

CHAPTER 8

THE GOVERNMENT OF THE HONG KONG SPECIAL ADMINISTRATIVE REGION

GENERAL REVENUE ACCOUNT

GOVERNMENT DEPARTMENT

University Grants Committee Secretariat

**University Grants Committee funded institutions —
Governance, strategic planning and
financial and performance reporting**

**Audit Commission
Hong Kong
31 March 2003**

UNIVERSITY GRANTS COMMITTEE FUNDED INSTITUTIONS — GOVERNANCE, STRATEGIC PLANNING AND FINANCIAL AND PERFORMANCE REPORTING

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UNIVERSITY GRANTS COMMITTEE FUNDED INSTITUTIONS — GOVERNANCE, STRATEGIC PLANNING AND FINANCIAL AND PERFORMANCE REPORTING

Summary and key findings

Introduction

A. The University Grants Committee (UGC) is a non-statutory advisory committee responsible for advising the Government on the development and funding needs of tertiary institutions in Hong Kong. The UGC is supported by a secretariat which is headed by its Secretary-General. The Secretary-General is the Controlling Officer who accounts for the expenditure of the UGC, including grants made to the higher-education institutions. In 2002-03, the approved budget for tertiary education amounted to \$13.5 billion, which represented 28% of the total government expenditure on education and 5% of the total government expenditure. There are eight higher-education institutions which receive government grants through the UGC, namely City University of Hong Kong (CityU), Hong Kong Baptist University (HKBU), Lingnan University (LU), The Chinese University of Hong Kong (CUHK), The Hong Kong Institute of Education, The Hong Kong Polytechnic University (PolyU), The Hong Kong University of Science and Technology (HKUST) and The University of Hong Kong (HKU) (paras. 1.2 to 1.5).

Audit review

B. Audit has recently conducted a value for money audit on the UGC-funded institutions. The audit covered three major areas, namely: (a) the governance, strategic planning and financial and performance reporting; (b) the general administrative services; and (c) the staff remuneration packages and stipends. This report deals with the governance, strategic planning and financial and performance reporting of the UGC-funded institutions. The objective of this audit review is to examine the adequacy of the governance and planning mechanism, and financial and performance reporting of the institutions in the provision of various higher-education services with a view to identifying areas for improvement (paras. 1.9 to 1.13).

C. Audit has identified some areas where improvements need to be made in the corporate governance of the institutions, which are described in paragraphs D to L below. In addition, there is room for improvement in the institutions' strategic planning as indicated in paragraphs M to O below, and their financial and performance reporting as shown in paragraphs P to X below.

Corporate governance of institutions

D. *Governance structure.* The governance structures of the eight institutions are largely similar, which, in general, include a council, a court and a senate. A council is normally the

governing body and the supreme decision-making body of the institution. A court plays an advisory role and does not take part in the day-to-day oversight of the institution's affairs. A senate is responsible to the council for directing and regulating the academic matters of the institution. Section 8A of the City University of Hong Kong Ordinance specifies that there is to be a Court as the advisory body of CityU. However, up to the time of completion of the audit in December 2002, CityU had not set up a Court as its advisory body. Section 7 of the University of Hong Kong Ordinance specifies that the Court shall be the supreme governing body, whereas the Council is specified as the executive body. However, the Court largely functions as an advisory body under the Statute of the Ordinance. In contrast, the Council has much wider powers for the administration and management of the affairs of the HKU under the Statute. In February 2003, a Review Panel on Governance and Management of the HKU recommended that the Council should be regarded as the *de facto* supreme governing body. The purpose of the Court should be cast as representing the wider interests of the communities served by the HKU (paras. 2.4 to 2.18).

E. ***Size and composition of governing bodies.*** As at 1 December 2002, the Council of the CUHK had 56 members and the Council of the HKU had 45 members (HKU could appoint up to 54 members under the relevant legislation). The size of the two Councils is relatively larger than that of the other six institutions. Moreover, according to the international trend, the optimum size of an institution's council is much smaller (paras. 2.24 to 2.26).

F. The CUHK, under Statute 11 of The Chinese University of Hong Kong Ordinance, has appointed seven life members to the Council (or over 10% of the 56 council members appointed). However, six of these life members did not attend the nine Council meetings held between July 2000 and November 2002. The CUHK needs to review whether it is desirable to appoint life members to the Council in future because they may not be able to sustain their input in the long term due to factors such as health and time constraints (paras. 2.27 to 2.29).

G. The Court of the HKU largely functions in an advisory capacity. However, the Court, being the supreme governing body, also carries the ultimate responsibility for all the affairs of the institution. As at 1 December 2002, the Court had 252 members (including 45 Council members and 173 Senate members who were ex-officio members of the Court under Statute XV of the University of Hong Kong Ordinance). The size of the Court of the HKU is six times that of similar bodies in the other institutions. With such a large membership, it is not conducive to making prompt decisions to meet the needs and demands of a fast changing and increasingly sophisticated society. There appears to be a need for the HKU to reduce the size of its Court to make it function more efficiently and productively (para. 2.30).

H. ***Low attendance rates of external members at Council meetings.*** The eight institutions each has a Council as its governing body. An audit analysis of the average attendance rates of external members of the Councils of the eight institutions for the three financial years 2000-01, 2001-02 and 2002-03 (July to November 2002) revealed that the overall attendance rates of external members ranged from 50% to 80%. The attendance rates in some institutions were low. In the case of the

CUHK, on average, 50% of the external members did not turn up at the Council meetings. In the case of the HKU, the average attendance rate of the external members was 58% (paras. 2.43 to 2.48).

I. A good practice of corporate governance for institutions is that their councils should consist of a majority number of independent external members, who are capable of exercising independent judgement on important issues. However, due to the absence of some external members, the external members might not constitute a majority when important decisions were taken at the Council meetings. In particular, Audit notes that in the case of the CUHK and the HKU, the external members did not constitute a majority at most of the Council meetings held in 2000-01, 2001-02 and 2002-03 (July to November 2002). There was over-reliance on the internal members when important decisions were taken (paras. 2.51 to 2.58).

J. ***Low attendance rates of external members at Court meetings.*** Four institutions have set up a Court as its advisory body as laid down in the relevant ordinances. An audit analysis of the average attendance rates of external members of the Courts of the four institutions in the three financial years 2000-01, 2001-02 and 2002-03 (July to November 2002) revealed that the average attendance rates of the HKU and the HKUST were low. A significant number of external members were absent at the Court meetings. In the case of the HKU, the average absence rates of the external members were 66% in 2000-01 and 73% in 2001-02. In the HKUST, the average absence rates of the external members were 64% in 2000-01, 69% in 2001-02, and 61% in 2002-03 (July to November 2002) (paras. 2.59 to 2.61).

K. ***Audit Committee.*** As the institutions are entrusted with large sums of public money, they have a duty to achieve a high standard of corporate governance, which includes the establishment of an audit committee. However, CityU, the HKBU, the CUHK, the PolyU and the HKU have not set up an audit committee (paras. 2.69 to 2.75).

L. ***Governance structure review.*** In November 2002, the Government accepted the recommendation of the UGC that the councils of the eight institutions should review the governance structures to ensure “fitness for purpose”. At the time of completion of the audit in December 2002, the institutions had taken action to review their governance structures. Audit considers that the governing bodies of the institutions need to conduct periodic reviews of their effectiveness, which will assist the governing bodies in achieving their objectives and finding the best way to oversee and direct the institutions (paras. 2.82 to 2.85).

Strategic planning of institutions

M. ***Preparation of strategic plans.*** In general, the objectives of the institutions are to provide for studies, training, research and development in different subjects of learning and assist in the economic and social development of Hong Kong. In order to achieve these objectives in an efficient and effective manner, it is necessary for the institutions to conduct strategic planning exercises periodically. Audit noted that, of the eight UGC-funded institutions, six had prepared a strategic plan setting out the strategic objectives, operational goals and strategic actions for achieving the goals.

The HKUST and the HKU were taking action to prepare/finalise their strategic plans (paras. 3.5, 3.8 and 3.9).

N. ***Preparation of operational plans.*** In order to ensure that the departmental and faculty plans and activities of an institution would lead to the achievement of the institution's visions and missions, the institution needs to develop an annual institutional operational plan, which would help implement the strategies stated in the institution's strategic plan. Audit's research of the practices of the largest university in each of the five advanced countries showed that these selected universities generally prepared annual operational plans to set out targets for achievement, which were derived from the goals stated in the strategic plans. However, Audit noted that the eight UGC-funded institutions did not produce annual institutional operational plans to provide a link to the institutions' strategic plans (paras. 3.10, 3.11 and 3.13).

O. ***Preparation of progress reports.*** Audit's research of the overseas universities' practices revealed that, in their annual reports, the selected overseas universities reported their progress of achievement in respect of the targets set out in their annual operational plans. However, Audit noted that the UGC-funded institutions did not adopt a practice of setting targets and reporting progress of achievement in respect of each target (paras. 3.12 to 3.14).

Financial reporting of institutions

P. ***Statement of recommended practice.*** In 1996, the UGC-funded institutions developed and implemented a Statement of Recommended Practice (SORP) for the preparation of financial statements of the institutions. However, the Hong Kong Society of Accountants (HKSA) could not give a formal endorsement to the SORP, because the SORP did not fully comply with the accounting standards of the HKSA. Furthermore, it is stated in the SORP that a detailed review of the practical application of the SORP would be undertaken three years from the first year of implementation, i.e. a review was to be carried out in 1999. However, Audit noted that, up to February 2003, the institutions had not completed the review (paras. 4.6, 4.7 and 4.47).

Q. ***Accounting treatment of recognition of expenses.*** The accounting standards of the HKSA state that the recognition of expenses in the accounts of an organisation should take place at the time of an outflow or depletion of assets. However, Audit noted that the UGC-funded institutions generally adopted a practice of recognising expenses at the time of placing orders instead of receipt of goods or services, which was at variance with the generally accepted accounting practices (para. 4.15).

R. ***Accounting treatment of property, plant and equipment.*** The accounting standards of the HKSA state that the depreciable amount of an item of property, plant and equipment should be allocated on a systematic basis over its estimated useful life. However, Audit noted that the UGC-funded institutions generally wrote off their capital expenditures instead of capitalising them as assets and amortising their value over their useful life by means of depreciation. This practice was at variance with the generally accepted accounting practices (para. 4.16).

S. ***Accounting treatment of recognition of assets.*** The accounting standards of the HKSA state that an asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise. However, Audit noted that the UGC-funded institutions generally wrote off their expenditure on library books and periodicals in the year of expenditure instead of capitalising them as assets. The annual expenditure of each of the institutions on library books and periodicals ranged from \$6 million to \$75 million. This accounting treatment was at variance with the generally accepted accounting practices (paras. 4.17 to 4.19).

T. ***Accounting treatment and presentation of consolidated financial statements.*** The accounting standards of the HKSA state that a parent entity that has one or more subsidiaries should present consolidated financial statements, in which intra-group balances and transactions and resulting unrealised profits should be eliminated in full. However, Audit noted that the UGC-funded institutions did not prepare consolidated financial statements. This practice was at variance with the practices adopted by universities in advanced countries. Audit also noted that, of the eight UGC-funded institutions, seven institutions each had one to 13 subsidiaries (paras. 4.20 to 4.25).

