when overseas governments were concentrating on downsizing, Hong Kong has allowed massive increases in the size of its civil service. Table A below illustrates the expansion pattern during the period 1990 to 2000, based on sample departmental statistics - a range of 22% to 163% increase.

Table A

Sample Department	No. of staff 1990	No. of staff 2001	Increase (Nos) Increase (%) Period 1990-2001
Customs & Excise	375	560	185 (49%)
Buildings Dept(*)	190	500	310 (163%)
Lands Dept(*)	830	1,500	650 (76%)
Education Dept	1,560	1,437	305 (27%)
Planning Dept	240	454	214 (89%)
Government Property Agency	80 (1994)	110	30 (37.5%) (1994 to 2001)
Civil Service Bureau(**)	170	270	100 (59%)
Civil Service Training School(**)	40	54	14 (35%)

(*) originally one department

By comparison, overseas governments have downsized considerably - UK and Canada by 40% over 10 years, Singapore 10% in 5 years, with Australia and New Zealand also initiating major reductions in the size of their civil service.

Such downsizing achievements were the result of politically imposed Programme of Reform driven by a variety of circumstances which can be summarized as:-

- 1) the need to control budgets and reduce the cost of public services by downsizing, outsourcing and market testing and

- (i) the need to replace poor performance, and "procedure-driven" bureaucracies with a public service based on clearly defined goals and pro-active performance targets especially at senior management levels.

Overseas reform programmes have included 4 outstanding features in order to rectify such situations:-

- 1) Identification of "non-core" government services for outsourcing - this establishes a medium term/long term target of reduction based on work function.
- 2) Outsourcing, market testing and competitive tendering - when a department or agency wishes to retain the right to provide a particular public service, the department must competitively tender and include in its bid all staffing and overhead costs necessary to provide the particular public service. Market testing is considered essential.
- 3) Incorporation of business management principles into the culture of the civil service - this established accountability for costing and implementation at all levels and particularly at senior grades. Regular efficiency programmes are required, reviewing the specific public service provided and the cost thereof.
- 4) An immediate short-term mandate to reduce a specified percentage of head-count within a specified period - this short term target imposed a sense of urgency, acts as a focal point for cultural change, and brings to a halt the habit of "breeding bureaucracy and expansion"

Incorporating such modern principles of good government into a Programme of Reform is essential if the "Ivory tower" culture - is to be modernized.

The Public Consultation document draws attention to the analytical study by PwC Consultants, and summarizes in table form the various "pay policies, structures and systems" used in Australia, Canada, New Zealand, Singapore and U.K. However, with the exception of Canada, there is no information provided on comparable civil service salaries between Hong Kong and the referred countries.

The Canadian experience is helpful; it shows that there has to be a political will to outsource, downsize and impose strict financial and budget constraints as part of a programme of reform; following which, changes in pay policies and pay structures will gradually emerge even in the most difficult circumstances (Canada had to endure a 7-year pay freeze for its civil service during the early 1990's).

The Canadian average for civil servants base pay is C\$45,000 per year (equating to HK\$18,750 per month). In U.K. a 2001 survey of professional salaries showed that experienced professional surveyors in the British Government earned the equivalent of HK\$29,000 per month with a contributory pension scheme. In the Australian government, they earn the equivalent of HK\$25,000 per month.

By comparison, the Hong Kong civil servants are millionaires. A senior surveyor and other senior professionals earn HK\$85,000 per month plus other expensive perks. "Chief level" professionals earn \$100,000 per month and "Government level" professionals earn HK\$122,000 p.m. in line with Administrative Officer Grade B. Administrative and Executive officers are generally in line with professional staff; do not have to contribute to the pension scheme (unlike MPFA). In the period 1990 to 2000 civil service salaries were increased by 100% "across the board". The 1990-2000 pay scales are shown in Table 2.

Table 2 - Directorate Grades

	1 April 1990 (HK\$)	1 st April 2000 (HK\$)	% Increase 1990-2000	5% 2001
D10	108,400	215,550	99.86%	227,450
D9	102,500	204,800	99.80%	215,000
D8	90,700	181,050	99.61%	190,100
D7	87,950	175,600	99.66%	184,350
D6	81,450	162,650	99.69%	170,750
D5	77,150	154,150	99.80%	161,850
D4	72,650-74,850	145,150-149,600	94.87%	152,400 upwards
D3	63,950-67,900	127,900-135,550	99.63%	134,300 upwards
D2	55,100-58,500	116,650-123,850	111.71%	122,450 upwards
D1	46,400-49,250	98,250-104,250	111.67%	103,150 upwards

Extract from Master Pay Scale (49 grades in total)

Sample Grade	1 April 1990 (HK\$)	1 st April 2000 (HK\$)	% Increase 1990-2000	2001
49	44,505	88,115	97.99%	92,510 (4.98%)
42	34,495	68,310	98.03%	
35	25,350	50,190	97.98%	
28	18,400	36,940	100.76%	
21	13,350	26,805	100.78%	
14	9,450	19,055	101.23%	
8	6,670	13,425	101.27%	
1	4,285	8,125	89.61%	8,320 (2.4%)

Such massive increases in salary together with the substantial increases in numbers of civil servants impose a huge financial burden on the taxpayer, and in answer to Q5 of the consultancy, it is more than obvious that "affordability" must be a dominant factor in establishing the size of the civil service, and the salary structure of the civil service.

Hong Kong has lost sight of this fundamental principle. The size of the bureaucracy has expanded out of control. Historically, there has been weakness and lack of political will when dealing with staff problems such as outsourcing. Civil servants are not able to make financial or commercial staffing decision which may "upset" other civil servants or their unions.