U. ***Accounting treatment of related-party transactions.*** The accounting standards of the HKSA state that if there have been transactions between related parties, the reporting enterprise should disclose the nature of the related-party relationships as well as the types of transactions and the elements of the transactions necessary for an understanding of the financial statements. However, Audit noted that the UGC-funded institutions did not make adequate disclosure of the transactions with their subsidiaries. This practice was at variance with the practices adopted by universities in advanced countries. The transactions which were not disclosed in the institutions' financial statements included amounts due from the institutions' subsidiaries, which ranged from \$700,000 to \$6.5 million (paras. 4.29 to 4.33).

V. ***Basis of presentation of financial statements.*** Audit's research of the practices of the largest university in each of the five advanced countries indicated that these selected universities stated that their financial statements had been prepared in accordance with the generally accepted accounting practices of their countries. However, Audit noted that the UGC-funded institutions stated that their financial statements had been prepared in accordance with the accounting policies generally adopted by higher-education institutions in Hong Kong (paras. 4.37 to 4.41).

Performance reporting of institutions

W. ***Disclosure of performance information.*** Audit noted that the UGC and the UGC-funded institutions did not disclose to the public some significant performance information which was collected every year. The information included student retention rates, admission qualifications of programmes, language examination results of newly admitted students, student admission ratios, student unit costs, etc. Furthermore, Audit's research on overseas universities' practices revealed that the overseas universities generally disclosed to the public much more performance information than that disclosed by the UGC-funded institutions (paras. 5.4 to 5.20).

X. *Satisfaction surveys.* From time to time, the eight UGC-funded institutions conducted opinion surveys of their stakeholders on the effectiveness of their services. The institutions conducted the surveys either by themselves or by engaging independent firms. In order to enable meaningful comparisons of the stakeholders' levels of satisfaction on different aspects of the delivery of tertiary education among the eight institutions, it would be desirable for the eight institutions to collaborate to jointly engage an independent firm to conduct the surveys (paras. 5.21 to 5.23).

Audit recommendations

Y. Audit has made the following major recommendations to the Secretary-General, University Grants Committee that he should:

Corporate governance of institutions

- (a) request CityU to urgently examine whether a Court should be set up as its advisory body. If CityU considers that there is no need to have a Court, it should amend the City University of Hong Kong Ordinance which stipulates the setting up of a Court (para. 2.19(a) and (b));
- (b) request the HKU to clarify the role of its Court, in view of the fact that it is specified as the supreme governing body in the University of Hong Kong Ordinance but functions largely in an advisory capacity (para. 2.19(c));
- (c) request the HKU to review the relevant legislation to ensure that the statutory role of its Court reflects its actual functions (para. 2.19(d));
- (d) request the CUHK, in reviewing its governance structure, to consider reducing the size of its Council and Senate. If the size of the Council is to be reduced, it should critically examine the appropriateness of appointing new life members to the smaller-size Council in future (para. 2.36(a));
- (e) request the HKU, in reviewing its governance structure, to consider reducing the size of its Council, Court and Senate (para. 2.36(b)(i));
- (f) advise the eight institutions (particularly CUHK and HKU) to ascertain, where necessary, the reasons for the low attendance rates of external members of their Councils at the Council meetings, and to take appropriate action to improve the attendance rate of external members of the Councils at the Council meetings (para. 2.62(a) and (b));

- (g) advise the HKU and the HKUST to ascertain the reasons for the low attendance rates of external members of the Courts at the Court meetings, and to take appropriate action to improve the attendance rates of the external members of the Courts (para. 2.62(c));
- (h) recommend to the Government and the institutions that, as a matter of principle, they should not re-appoint those Council/Court members whose attendance at Council/Court meetings is low (para. 2.62(d));
- (i) request CityU, the HKBU, the CUHK, the PolyU and the HKU to set up an audit committee so as to strengthen the internal audit function and the corporate governance structure (para. 2.76);
- (j) request the eight institutions to conduct periodic (say every five years) reviews of the effectiveness of their governing bodies (para. 2.86(b));

Strategic planning of institutions

- (k) request the HKUST and the HKU to expedite action to finalise their strategic plans to set out their strategic objectives, operational goals and strategic actions for achieving the goals (para. 3.22(a));
- (l) request the eight institutions to:
 - (i) develop annual institutional operational plans to set out clear targets for achievement (para. 3.22(c)(i));
 - (ii) prepare annual progress reports to present the progress of achievement in respect of the targets set out in their annual operational plans (para. 3.22(c)(ii));
 - (iii) upload their progress reports onto their websites for the information of the public (para. 3.22(c)(iii)); and
 - (iv) enhance their role in the provision of community services by setting relevant targets for achievement in their annual operational plans (para. 3.22(c)(iv));

Financial reporting of institutions

- (m) collaborate with the eight institutions and the HKSA to develop a set of revised SORP for compiling the institutions' financial statements. The SORP should comply with the accounting standards of the HKSA (para. 4.48(b));
- (n) request the eight institutions to strictly comply with the revised SORP in preparing their financial statements (para. 4.48(c));

Performance reporting of institutions

- (o) based on good overseas practices, discuss and work out with the eight institutions a revised set of clear and quantifiable performance indicators for assessing and reporting the performance of the institutions (para. 5.24(a));
- (p) based on the agreed performance indicators, request the eight institutions to provide the UGC with their annual performance data (para. 5.24(b));
- (q) publish the performance data provided by the eight institutions in the UGC's annual reports (para. 5.24(c));
- (r) collaborate with the eight institutions with a view to jointly engaging an independent firm to conduct common satisfaction surveys of the stakeholders of the institutions (para. 5.24(e));
and
- (s) disclose the results of the common satisfaction surveys in the UGC's annual reports and website (para. 5.24(f)).

Response from the Administration and the UGC-funded institutions

Z. The Administration and the UGC-funded institutions have generally accepted the audit recommendations.

PART 1: INTRODUCTION

1.1 This PART describes the background and the objectives of the audit report.

Background

1.2 Tertiary education is an important part of the education system. In 2002-03, the approved budget for tertiary education amounted to \$13.5 billion, which represented 28% of the total government expenditure on education and 5% of the total government expenditure.

University Grants Committee

1.3 The University Grants Committee (UGC) is a non-statutory advisory committee responsible for advising the Government on the development and funding needs of tertiary institutions in Hong Kong. It has neither statutory nor executive powers. The UGC is appointed by the Chief Executive of the Hong Kong Special Administrative Region. It comprises a Chairman and 21 members. The membership of the UGC and its subordinating committees includes academics from local and overseas tertiary institutions. The UGC is supported by a secretariat which is headed by the Secretary-General, UGC. The Secretary-General is the Controlling Officer who accounts for the expenditure of the UGC, including grants made to the higher-education institutions.

1.4 The main functions of the UGC are to:

- (a) advise the Government on the development and funding of higher education in Hong Kong;
- (b) administer government grants made to the UGC-funded higher-education institutions;
- (c) maintain and improve the quality of teaching, learning and research in the UGC-funded institutions; and
- (d) monitor the efficiency and effectiveness of the institutions' activities.

UGC-funded institutions

1.5 There are eight higher-education institutions which receive government grants through the UGC. They are, in alphabetical order:

- (a) City University of Hong Kong (CityU);
- (b) Hong Kong Baptist University (HKBU);
- (c) Lingnan University (LU);
- (d) The Chinese University of Hong Kong (CUHK);
- (e) The Hong Kong Institute of Education (HKIEd);
- (f) The Hong Kong Polytechnic University (PolyU);
- (g) The Hong Kong University of Science and Technology (HKUST); and
- (h) The University of Hong Kong (HKU).

1.6 In the 2000-01 academic year (normally from September to August), the eight institutions together enrolled 59,408 full-time students and 22,064 part-time students (Note 1). They are hereinafter referred to as the institutions.

1.7 Each of the eight institutions is an autonomous body which was established under its own ordinance with its own governing council. The institutions have substantial freedom in the control of their curricula and academic standards, selection of staff and students, and internal allocation of resources. The institutions are diverse in character and in their different contributions to the educational, cultural and economic development of Hong Kong. As stated in the UGC's report "*Facts and Figures 2001*", the eight institutions can be categorised according to their characteristics as follows:

- (a) ***CUHK, HKUST and HKU:*** concentrating on first and higher degree work, and emphasising scholarship and research;

Note 1: *The 59,408 full-time students included 10,284 sub-degree students, 44,241 undergraduate students, 1,593 taught postgraduate students and 3,290 research postgraduate students. The 22,064 part-time students included 8,365 sub-degree students, 3,365 undergraduate students, 9,662 taught postgraduate students, and 672 research postgraduate students.*

- (b) *CityU and PolyU*: offering a range of programmes including sub-degree, undergraduate and postgraduate courses, with a strong emphasis on professional and vocational education;
- (c) *HKBU and LU*: aiming at providing a broad general education rather than a specialised professional training; and
- (d) *HKIEd*: offering a wide range of courses for the teaching profession.

UGC Higher Education Review

1.8 In May 2001, the Secretary for Education and Manpower commissioned the UGC to launch a comprehensive review of higher education. The review was led by Lord Sutherland, who was a senior member of the UGC and Principal and Vice-Chancellor of the University of Edinburgh of the UK. The review covered all aspects of higher education provision, including the governance of universities. In March 2002, the UGC published the review report entitled “*Higher Education in Hong Kong*” (the Sutherland Report). Following public consultation on the Sutherland Report, the UGC submitted its final recommendations to the Secretary for Education and Manpower in September 2002. The Government accepted most of the UGC’s final recommendations and announced in November 2002 a blueprint for the further development of higher education in Hong Kong.

Audit review of UGC-funded institutions

1.9 Against the above background, Audit has recently conducted a value for money audit on the institutions. Since this is a broad subject, the scope of this audit review is divided into three topics. The audit findings are contained in three separate reports, as follows:

- (a) University Grants Committee funded institutions — Governance, strategic planning and financial and performance reporting (the subject matter of this report);
- (b) University Grants Committee funded institutions — General administrative services (Chapter 9 of Director of Audit’s Report No. 40); and
- (c) University Grants Committee funded institutions — Staff remuneration packages and stipends (Chapter 10 of Director of Audit’s Report No. 40).

Audit review of UGC-funded institutions: Governance, strategic planning and financial and performance reporting

1.10 Because the activities of the institutions are mainly supported by public funds, the Government and the community at large have a legitimate expectation that the services of the institutions have been provided in an efficient and effective manner and, in particular, that there is a proper system of governance of the institutions and reporting of the resources used and the outcome of using the resources.

1.11 In this report, the audit findings are covered in the following PARTs:

- (a) the corporate governance of the institutions (PART 2);
- (b) the strategic planning of the institutions (PART 3);
- (c) the financial reporting of the institutions (PART 4); and
- (d) the performance reporting of the institutions (PART 5).

1.12 The objective of the audit review is to examine the adequacy of the governance and strategic planning, and financial and performance reporting of the institutions in the provision of various higher-education services. Audit has found that there are areas where improvements can be made. Audit has made a number of recommendations to address the issues.

1.13 In carrying out the audit review, Audit examined the records and interviewed the staff of the eight institutions and the UGC Secretariat. Audit would like to acknowledge with gratitude the full cooperation of the staff of the eight institutions and the UGC Secretariat.

General response from the HKU

1.14 The **Vice-Chancellor, The University of Hong Kong** has compiled an overarching statement on the whole audit review exercise (comprising three separate audit reports — see para. 1.9 above). The purpose of this statement is to provide all stakeholders (including the Public Accounts Committee of the Legislative Council and the public at large) with pertinent background information on the academic, moral and social values of higher education, so that they can interpret the audit reports in the proper context. The HKU's overarching statement is attached at Appendix A.

PART 2: CORPORATE GOVERNANCE OF INSTITUTIONS

2.1 This PART examines corporate governance issues of the eight institutions with a view to identifying areas for improvement.

Background

2.2 A good corporate governance of a public organisation helps:

- (a) assure that the organisation uses its resources efficiently;
- (b) ensure that the organisation takes into account the interests of a wide range of constituencies and of the community; and
- (c) ensure that its governing bodies are accountable to the stakeholders.

This, in turn, helps maintain the confidence of the stakeholders of the organisation and assure that the organisation operates for the benefit of the community. As the eight institutions are entrusted with large sums of public funds, they are expected to adopt a high standard of corporate governance.

2.3 The eight institutions are autonomous organisations which are responsible for the provision of teaching, pursuit of knowledge and conduct of research. These institutions have different visions and missions and distinctive ethos.

Governance structures of institutions

2.4 Each of the eight institutions was established by its own ordinance which, among other things, sets out its governance structure. Their governance structures are largely similar and are summarised in Table 1 below.

Table 1

**Governance structure of the eight institutions
as laid down in the ordinances**

| Institution | Legislation | Executive/ governing body | Advisory body | Academic supervisory body |
|--------------------|--|--|--------------------------|--|
| CityU | City University of Hong Kong Ordinance (Cap. 1132) | Council | Court | Senate |
| HKBU | Hong Kong Baptist University Ordinance (Cap. 1126) | Council | Court | Senate |
| LU | Lingnan University Ordinance (Cap. 1165) | Council | Court | Senate |
| CUHK | The Chinese University of Hong Kong Ordinance (Cap. 1109) | Council | — | Senate |
| HKIED | The Hong Kong Institute of Education Ordinance (Cap. 444) | Council | — | Academic Board |
| PolyU | The Hong Kong Polytechnic University Ordinance (Cap. 1075) | Council | (Note) | Senate |
| HKUST | The Hong Kong University of Science and Technology Ordinance (Cap. 1141) | Council | Court | Senate |
| HKU | University of Hong Kong Ordinance (Cap. 1053) | Court (governing body) Council (executive body) | | Senate |

Source: The Laws of Hong Kong

Note: While the relevant legislation does not specify the setting up of a court, the PolyU has set up a court as an advisory body to its Council.

2.5 It can be seen from Table 1 above that, in general, the governance structure of the eight institutions includes:

- (a) a Council;
- (b) a Court; and
- (c) a Senate.

2.6 **Council.** A council of an institution is normally its governing body and the supreme decision-making body of the institution. (In the case of the HKU, the relevant legislation stipulates that the Court is the governing body.) A council is responsible for the administration and the conduct of the affairs of an institution. A number of council committees (e.g. Finance Committee, Staffing Committee and Estates Committee) are set up to support the functions of a council. The Councils of the eight institutions have a majority of their members from outside of the institutions (i.e. the external members). The Chairmen of the Councils are external members, who are appointed by the Chief Executive of the Hong Kong Special Administrative Region. (Some Chairmen are appointed by the Chief Executive in his capacity as the Chancellor of the institutions concerned.) Other members include the Heads of Institutions and senior staff of the institutions, and representatives of staff and student bodies.

2.7 **Court.** Five of the eight institutions have set up a court. The courts do not take part in the day-to-day oversight of the institutions' affairs or in the decision-making processes. Instead, they play an advisory role (including the Court of the HKU although it is stipulated as the governing body under the relevant legislation). A court normally meets once a year to receive the annual report and annual financial statements of the institution. In most institutions, the majority of the members of the courts are external members who are community leaders and who have an interest in the work of the institutions. Other members include the Heads of Institutions, senior staff as well as the representatives of the staff and student bodies of the institutions.

2.8 **Senate.** A senate of an institution (called the Academic Board in the HKIEd) is responsible to the council for directing and regulating the academic matters of the institution, such as setting academic standards and awarding degrees. Members of a senate are drawn mainly from the academic staff and students of the institution.

Variations in governance structure

2.9 Table 1 (in para. 2.4) above shows that there are some variations in the governance structure among the institutions. Seven institutions have established a council as their supreme

decision-making body. However, the Council of the HKU is specified as the executive body in the University of Hong Kong Ordinance, whereas its Court is specified as its governing body.

2.10 Five institutions are required to set up a court under the relevant ordinances. While the Courts of CityU, the HKBU and the HKUST are specified as advisory bodies, the Court of the HKU is stated as the governing body. Although the role of the Court of the LU is not explicitly specified in the Lingnan University Ordinance, it functions largely as an advisory body.

2.11 Audit notes that many overseas universities, such as the post-1992 universities in the UK (they were mainly the former polytechnics which have acquired university designation since 1992), do not have a court as an advisory body in their governance structure.

Audit observations on governance structure

Court of CityU

2.12 Section 8A of the City University of Hong Kong Ordinance specifies that there is to be a Court as the advisory body of CityU. Section 8A also stipulates that the Court has the following functions:

- (a) to receive an annual report from the Head of Institution;
- (b) to consider reports made to it by the Council;
- (c) to discuss any motion on general policy of CityU;
- (d) to raise funds at the request of CityU to further CityU's objects; and
- (e) to promote the interests of CityU in Hong Kong and elsewhere.

2.13 **Although Section 8A of the City University of Hong Kong Ordinance was enacted in 1994, up to the time of completion of audit in December 2002, CityU had not set up a Court as its advisory body. This is at variance with the provision in the Ordinance, which specifies that there is to be a court.** In response to Audit enquiries, CityU has stated that CityU will review the need for setting up a court, as part of the review of the governance structure to ensure "fitness for purpose" as recommended by the Government in November 2002 (see paras. 2.82 and 2.83 below).

Court and Council of the HKU

2.14 The University of Hong Kong Ordinance provides a two-tier system for the governing and executive body of the HKU. Section 7 of the Ordinance specifies that the Court shall, subject to the provisions of the Ordinance and the statutes, be the supreme governing body of the institution, whereas the Council is specified as the executive body.

2.15 Although the Court of the HKU is specified as the governing body in Section 7 of the University of Hong Kong Ordinance, Audit notes that under Statute XVII of the Ordinance, it largely functions as an advisory body. Under the Statute, the functions of the Court are to:

- (a) recommend to the Chancellor additions to, or the amendment or repeal of, any of the statutes on the proposal of the Council;
- (b) consider the annual budget estimates and to make representations thereon to the Council;
- (c) consider the annual accounts together with comments that may have been made by the auditors;
- (d) consider any reports that may be made by the Council to the Court;
- (e) discuss any motion on general policy of the HKU that may be introduced by a member; and
- (f) appoint life members and to prescribe the procedure for making such appointments.

2.16 In contrast, the Council of the HKU has much wider powers under Statute XIX of the University of Hong Kong Ordinance. The Council has a long list (24 items) of specific powers for the administration and management of the affairs of the HKU. In addition, the Council has general powers to administer the affairs of the institution other than those vested in the Ordinance. The Council has general powers to set the vision and mission, goals and strategic planning for the future development of the institution. It also has the powers to monitor the progress and implementation of the goals and plans.

2.17 **Audit considers that there is a need to review whether it is necessary to have a two-tier system within the HKU's governing and executive structure. In particular, the HKU needs to consider whether the role of the Court should be formally changed to an advisory one similar to the arrangements of the other institutions in Hong Kong and some institutions in the UK.**

2.18 At the time of the audit in December 2002, the HKU had appointed an international review panel to review its governance structure (see paras. 2.82 and 2.83 below). In February 2003, the Review Panel on Governance and Management submitted a review report to the HKU. The Review Panel has recommended, inter alia, that:

- (a) the Council should be regarded as the *de facto* supreme governing body of the HKU. The Council should have a clear majority of external members. The ratio of external to internal members should be about two to one; and
- (b) the purpose of the Court should be cast as representing the wider interests of the communities served by the HKU, including its alumni. The Court should retain its power to make, repeal, and amend statutes of the HKU.

The Council of the HKU would consult the stakeholders on the recommendations of the Review Panel.

Audit recommendations on governance structure

2.19 **Audit has *recommended* that the Secretary-General, University Grants Committee should:**

- (a) **request CityU to urgently examine whether a Court should be set up as its advisory body in accordance with the City University of Hong Kong Ordinance (see para. 2.13 above);**
- (b) **if CityU considers that there is no need to have a Court, make a recommendation to the Government to amend the relevant legislation which stipulates that a Court for CityU should be set up (see para. 2.13 above);**
- (c) **request the HKU to clarify the role of its Court, in view of the fact that it is specified as the supreme governing body in the University of Hong Kong Ordinance but functions largely in an advisory capacity (see paras. 2.14 and 2.15 above); and**
- (d) **request the HKU to review the relevant legislation in order to ensure that the statutory role of its Court reflects its actual functions (see para. 2.17 above).**

Response from the Administration and the institutions

2.20 The **Secretary for Education and Manpower** has said that Audit's observations and recommendations on the governance structure are in line with the Government's decision following the UGC Higher Education Review 2002 (see para. 1.8 above). The Government accepted the UGC's recommendation that the universities should review their governance and management structures to ensure that they are appropriate for modern days, drawing on the principles and international good practices. He notes the institutions' comments and their follow-up plan.

2.21 The **Secretary-General, University Grants Committee** has said that the UGC welcomes the Audit's recommendations, which are generally in line with what has been put forth in the UGC Higher Education Review 2002. The UGC considers it paramount that each institution should have in place a governance structure which is "fit for purpose".

2.22 The **President, City University of Hong Kong** has said that:

- (a) the Chairman of the Court is the Chancellor of CityU (i.e. the Chief Executive of the Hong Kong Special Administrative Region). In view of the Chief Executive's schedule, it was not felt practical to establish the Court under his chairmanship; and
- (b) CityU has recently established a committee to review the governance and structure of CityU. The issue of whether there should be a Court and its structure will be considered as part of the review.

2.23 The **Vice-Chancellor, The University of Hong Kong** has said that:

- (a) the HKU responded positively to the recommendation of the Sutherland Report (see para. 1.8 above) by commissioning, in July 2002, an independent 'blue-ribbon' panel of external experts (comprising the former heads of the Harvard University and the University of New South Wales, and the Chief Justice of the Hong Kong Special Administrative Region) to undertake an overall review of the HKU's governance and management structures. The Panel recognised at the outset that a modern university, operating in a rapidly changing and fiercely competitive globalised environment, must adopt a model of governance that is fit for purpose;
- (b) the Panel's report was submitted to the HKU's governing Council in early-February 2003 and, after a period of intensive consultation, will be considered for adoption by the end of April 2003. Assuming that the report will be accepted by the HKU, the successful

implementation of the whole package of reform will have adequately addressed the observations and recommendations arising from the audit; and

- (c) the HKU's Review Panel has, amongst others, recommended that the purpose of the Court should be recast (see para. 2.18(b) above). The HKU agrees to the need for making necessary changes to its Ordinance and Statutes to clarify the roles of its Court as an advisory body.

Size and composition of governing bodies

2.24 A feature that characterises the governing bodies of some institutions in Hong Kong is that they have a large number of members. The number of members of the governing bodies of the eight institutions, as at 1 December 2002, is summarised in Table 2 below.

Table 2
Number of members of the Councils, Courts and Senates
of the eight institutions as at 1 December 2002

| Institution | Executive/ governing body (Council members) | Advisory body (Court members) | Academic supervisory body (Senate members) |
|-------------|---|----------------------------------|--|
| CityU | 31 | – | 97 |
| HKBU | 33 | 40 | 70 |
| LU | 30 | 37 | 38 |
| CUHK | 56 | – | 146 |
| HKIEd | 27 | – | 39 Academic Board |
| PolyU | 29 | – | 87 |
| HKUST | 28 | 44 | 53 |
| HKU | 45 | 252 (Note) | 173 |

Source: Institutions' records

Note: Although the Court of the HKU is specified as the governing body, it largely functions in an advisory capacity. According to Statute XV of the University of Hong Kong Ordinance, members of the Council and members of the Senate are ex-officio members of the Court.

Audit observations on the size and composition of governing bodies

Councils of the CUHK and the HKU

2.25 Table 2 shows that the Council of the CUHK had 56 members, and the Council of the HKU had 45 members (up to 54 members could be appointed under the relevant legislation). **The size of the two Councils is relatively larger than that of the other six institutions.** Audit appreciates that the Councils need to have a sufficient number of members to represent the various stakeholders, who have the knowledge to provide the necessary input. However, according to the international trend, the optimum size of an institution's council is much smaller.

2.26 According to Audit's research, in the UK, on average, a council of the pre-1992 universities (Note 2) has about 33 members. A council of the post-1992 universities (Note 3) has no more than 25 members as required by the 1992 Further and Higher Education Act. In Australia, the average size of the Councils of 39 universities and colleges is 21 members (e.g. the University of Melbourne and the Monash University have 21 members in their Councils). The Council of the University of California (called the Regents) has 26 members. The University of Auckland has 18 Council members and the National University of Singapore has 17 Council members.

2.27 Audit notes that, under Statute 11 of The Chinese University of Hong Kong Ordinance, the Council of the CUHK can appoint life members. Before September 2002, there were six life members. The Council held nine meetings in the financial years (Note 4) of 2000-01, 2001-02 and 2002-03 (July to November 2002). However, these six life members did not attend the nine Council meetings held between July 2000 and November 2002. On 11 September 2002, the Chairman of the Council was also appointed as a life member. These seven life members, before their appointment as life members, were long-serving external members of the Council and had made significant contributions towards the CUHK. Currently, over 10% (i.e. 7 out of 56) of the members of the Council are life members.

Note 2: *Pre-1992 universities in the UK are those universities which acquired the university status before 1992.*

Note 3: *Post-1992 universities in the UK refer to higher education institutions, mainly the former polytechnics, which have acquired the university status since 1992. The councils of these universities are called boards of governors.*

Note 4: *The institutions' financial year is from 1 July to 30 June. All financial years hereinafter refer to the institutions' financial year unless otherwise specified.*

2.28 Judging from the attendance records of the nine Council meetings, it is not clear what contributions the six life members have made towards the governance of the CUHK at the Council meetings in recent years. Continuous life appointment is not always desirable. International good practice suggests that the length of service of an external member in a council should not be more than eight to nine years. The CUHK needs to review whether it is desirable to appoint life members to the Council in future because they may not be able to sustain their input in the long term due to factors such as health and time constraints. Audit considers that it is important that life members provide input to council proceedings.

2.29 The CUHK has advised Audit that the CUHK is most grateful to the life members of the Council who are very long-serving Council members and have made significant contributions to the CUHK in many respects. The roles played and contributions made by these life members are still very important to the Council and the CUHK as a whole. Although they may not be present at the three to five Council meetings held each year due to old age, ill health or other reasons, many of them still offer to the Council and the CUHK their wise counsel. They also play an active and important part in helping the CUHK to launch major development programmes, secure the much-needed opportunities and relationship for enhancing the CUHK's position, reputation and programmes, and in fund-raising. Their contributions to the governance of the CUHK should not be doubted.

Court of the HKU

2.30 The Court of the HKU largely functions in an advisory capacity. However, the Court, being the supreme governing body, also carries the ultimate responsibility for all the affairs of the institution. The Court of the HKU had 252 members as at 1 December 2002. Under Statute XV of the University of Hong Kong Ordinance, the Court shall consist of, among others, members of the Council and members of the Senate (which had 45 and 173 members respectively). The size of the Court of the HKU is six times that of similar bodies in the other institutions (see Table 2 in para. 2.24 above). With such a large membership:

- (a) it is not conducive to making prompt decisions to meet the needs and demands of a fast changing and increasingly sophisticated society;
- (b) it is difficult for the Court to make effective use of the members' time; and
- (c) if a large number of members attend the meetings, they may not be able to make effective contributions on important matters.

There appears to be a need for the HKU to reduce the size of its Court so as to make it function more efficiently and productively.

2.31 Audit also noted that of the 252 members of the Court, 173 (or 69%) were Senate members who were mainly the academic staff of the HKU. External members constituted 23% of the total number of members (the other 8% of members were student/alumnus/convocation representatives). The percentage of external members was significantly below the percentages of the HKBU, the LU and the HKUST (see Table 7 in para. 2.59 below). Independent external members are in a better position to provide independent advice. There is a need for the HKU to review the composition of the membership of the Court by reducing the proportion of internal members.

2.32 As of December 2002, the HKU had appointed six life members to the Court under the University of Hong Kong Ordinance in recognition of their valuable contributions. The Court held meetings once a year in the past three financial years. The minutes of the Court meetings held in the three financial years of 1999-2000, 2000-01 and 2001-02 showed that all six life members had not attended any Court meetings held in that period. It is doubtful whether life members can contribute continuously at Court meetings throughout their lifetime. The HKU may wish to consider whether the practice of appointing life members is still appropriate.

2.33 The HKU has advised Audit that the main purpose of appointing life members to the Court is to maintain a link with these prominent members of the community. Life members can contribute in many different manners, and attending Court meetings is not the only contribution that life members are able to make.

Senates of the HKU and the CUHK

2.34 Audit notes that the Senate of the HKU had 173 members and the Senate of the CUHK had 146 members. **Their size was relatively large in comparison with that of the other six institutions.** It is noted that the Senates of the HKUST, the HKIEd and the LU had 53, 39 and 38 members respectively. The HKU and the CUHK need to review whether the size of their Senate should be reduced to make it function more effectively.

Reviews on governance structures of the institutions

2.35 In November 2002, the Government announced that it supported the UGC's recommendation that the eight institutions should review their governance structures to ensure "fitness for purpose". At the time of the audit in December 2002, the HKU and the CUHK had embarked on a review of their governance structures, and the other six institutions would also conduct a review of their governance structures.

Audit recommendations on the size and composition of governing bodies

2.36 **To enable the governing bodies of the institutions to function more effectively, Audit has recommended that the Secretary-General, University Grants Committee should request:**

- (a) **the CUHK, in reviewing its governance structure, to:**
 - (i) **consider reducing the size of its Council and Senate (see paras. 2.25 and 2.34 above); and**
 - (ii) **if the size of the Council is to be reduced, critically examine the appropriateness of appointing new life members to the smaller-size Council in future (see para. 2.28 above);**

- (b) **the HKU, in reviewing its governance structure, to consider:**
 - (i) **reducing the size of its Council, Court and Senate (see paras. 2.25, 2.30 and 2.34 above); and**
 - (ii) **modifying the composition of the Court (which will act as an advisory body), with a view to increasing the proportion of external members (see para. 2.31 above); and**

- (c) **CityU, the HKBU, the LU, the HKIEd, the PolyU and the HKUST to review the size and composition of their governing bodies and make necessary changes (see para. 2.35 above).**

Response from the Administration and the institutions

2.37 The **Secretary for Education and Manpower** has said that Audit's observations and recommendations on the governance structure are in line with the Government's decision following the UGC Higher Education Review 2002 (see para. 1.8 above). The Government accepted the UGC's recommendation that the universities should review their governance and management structures to ensure that they are appropriate for modern days, drawing on the principles and international good practices. He notes the institutions' comments that their governing/advisory bodies would review their governance structure, and he notes their follow-up plan.

2.38 The **Secretary-General, University Grants Committee** has said that:

- (a) the UGC welcomes the Audit's recommendations, which are generally in line with what has been put forth in the UGC Higher Education Review 2002. The UGC considers it paramount that each institution should have in place a governance structure which is "fit for purpose";

- (b) mindful of the fact that it is a matter best done by the institutions themselves, the UGC has requested the governing bodies of institutions to review their governance structures, drawing on principles set out in the UGC review report and the examples of international good practices listed there; and
- (c) the UGC is pleased to note that an independent review on the HKU's governance structure, commissioned by the HKU Council, has recently been completed, and that an Ad Hoc Task Group had been set up by the HKU to follow up the review recommendations. The UGC also notes that other institutions are either in the process of reviewing their governance structures or have put in hand preparatory work for such an exercise.

2.39 The **Vice-Chancellor, The Chinese University of Hong Kong** has said that Council has appointed a Task Force to review the governing structure of the CUHK. Audit's recommendations will be reviewed by the said Task Force and the Council.

2.40 The **Vice-Chancellor, The University of Hong Kong** has said that:

- (a) the HKU's Review Panel has made relevant recommendations that:
 - (i) the Council should be regarded as the supreme governing body;
 - (ii) the size of the Council should be reduced to the range of 18 to 24 members, with a clear majority of external members over internal members in the ratio of two to one, each acting as a trustee rather than representative of a constituency; and
 - (iii) membership of the Senate should be set in the range of 42 to 50, and its composition should include the HKU's senior academic officers and representatives from Faculties and students; and
- (b) regarding the Court, as it has been rightly pointed out by Audit, it is principally an advisory body. Its size should not create any difficulty (the HKU indeed wishes to have representatives from as many sectors as possible to provide it with advice) and proportional representation in this case is not as relevant as in other executive bodies. In any case, since the size and composition of the Court will, in part, reflect those of the Council and Senate, an adjustment is very likely, following the proposed new structure of the Council.

2.41 The **President, City University of Hong Kong** and the **President, The Hong Kong Institute of Education** have said that they have established a Review Committee/Task Force to review their governance structures. The **President, The Hong Kong Polytechnic University** has said that PolyU has been reviewing and modifying the size and composition of its governing bodies as a standard practice to maintain an effective governance structure appropriate to the prevailing situation.

2.42 The **President and Vice-Chancellor, Hong Kong Baptist University** has said that the HKBU Council has agreed to conduct the review later this year. The **President, Lingnan University** has said that he will forward to the Council that the size and composition of the governing bodies be reviewed and changes be made if necessary. The **President, The Hong Kong University of Science and Technology** has said that the review will be referred to the Council for consideration.

Attendance rates of external members at Council meetings

2.43 Contributions made by members of governing bodies are important, as the effective governance of any organisation is very much people-oriented. The contributions rely heavily on the knowledge, skills and commitment of members of governing bodies. Responsibilities of the governing bodies include providing strategic insights and effective monitoring of the performance of the management. For the governing body of an institution to effectively fulfil its responsibilities, it needs to have a majority of external members who are capable of giving independent advice and exercising independent judgement on important issues (e.g. setting strategic directions and appointment of the head of the institution). The contributions of external members are crucial. External members constitute a majority in the composition of the governing bodies of other public organisations in Hong Kong (such as the Vocational Training Council, the Hong Kong Airport Authority, the Hong Kong Housing Authority and the Kowloon-Canton Railway Corporation). The relevant ordinances for the eight institutions have provided that there should be a majority of external members (who are not the officers and employees of the institutions) in their Councils.

2.44 While various stakeholders are represented in the Council of the eight institutions, the numbers and proportion of internal members (ex-officio and elected/appointed staff representatives), student/alumnus/convocation representatives, and external members vary among the institutions. The methods of appointments are also different. The composition of the Councils of the eight institutions under the relevant ordinances is summarised in Table 3 below.

Table 3

**A summary of the composition of
the Councils of the eight institutions as laid down
in the relevant ordinances and the actual number of members (in brackets — Note 1)**

| | Total number of members (a) | Internal members | | Student/ alumnus/ convocation representatives (d) | External members (e) | Percentage of external members expressed as a percentage of total number of members $(f) = \frac{(e)}{(a)} \times 100\%$ |
|-------|--|-----------------------|---|---|--------------------------------|--|
| | | Ex-officio (b) | Staff (elected or appointed) (c) | | | |
| LU | 33 (30) | 2 (2) | 5 (5) | 1 (1) | 25 (22) | 76% |
| PolyU | 29 (29) | 2 (2) | 5 (5) | 2 (2) | 20 (20) | 69% |
| HKUST | 33 (28) | 8 (8) | 3 (2) | 1 (0) | 21 (18) | 64% |
| HKIEd | 28 (27) | 4 (4) | 6 (6) | 1 (1) | 17 (16) | 61% |
| CityU | 37 (31) | 11 (11) | 3 (2) | 2 (1) | 21 (17) | 57% |
| CUHK | 57 (Note 2) (56) | 16 (15) | 7 (7) | 3 (3) | 31 (Note 2) (31) | 54% |
| HKBU | 34 (33) | 11 (10) | 4 (4) | 1 (1) | 18 (18) | 53% |
| HKU | 54 (45) | 18 (17) | 2 (2) | 6 (4) | 28 (22) | 52% |

Source: The Laws of Hong Kong and institutions' records

Note 1: Numbers in brackets denote the actual number of members as at 1 December 2002.

Note 2: The Council of the CUHK can appoint life members under Statute 11 of The Chinese University of Hong Kong Ordinance. The maximum number of life members is not specified. As at 1 December 2002, there were seven life members who were external members.

2.45 Audit conducted an analysis of the average attendance rates of external members of the Councils of the eight institutions by examining the minutes of the Council meetings held in the three financial years of 2000-01, 2001-02 and 2002-03 (July to November 2002). The results of the analysis are summarised in Table 4 below.

Table 4
Average attendance rates of external members
of the Councils of the eight institutions for three years (Note 1)

| Institution | 2000-01 (July 2000 to June 2001) | 2001-02 (July 2001 to June 2002) | 2002-03 (July to November 2002) | Average attendance rate for three years (Note 3) |
|--------------------|---|---|--|---|
| PolyU | 76% | 82% | 85% | 80% |
| LU | 76% | 75% | 55% | 73% |
| CityU | 70% | 74% | 53% | 69% |
| HKUST | 68% | 65% | 67% | 67% |
| HKBU | 68% | 60% | No meeting held | 65% |
| HKIEd | 60% | 66% | 58% | 63% |
| HKU | 58% | 62% | 51% | 58% |
| CUHK (Note 2) | 46% | 53% | 50% | 50% |

Source: Institutions' records

Note 1: Unfilled vacancies of external members were excluded in the computation.

Note 2: Life members were included in the computation.

Note 3: Details of the average attendance rates of external members of the Councils of the eight institutions for the three years are shown in Appendix B.

Audit observations on attendance rates of external members of the Councils

2.46 Table 4 above shows that:

- (a) the overall attendance rates of external members of the Councils of the eight institutions for the three financial years ranged from 50% to 80%. The attendance rates in some institutions were low;
- (b) in the case of the CUHK, on average, 50% of the external members did not turn up at the Council meetings. In the case of the HKU, the average attendance rate of the external members was 58%; and
- (c) the attendance rates for the LU dropped from 75% in 2001-02 to 55% in 2002-03 (July to November 2002), and the attendance rates for CityU also dropped from 74% in 2001-02 to 53% in 2002-03 (July to November 2002).

2.47 Audit has observed that in some institutions, some external members did not attend any of the Council meetings held in 2000-01 or 2001-02. For example, in one institution, 12 external members did not attend any of the Council meetings held in 2000-01, and ten external members did not attend any of the Council meetings held in 2001-02. Please see details at Appendix C.

2.48 In order to gainfully make use of the knowledge and skills of external members for the benefit of the institutions, there is a need for the institutions to take measures (e.g. by preparing adequate guidelines for the external members to understand their role and responsibilities) to encourage external members to show their strong and sustained commitment by attending Council meetings for discussing and deciding on important matters.

2.49 The LU has advised Audit that the reason for the drop in attendance rate of external Council members was that the attendance rate reflected only one meeting held on 27 November 2002 during the period. In the second meeting held on 27 February 2003, the attendance rate of external members rose to 77%. As the attendance rate may fluctuate in the remaining Council meetings of the year, most probably the attendance rate of external members in 2002-03 would be more or less the same as the average attendance rates in 2000-01 and 2001-02.

2.50 CityU has advised Audit that at the time the audit report was compiled, there had been only one meeting of the Council, whereas there were three meetings in the previous years. The

attendance rates of external members stood at 70% for 2000-01 and 74% for 2001-02. In addition, some members were sick or had the urgent need to attend to their businesses.

External members did not constitute a majority at the Council meetings

2.51 A good practice of corporate governance for institutions is that their councils should consist of a majority number of **independent** external members, who are capable of exercising independent judgement on important issues (such as scrutinising policies on allocation of resources, and overseeing senior appointments and performance). The relevant ordinances for the eight institutions have provided that there should be a majority of external members in the Councils of the eight institutions (see Table 3 in para. 2.44 above).

2.52 However, due to the absence of some external members, the external members present at the Council meetings might not constitute a majority vote when important decisions were taken. In particular, Audit notes that in the case of the CUHK and the HKU (see paras. 2.53 to 2.58 below), the external members did not constitute a majority at most of the Council meetings held in the three financial years of 2000-01, 2001-02 and 2002-03 (July to November 2002). There was over-reliance on the internal members when important decisions were taken.

Council meetings of the CUHK

2.53 Under The Chinese University of Hong Kong Ordinance, the CUHK can appoint a total of 57 Council members, comprising:

- (a) 23 internal members (16 ex-officio members, and seven elected/appointed staff members);
- (b) three convocation representatives; and
- (c) 31 independent external members (seven life members and 24 other external members).

2.54 Audit's examination of the minutes of the CUHK's Council meetings indicates that six of the seven life members did not attend any of the nine Council meetings held between July 2000 and November 2002. The average numbers and average attendance rates of internal members, the convocation representatives and the external members at the Council meetings in the three financial years of 2000-01, 2001-02 and 2002-03 (July to November 2002) are summarised in Table 5 below.

Table 5

Average numbers and average attendance rates of the Council members of the CUHK in attendance at the Council meetings in 2000-01, 2001-02 and 2002-03 (Note)

| | 2000-01 (July 2000 to June 2001) | | 2001-02 (July 2001 to June 2002) | | 2002-03 (July to November 2002) | |
|-----------------------------|-------------------------------------|--------------------------|-------------------------------------|--------------------------|------------------------------------|--------------------------|
| | Average numbers in attendance | Average attendance rates | Average numbers in attendance | Average attendance rates | Average numbers in attendance | Average attendance rates |
| Internal members | 20 (56%) | 89% | 20 (51%) | 93% | 18 (50%) | 90% |
| Convocation representatives | 3 (8%) | 100% | 3 (8%) | 100% | 3 (8%) | 100% |
| External members | 13 (36%) | 46% | 16 (41%) | 53% | 15 (42%) | 50% |
| Total | 36 | | 39 | | 36 | |

Source: Records of the CUHK

Note: Unfilled vacancies of Council members were excluded in the computation.

2.55 Table 5 above shows that the external members in attendance at the Council meetings in 2000-01, 2001-02 and 2002-03 (July to November 2002) of the CUHK did not constitute the majority. Even counting the convocation representatives as external members, they still did not constitute the majority at most of the Council meetings held between July 2000 and November 2002. This was not in line with a good governance practice for a publicly funded organisation that there should be a majority of number of **independent** external members in the governing body when making decisions of great importance. There was over-reliance on internal members to make decisions at the Council meetings.

Council meetings of the HKU

2.56 Under the University of Hong Kong Ordinance, the HKU can appoint a total of 54 Council members, comprising:

- (a) 20 internal members (18 ex-officio members and 2 elected/appointed staff members);

- (b) six student/alumnus/convocation representatives; and
- (c) 28 external members (who are not officers or employees).

2.57 Audit's examination of the minutes of the HKU's Council meetings indicates that the actual numbers of appointed external members were less than 28 due to unfilled vacancies. The actual number of external members appointed decreased from 27 in 2000-01 to 24 in 2001-02, and to 22 in 2002-03 (July to November 2002). The average numbers and the average attendance rates of internal members, student/alumnus/convocation representatives and external members at the Council meetings in the three financial years of 2000-01, 2001-02 and 2002-03 (July to November 2002) are summarised in Table 6 below.

Table 6
Average numbers and average attendance rates of the
Council members of the HKU in attendance at the Council meetings
in 2000-01, 2001-02 and 2002-03 (Note)

| | 2000-01 (July 2000 to June 2001) | | 2001-02 (July 2001 to June 2002) | | 2002-03 (July to November 2002) | |
|---|-------------------------------------|--------------------------|-------------------------------------|--------------------------|------------------------------------|--------------------------|
| | Average numbers in attendance | Average attendance rates | Average numbers in attendance | Average attendance rates | Average numbers in attendance | Average attendance rates |
| Internal members | 15 (43%) | 88% | 17 (48%) | 90% | 15 (54%) | 84% |
| Student/alumnus/convocation representatives | 4 (11%) | 69% | 3 (9%) | 52% | 2 (7%) | 42% |
| External members | 16 (46%) | 58% | 15 (43%) | 62% | 11 (39%) | 51% |
| Total | 35 | | 35 | | 28 | |

Source: Records of the HKU

Note: Unfilled vacancies of Council members were excluded in the computation.

2.58 Table 6 above shows that the average number of external members in attendance at the Council meetings of the HKU held between July 2000 and November 2002 did not constitute the majority. The average number of external members in attendance dropped from 16 in 2000-01 to 11 in 2002-03 (July to November 2002). Even counting the student/alumnus/convocation representatives as external members, they still did not constitute the majority at the Council meetings held in 2002-03 (July to November 2002). This was not in line with a good governance practice for a publicly funded organisation that there should be a majority of **independent** external members in the governing body when making decisions of great importance. There was over-reliance on internal members to make decisions at the Council meetings.

Audit observations on attendance rates of external members of the Courts

2.59 Of the eight institutions, four (i.e. HKBU, LU, HKUST and HKU) have set up a Court as the advisory body of the institution as laid down in the relevant ordinances. The composition of the membership of the Courts, as at 1 December 2002, is summarised in Table 7 below.

Table 7
The composition of the Courts of HKBU, LU, HKUST and HKU
as at 1 December 2002

| | Total number of members | Internal members | | Student/ alumnus/ convocation representatives | External members | Percentage of external members expressed as a percentage of total number of members |
|-------|-------------------------|------------------|------------------------------|---|------------------|---|
| | | Ex-officio | Staff (elected or appointed) | | | |
| | (a) | (b) | (c) | (d) | (e) | $(f) = \frac{(e)}{(a)} \times 100\%$ |
| HKBU | 40 | 10 | 3 | 2 | 25 | 63% |
| LU | 37 | 2 | 3 | 2 | 30 | 81% |
| HKUST | 44 | 2 | 4 | 2 | 36 | 82% |
| HKU | 252 (Note) | 110 | 62 | 22 | 58 | 23% (Note) |

Source: The Laws of Hong Kong and institutions' records

Note: See Audit's observations in paragraphs 2.30 and 2.31 above. According to Statute XV of the University of Hong Kong Ordinance, members of the Council and members of the Senate are ex-officio members of the Court.

2.60 Audit conducted an analysis of the average attendance rates of external members of the Courts of the four institutions by examining the minutes of the Court meetings held in the three financial years 2000-01, 2001-02 and 2002-03 (July to November 2002). The results of the analysis are summarised in Table 8 below.

Table 8

Average attendance rates of external members of the Court of HKBU, LU, HKUST and HKU in 2000-01, 2001-02 and 2002-03 (Note)

| | 2000-01 (July 2000 to June 2001) | 2001-02 (July 2001 to June 2002) | 2002-03 (July to November 2002) |
|-------|---|---|--|
| HKBU | 72% | 73% | 58% |
| LU | No meeting held | 66% | No meeting held |
| HKUST | 36% | 31% | 39% |
| HKU | 34% | 27% | No meeting held |

Source: Institutions' records

Note: Details of the attendance rates of external members of the four institutions attending the Court meetings are shown in Appendix D.

2.61 Table 8 above shows that the average attendance rates of the external members of the Court of the HKU and the HKUST were low. A significant number of external members were absent at the Court meetings. In the HKU, the average absence rates of external members of the Court were 66% (100% – 34%) in 2000-01 and 73% (100% – 27%) in 2001-02. In the HKUST, the average absence rates of external members of the Court were 64% (100% – 36%) in 2000-01, 69% (100% – 31%) in 2001-02 and 61% (100% – 39%) in 2002-03 (July to November 2002). The average attendance rates in the LU and the HKBU were relatively better.

Audit recommendations on attendance rates of external members of the Councils and the Courts

2.62 Audit has *recommended* that the Secretary-General, University Grants Committee should:

- (a) advise the eight institutions (particularly CUHK and HKU) to ascertain, where necessary, the reasons for the low attendance rates of external members of their

Councils at the Council meetings (e.g. by conducting a survey on the reasons for non-attendance) (see paras. 2.46 and 2.47 above);

- (b) advise the eight institutions to take appropriate action to improve the attendance rate of external members of the Councils at the Council meetings (e.g. providing adequate guidelines on the role and responsibilities of Council members) (see para. 2.48 above);**
- (c) advise the HKU and the HKUST to ascertain the reasons for the low attendance rates of external members of the Courts at the Court meetings, and to take appropriate action to improve the attendance rates of the external members of the Courts (see para. 2.61 above); and**
- (d) recommend to the Government and the institutions that, as a matter of principle, they should not re-appoint those Council/Court members whose attendance at Council/Court meetings is low (see paras. 2.46, 2.47 and 2.61 above).**

Response from the Administration and the institutions

2.63 The **Secretary for Education and Manpower** agrees with Audit's recommendation that, in principle, the Government and the institutions should not re-appoint Court/Council members whose attendance is low. He has said that:

- (a) the Education and Manpower Bureau (EMB) has attached importance to the attendance of external members of Court/Council appointed by the Chief Executive or by him in the capacity as the Chancellor of the institutions;
- (b) when appointing external members, the EMB has specified that the Secretariat of the Court/Council will keep their attendance records, participation in sub-committees, years of service in the Court/Council and the occupation/profession by broad categories for each member. This information will be disclosed to the public on request;
- (c) attendance is one of the factors that will be taken into consideration in all re-appointment exercises; and
- (d) in fact, the attendance of most of the external members appointed by the Chief Executive is well beyond 50%.

2.64 The **Secretary-General, University Grants Committee** has said that the UGC welcomes the Audit's recommendations, which are generally in line with what has been put forth in the UGC Higher Education Review 2002.

2.65 In their replies, the **Heads of Institutions** have said that:

- (a) they will review the matter and explore additional measures to facilitate high attendance of external members (e.g. enhancing communication with external members, providing external members with useful information about the operation of the institution and on their role and responsibilities); and
- (b) attendance rate should not be the only major consideration, nor the principal indicator, in assessing the performance and contributions of the Council members towards the effective management and the institution's affairs. External members actively participate in different committees of the institution and in a wide variety of activities of the institution.

2.66 The **Vice-Chancellor, The Chinese University of Hong Kong** has also said that:

- (a) although it is true that the external members in attendance at the Council meetings in 2000-01, 2001-02 and 2002-03 (July to November 2002) did not constitute the majority, the average number of external members (including convocation representatives) present were already very large:

| | 2000-01 | 2001-02 | 2002-03 |
|------------------|----------------|----------------|----------------|
| External members | 16 (44%) | 19 (49%) | 18 (50%) |
| Internal members | 20 (56%) | 20 (51%) | 18 (50%) |

The external members who were present at the Council meetings took an active part in the deliberation and their views were highly respected and taken into careful consideration. The Council resolutions were passed more often by consensus with support of the external members present, after deliberations and debate;

- (b) Council members were able to participate in the deliberation of any matter on the agenda of a meeting by making their views known in writing or through another Council member attending the meeting even if they could not attend the meeting in person. Furthermore, Council business was transacted by circulation of papers between two Council meetings;

- (c) the external Council members were nominated by various constituent or related organisations of the CUHK or invited by the Council to serve on the Council on a voluntary and non-remunerative basis. Council members were committed to the cause of the CUHK, and had been very generous in contributing their time, efforts and other resources towards enhancing the CUHK's development. The CUHK Council was but one of many public bodies or community/voluntary service organisations soliciting their support. Where the date of a Council meeting clashed with that of another public body/committee, the external Council member concerned might have to be absent from the meeting. At times, it was not always possible to reconcile the dates of Council meetings with external members' travel plans; and
- (d) if presence at all or a majority of Council meetings (three to five times a year) became a pre-requisite for nomination, and failure to do so would attract unwanted public or media attention, it would be even more difficult for the Council to find community-minded persons to serve on the Council.

2.67 **The Vice-Chancellor, The University of Hong Kong** has also said that:

- (a) the HKU's Review Panel has recommended the following to facilitate members' contribution to the Council:
 - (i) induction and continuing development should be made available; and
 - (ii) the agenda should be more structured.

With these initiatives, members will be better advised of the operations of the HKU and will serve on the Council in ways that make best use of their expertise;

- (b) the HKU's Review Panel has also recommended that the appointment term of Council members shall be no more than three consecutive terms of three years, and appointments shall be made on the basis of recognised expertise and contribution. These measures will allow the appointment terms be reviewed regularly and also assist in improving the effectiveness of the Council; and
- (c) the HKU believes that since its Court is an advisory body, attendance at meetings is not the main role of Court members who will be able to contribute in many other manners. In any case, the HKU expects that, with the roles of the Court redefined and its composition recast, the attendance rate of members will be improved.

2.68 The **President, The Hong Kong University of Science and Technology** has said that:

- (a) the audit recommendation on attendance rates of external members of the Court will be referred to the Council for consideration in relation to a review of the HKUST's governance structure; and
- (b) the Court has an advisory and not an executive role. The contribution made by the external members of the Court to the affairs of the HKUST often far exceeds anything that can be measured in terms of attendance at Court meetings.

Audit Committee

2.69 A good corporate governance practice for institutions is that their councils should comprise a majority number of **independent** external members who are capable of exercising independent judgement on important issues, particularly where there is potential conflict of interest. The governance structure should have an audit committee that consists of a majority of **independent** external members, who have the necessary financial expertise and the time to examine the institution's financial affairs more vigorously than the governing body as a whole.

2.70 An audit committee is a well-established feature of corporate governance both in Hong Kong and overseas. In 1997, the Hong Kong Society of Accountants (HKSA — Note 5) issued a "*Guide for the Formation of an Audit Committee*". In 1998, the Stock Exchange of Hong Kong formally endorsed the establishment of an audit committee by listed companies in the Main Board Code of Best Practice and referred to the Guide issued by the HKSA. This HKSA Guide is also referred to by the Stock Exchange of Hong Kong in the Growth Enterprise Market Listing Rules (Chapter 5) as a source of further guidance on the establishment of an audit committee. The concepts contained in this Guide are also applicable to other public corporations, including large not-for-profit organisations. In the UK, the Funding Councils require institutions to appoint an audit committee in accordance with an Audit Code of Practice.

2.71 An audit committee is nowadays a fundamental part of the corporate governance landscape in Hong Kong. The function of an audit committee is seen as assisting the governing body in providing an independent review of the effectiveness of the financial reporting process, internal control and risk management system of the organisation, overseeing the audit process and performing other duties as assigned by the governing body. The committee will report and make recommendations to the governing body on matters pertaining to its work and findings. Members of the audit committee, as external members of the governing body, are an integral part of the governing body. In February 2002, the HKSA published a "*Guide for Effective Audit Committees*", which sets out, as an updated guide, to cover the implementation and disclosure aspects of an effective audit committee.

Note 5: *The HKSA is established under the Professional Accountants Ordinance (Cap. 50). Its main function is to regulate the practice of the accountancy profession and set professional standards.*

2.72 Audit examined the internal audit arrangements of the eight institutions. (The financial statements of the eight institutions are audited by certified public accountants.) The internal audit arrangements are summarised in Table 9 below.

Table 9

Internal audit arrangements of the eight institutions

| | Setting up of an internal audit section | Internal audit reporting to the Council | Setting up of an Audit Committee |
|-------|--|--|---|
| CityU | ✓ | ✓ | ✗ |
| HKBU | ✗ | ✗ | ✗ |
| LU | ✗ | ✓ | ✓ |
| CUHK | ✓ | ✗ | ✗ |
| HKIEd | ✓ | ✓ | ✓ |
| PolyU | ✓ | ✓ | ✗ |
| HKUST | ✓ | ✓ | ✓ |
| HKU | ✓ | ✓ | ✗ |

Legend: ✓ = Yes

✗ = No

Source: Institutions' records

Audit observations on internal audit and audit committee

2.73 The HKBU and the LU have not set up an internal audit section. The internal audit function of the HKBU is largely taken up by the Finance Office, and the findings of the internal audit work are reported to the Director of Finance. The HKBU and the LU outsource ad hoc internal audit reviews to external consultants as and when such work is required. The internal audit section of the CUHK reports its findings and work to the Head of Institution, instead of to an audit committee or to the Council. The internal audit section of CityU, and that of the PolyU, periodically submits summary reports to the Executive Committee (a Council Committee) and the Council. The internal audit section of the HKU reports its findings and work to the Finance

Committee of the HKU Council on a quarterly basis from January 2003, instead of reporting on an annual basis.

2.74 The LU has set up an Internal Audit Committee, which is similar to an Audit Committee. It comprises a small number of external members of the Council, and reports its work to the Council. Probably due to the fact that the Internal Audit Committee was only established recently, it did not have an audit programme and no work had been assigned to it. The LU has advised Audit that the LU is in the process of developing a five-year rolling internal audit programme, and would invite proposals from relevant professional firms (external consultants) to carry out the required work to be commenced in 2003.

2.75 Audit notes that CityU, the HKBU, the CUHK, the PolyU and the HKU have not set up an audit committee. As the institutions are entrusted with large sums of public money, they have a duty to achieve a high standard of corporate governance, which includes the establishment of an audit committee. The audit committee will assist the governing body by providing an independent review of the effectiveness of the auditing and financial reporting processes, internal controls and risk management systems of the institutions. The audit committee will also help enhance economy, efficiency and effectiveness and secure value for money in all areas of activities of the institutions.

Audit recommendation on internal audit and audit committee

2.76 **To strengthen the internal audit function and the corporate governance structure of the institutions, Audit has recommended that the Secretary-General, University Grants Committee should request CityU, the HKBU, the CUHK, the PolyU and the HKU to set up an audit committee (see para. 2.75 above).**

Response from the Administration and the institutions

2.77 The **Secretary for Education and Manpower** has said that Audit's recommendation is in line with the Government's decision following the UGC Higher Education Review (see para. 1.8 above). The Government accepted the UGC's recommendation that the universities should review their governance and management structures to ensure that they are appropriate for modern days, drawing on the principles and international good practices.

2.78 The **Secretary-General, University Grants Committee** has said that the UGC welcomes the Audit recommendation. The UGC also sees the importance of the role of an independent Audit Committee in the institutions' governance structure. The Chairperson, UGC had asked the Heads of Institutions to pay particular attention to this aspect in her meeting with the Heads of Institutions in November 2002.

2.79 The **President, The Hong Kong Polytechnic University** agrees with the audit recommendation to set up an audit committee. The **Vice-Chancellor, The University of Hong**

Kong has said that the Review Panel on Governance and Management has reviewed the committee structure of the Council, and has made a recommendation for the Council to set up an audit committee.

2.80 The **President, City University of Hong Kong** has said that the Review Committee on Governance and Management will consider whether it is necessary to set up an audit committee in addition to the existing internal audit section. The **President and Vice-Chancellor, Hong Kong Baptist University** has said that he is prepared to take up the audit recommendation of setting up an audit committee in the context of the “fitness for purpose” review of the governance and management structures.

2.81 The **Vice-Chancellor, The Chinese University of Hong Kong** has said that the CUHK has set up a professional and very rigorous internal audit function for a decade. Audit’s recommendation for an audit committee to be established under the Council will be seriously considered.

Audit observations on governance structure review

2.82 Institutional governance is one of the subjects covered by the Sutherland Report (see para. 1.8 above). Chapter 3 of the Report provides a comprehensive analysis on governance in Hong Kong institutions. The Report also draws reference to principles and international good practices on governance and management structures of overseas institutions. One of the recommendations of the Report which was accepted by the Government was that the councils of the eight institutions should review their governance structures to ensure “fitness for purpose”, drawing on the principles and international good practices set out in the UGC review report.

2.83 At the time of completion of this Audit in December 2002, the HKU and the CUHK had separately embarked on a review on their governance structures. The Review Panel of the HKU submitted its report to the HKU in February 2003. The review panel of the CUHK was expected to submit a report to the CUHK in March 2003. Other institutions would also conduct a review of their governance structures.

2.84 Audit supports the action taken or to be taken by the eight institutions to review their governance structures. Audit considers that the governing bodies of the institutions need to conduct periodic reviews of their effectiveness. Periodic and systematic self-assessments on effectiveness will assist the governing bodies in achieving their objectives and finding the best way to oversee and direct the institutions. The scope of the review may include evaluating the governing bodies’ own effectiveness, arrangements for disclosing their own performance to the various stakeholders (e.g. students, teaching and other staff and the public), and the performance of the institutions on their principal activities and responsibilities.

2.85 In the UK, a principal recommendation arising from the 1997 Report of the National Committee of Inquiry into Higher Education in England, Wales and Northern Ireland (the Dearing Report) was that the governing bodies should periodically review their own effectiveness. In response, the Committee of University Chairmen has published two progress reports on the effectiveness of university governing bodies. The progress report of 2000 contains a composite checklist of possible review points, covering the governing body's role, responsibilities and its methods of operation. The eight institutions could make reference to these progress reports about the principles, good practices and possible methods of conducting a review on the effectiveness of their governing bodies.

Audit recommendations on governance structure review

2.86 **Audit has recommended that the Secretary-General, University Grants Committee should request the eight institutions to:**

- (a) **take into account the findings of this audit report on governance arrangements and good practices in their reviews of their governance structures (see para. 2.83 above); and**
- (b) **conduct periodic (say every five years) reviews of the effectiveness of their governing bodies (see para. 2.84 above).**

Response from the Administration and the institutions

2.87 The **Secretary for Education and Manpower** has said that Audit's recommendations are in line with the Government's decision following the UGC Higher Education Review (see para. 1.8 above). The Government accepted the UGC's recommendation that the universities should review their governance and management structures to ensure that they are appropriate for modern days, drawing on the principles and international good practices.

2.88 The **Secretary-General, University Grants Committee** has said that the UGC welcomes the Audit's recommendations, which are generally in line with what has been put forth in the UGC Higher Education Review 2002. As part of the UGC's efforts in promoting institutions' performance, the UGC will conduct a Comprehensive Audit on institutions, which will cover teaching, research, community service, governance and management. The UGC plans to conduct the first Comprehensive Audit in the 2005-08 triennium.

2.89 The **Heads of Institutions** agree to take the audit recommendations into consideration in the "fitness for purpose" review, or will continue the practice to conduct periodic reviews of the governance structure and effectiveness.

PART 3: STRATEGIC PLANNING OF INSTITUTIONS

3.1 This PART examines the efficiency and effectiveness of the strategic planning processes and arrangements of the institutions for achieving their missions.

Institutions' objects as stated in Ordinances

3.2 With the exception of the CUHK and the HKU, the Ordinances which established the other six institutions have set out the objects of the institutions. The objects of these six institutions are:

- (a) **CityU:** to provide for studies, training and research and development in technology, engineering, science, commerce, arts and other subjects of learning;
- (b) **HKBU:** to provide for studies, training and research in science, commerce, social science, arts and other subjects of learning;
- (c) **LU:** to provide for education, studies, training and research in arts, humanities, business, social sciences, science and other subjects of learning;
- (d) **HKIEd:** to provide teacher education and facilities for research into and the development of education;
- (e) **PolyU:** to provide for studies, training and research in technology, science, commerce, arts and other subjects of learning; and
- (f) **HKUST:**
 - (i) to advance learning and knowledge through teaching and research, particularly in science, technology, engineering, management and business studies, and at the postgraduate level; and
 - (ii) to assist in the economic and social development of Hong Kong.

3.3 In the preamble of the Chinese University of Hong Kong Ordinance, it is stated that the *CUHK* shall continue to:

- (a) assist in the preservation, dissemination, communication and increase in knowledge;
- (b) provide regular courses of instruction in the humanities, the sciences and other branches of learning of a standard required and expected of a university of the highest standing; and
- (c) stimulate the intellectual and cultural development of Hong Kong and thereby to assist in promoting its economic and social welfare.

3.4 In Statute XXIII of the University of Hong Kong Ordinance, it is stated that the Senate of the *HKU* shall have power, in consultation with the Boards of Faculties, to provide courses of study for the degrees, diplomas, certificates, and other awards by the university and such other courses of study as may be thought desirable, to direct and regulate the instruction and education in the university, to stimulate the advancement of knowledge by research and publications, and to direct the manner in which examinations shall be conducted.

Audit observations on strategic planning of institutions

Institutions' strategic and operational planning

3.5 As stated in paragraphs 3.2 to 3.4 above, in general, the objects of the institutions are to provide for studies, training, research and development in different subjects of learning and assist in the economic and social development of Hong Kong. In order to achieve these objects in an efficient and effective manner, it is necessary for the institutions to conduct strategic planning exercises periodically.

3.6 An institution's strategic plan normally covers a period of three years or more. The plan generally sets out the institution's strategic objectives, operational goals, strategic actions for achieving the goals and outcome indicators for measuring its performance. Furthermore, under good management practices, an institution normally prepares annual operational plans which set out the initiatives and targets for achievement in relation to the strategic objectives and operational goals stated in its strategic plan. The institution also adopts an annual review process for examining the extent to which the targets have been attained.

3.7 In Audit's review of the arrangements of the institutions in relation to the strategic and annual planning processes, Audit noted that there was room for improvement in some institutions. Audit's observations are discussed in paragraphs 3.8 to 3.21 below.

Need for institutions to prepare strategic plan

3.8 At the time of completion of Audit's examination in late December 2002, Audit noted that:

- (a) with the exception of the HKUST and HKU, the other six institutions had prepared a strategic plan which set out the strategic objectives, operational goals and strategic actions for achieving the goals; and
- (b) of the six institutions which had prepared strategic plans, with the exception of the LU, five institutions (CityU, HKBU, CUHK, HKIEd and PolyU) had made their strategic plans available to the public by uploading them onto the institutions' websites.

3.9 Audit noted that, in 1996, the HKU prepared a "Strategic Priorities and Objectives of the University" document. In early 2000, the HKUST adopted a statement known as the Mission, Vision and Objectives. Audit also noted that the HKUST and the HKU were taking action to finalise their strategic plans. **Audit considers that the HKUST and the HKU need to expedite action to finalise their strategic plans to formally set out their strategic objectives, operational goals and strategic actions for achieving the goals.**

Need for institutions to prepare institutional operational plans

3.10 Audit noted that individual departments/faculties of each institution normally prepared their own departmental or faculty operational plans. These operational plans were developed by the departments/faculties after consultation with the staff and relevant committees. Some of these operational plans provided a link to the institutions' strategic plans. However, at the time of completion of Audit's examination in late December 2002, Audit noted that all the eight institutions did not produce annual institutional operational plans to provide a link to the institutions' strategic plans.

3.11 **In order to ensure that the departmental and faculty plans and activities of an institution would lead to the achievement of the institution's visions and missions, there is a need for the institution to develop an annual institutional operational plan for implementing the strategies in the strategic plan.** This operational plan would help consolidate the key objectives, strategic initiatives and targets into one document. In December 2002, in response to Audit's enquiries, the HKU stated that it would develop an annual institutional operational plan after its strategic plan had been approved by the HKU's Senate and Council.

Need for institutions to prepare progress reports

3.12 *Institutions' reporting of achievements against targets.* As discussed in paragraph 3.10 above, the eight institutions did not prepare annual institutional operational plans. In general, the

institutions reported their achievements in their annual reports, ad hoc reports, periodicals, websites and submissions to the UGC. In such reports and submissions, the institutions generally reported their research outputs, academic commendations and prizes awarded to their students and academics, new developments and achievements of each area of teaching and learning, student exchange programmes, new initiatives, etc. Unlike universities in advanced countries, the institutions did not adopt a practice of setting targets and reporting progress of achievement in respect of each target.

3.13 ***Overseas universities' reporting of achievements against targets.*** Audit conducted a research on the reporting of achievements by some universities in advanced countries against the targets set by them. In the research, Audit selected the largest university (in terms of student population) in Australia, Canada, New Zealand, UK and USA (Note 6) for examination. Audit noted that, in general, the five selected universities prepared annual plans which set out targets for achievement, which were derived from the goals set out in their strategic plans. In their annual reports, the universities reported their progress of achievement in respect of the goals and/or targets. The practices of these universities were as follows:

- (a) ***Australia.*** The university set out seven goals in its strategic plan. For each of the goals, the university set out a number of objectives for achievement. In its annual reports, the university reported the progress of achievement in respect of each of the seven goals of the university;
- (b) ***Canada.*** The university set out ten key priorities in its strategic plan. For each of the key priorities, the university set out a number of objectives for achievement. One of its objectives was that the university should have in place the means for determining and reporting, on a regular and on-going basis, progress in meeting its objectives. Every year, the university published a report on performance indicators for governance which summarised the major areas of achievement of the university in relation to the targets and goals set out in the strategic plan;
- (c) ***New Zealand.*** The university established eight goals in its *Mission Goals and Strategies*. Every year, the university published an annual report which, in respect of each of the goals of the university, presented the achievements and highlights of the university in the past year. In the statements of service performance of the annual reports, the university also set out targets for achievement in respect of some key result areas and reported the progress of achievement of the targets set;

Note 6: *The largest university in the UK and in the USA each comprises a number of colleges. Audit selected the largest college (in terms of student population) in each of these two universities for examination.*

- (d) **UK.** Individual departments of the university published their annual reports which set out the aims and objectives of the departments. Every year, each department conducted a self-assessment of its performance in teaching, learning and assessment and reported the results in its annual report. The departmental annual reports also included progress of student progression, student achievement, quality assurance and quality enhancement; and
- (e) **USA.** In the university's New Business Architecture Strategy, it set out the university's goals and performance measures. Based on these goals and measures, individual campuses of the university developed their specific business-area goals and measures and reported their performance accordingly.

3.14 **In order to enhance public accountability, Audit considers that the institutions need to consider adopting the good practices of universities in advanced countries on setting targets and reporting progress, as discussed in paragraph 3.13 above. The institutions' annual progress reports should be made available to the public (e.g. by uploading them onto their websites).**

Need for institutions to include community services in operational plans

3.15 ***Community services included in the ordinances of some institutions.*** In The Hong Kong University of Science and Technology Ordinance, it is set out that one of the objectives of the HKUST is to assist in the economic and social development of Hong Kong (see para. 3.2(f)(ii) above). In The Chinese University of Hong Kong Ordinance, it is also stated that one of the CUHK objectives is to stimulate the intellectual and cultural development of Hong Kong and thereby to assist in promoting its economic and social welfare (see para. 3.3(c) above).

3.16 ***Community services included in institutions' strategic plans.*** Some institutions included mission statements relating to community services in their strategic plans. The mission statements are as follows:

- (a) ***CityU:*** to cooperate with industry, commerce and the community, and to offer access to the university's human, physical and technological resources for the benefit of society;
- (b) ***CUHK:*** to assist in the preservation, creation, application and dissemination of knowledge by teaching, research and public service in a comprehensive range of disciplines;

- (c) **HKIEd:** to collaborate with schools and other relevant organisations on innovation and change in education; and
- (d) **PolyU:** dedicated partnerships with business, industry and the professions.

3.17 In December 2002, in response to Audit's enquiries, the HKU stated that it had a proposal to produce a community service plan which would assist staff and students to engage in outreach programmes for the community, so that the quality and benefits of the HKU's scholarship could be communicated beyond campus.

3.18 **Community services provided by institutions.** The following are the major community services provided by the institutions:

- (a) staff serving as members of government advisory bodies and public organisations in their personal capacity. In some circumstances, institutions grant special leave to staff to enable them to provide such services;
- (b) staff offering professional opinions to society through the media in their personal capacity;
- (c) institutions participating in consultancy projects for the Government and public organisations;
- (d) institutions providing free services to school students and the elderly; and
- (e) institutions conducting public seminars, workshops, symposiums, forums and conferences on a wide range of topics.

3.19 **Reporting of community services.** The institutions generally reported their activities relating to the provision of community services in their annual reports, ad hoc reports, periodicals, websites and submissions to the UGC. In addition, the institutions' faculties and departments compiled annual reports which covered initiatives and actions taken relating to the provision of community services. Furthermore, some institutions required their staff members to include the community services provided by them in their annual performance appraisal reports, which formed a part of the performance assessment.

3.20 In a speech in the Legislative Council on 26 June 2002, the then Secretary for Education and Manpower said that:

- the core task of a university was no doubt to create knowledge, nurture talents and serve the community. In the academic world, research work was often looked upon as a means of asserting one's status and reputation. Many professors regarded teaching as their career mission, and, to them, serving the community was only of secondary importance; and
- as times changed, the mission of universities should be revised accordingly. At this time of social anxieties and economic restructuring, the responsibilities of universities had become ever heavier than before, as they had to serve as the beacons of society, take an impartial lead in discussions about social issues, draw the strengths of society together and assist in social development founded on their solid research capabilities.

3.21 **Audit considers that the institutions should enhance their role in the provision of community services. To achieve this goal, the institutions should set out in their annual institutional operational plans their targets for achievement in the area of community services.**

Audit recommendations on strategic planning of institutions

3.22 **In order to enhance the public accountability of the institutions, Audit has recommended that the Secretary-General, University Grants Committee should request:**

- (a) **the HKUST and the HKU to expedite action to finalise their strategic plans to set out their strategic objectives, operational goals and strategic actions for achieving the goals (see para. 3.9 above);**
- (b) **the LU, the HKUST and the HKU to upload their strategic plans onto their websites for the information of the public (see para. 3.8(a) and (b) above); and**
- (c) **the eight institutions to:**
 - (i) **develop annual institutional operational plans to set out clear targets for achievement (see para. 3.11 above);**

- (ii) **prepare annual progress reports to present the progress of achievement in respect of the targets set out in their annual operational plans (see para. 3.14 above);**
- (iii) **upload their progress reports onto their websites for the information of the public (see para. 3.14 above); and**
- (iv) **enhance their role in the provision of community services by setting relevant targets for achievement in their annual operational plans (see para. 3.21 above).**

Response from the Administration and the institutions

3.23 The **Secretary for Education and Manpower** has said that:

- (a) Audit's recommendations on the strategic planning of the institutions are in line with the Government's decision that role differentiation among the UGC-funded institutions should be strengthened to promote diversity and excellence. This requires the institutions to articulate a clear mission and to focus their efforts strategically to compete at the highest international level; and
- (b) the EMB agrees with Audit's recommendations that individual institutions should better map out their own strategic development blueprint, develop operational plans and monitor progress regularly. This should facilitate the institutions in their strategic development and the pursuit of role differentiation. The UGC will conduct periodic comprehensive reviews on the institutions covering research, teaching, governance and management as well as community service.

3.24 The **Secretary-General, University Grants Committee** has said that:

- (a) the UGC welcomes Audit's recommendations on the strategic planning of the institutions, and considers them to be generally in line with the UGC's aim of ensuring stronger role differentiation among the institutions, concentrating resources in areas of strength, encouraging diversity and excellence, and inducing enhanced transparency to stakeholders;
- (b) to reward and further encourage the institutions' performance according to their respective roles, the UGC will conduct another round of performance-based funding scheme to inform funding for the 2005-08 triennium, in which the institutions' overall

vision, strategic orientation, development and operational plans, support mechanisms, efforts in key result areas and how they are measured will be looked at comprehensively and qualitatively; and

- (c) the UGC agrees that community service should feature as an important aspect of the institutions' performance. It is the UGC's plan to include community service as an element in the forthcoming performance-based funding exercise and in the Comprehensive Audit in future.

3.25 The **President, City University of Hong Kong** agrees with Audit's recommendations on:

- (a) developing annual institutional operational plans;
- (b) preparing annual progress reports to present the progress of achievement in respect of the targets set out in the operational plans; and
- (c) uploading the progress reports onto CityU's website for the information of the public.

3.26 The **President and Vice-Chancellor, Hong Kong Baptist University** has said that the HKBU is prepared to take up Audit's recommendations on developing annual institutional operational plans and progress reports, uploading progress reports onto the HKBU's website and the provision of community services in the context of the HKBU's "fitness for purpose" review of the governance and management structures, which is to be conducted later this year.

3.27 The **President, Lingnan University** has said that:

- (a) the LU will upload its strategic plan onto its website so that the plan will be accessible to the public;
- (b) in its "*Updated Strategic Plan 1997-2002*" and the draft "*Strategic Plan for 2003-10*", the LU provided "operational goals, activities/tactics in support of goals, implementation time frame, responsible units, and outcome indicators/evaluation" which link to the strategic objectives in the University's four main strategic areas. The LU conducted two rounds of comprehensive evaluations of the LU's strategic plan as well as all unit-level strategic plans at the senior management retreats, although the evaluations were not conducted on an annual basis;

- (c) as recommended by Audit, the LU will prepare an annual operational plan from 2003 onwards. Units of the LU will be required to report their progress and whether targets have been achieved on an annual basis; and
- (d) in the LU's *"Updated Strategic Plan 1997-2002"*, it spells out that the LU needs to strengthen its relationship and linkages with external stakeholders including assistance in the development of the Hong Kong community with special attention to the Northwest New Territories. The LU has set up a Community Development Committee since 1995, which is unique in Hong Kong's tertiary institutions. During the period 1995-2002, the LU had been encouraging staff members and students to get involved in many community projects such as the "Project X", which was a joint project with the Tuen Mun Police Headquarters and Tuen Mun District Fight Crime Committee. In addition, academic staff are also encouraged to provide research data to the public on public issues, for example the research on impact of stress on managers and practicum research on the care of the aged.

3.28 **The President, The Hong Kong Institute of Education** has said that:

- (a) in its current strategic planning framework, the HKIED develops Institutional Development Plans with a three-year focus and annual Unit Operational Plans with a one-year focus. The HKIED will consider streamlining the existing planning processes to include the development of an annual institutional operational plan, the achievements of which are to be reviewed through annual progress reports, when it starts to develop its next Strategic Plan for 2004 and beyond; and
- (b) in relation to the provision of community services, two of the key missions of the HKIED are to collaborate with schools and other relevant organisations on innovation and change in education, and to contribute to the formulation and development of educational policies in Hong Kong. In December 2001, the HKIED developed a preliminary set of Institute-level Performance Indicators, which included the number and types of community services provided by the HKIED's staff, together with their consultancies and professional support services in schools. Recently, the HKIED has also set up a Focus Group on Research and Community Services to review, inter alia, the HKIED's contributions to community services such as school partnership and networks and collaborative projects with educational communities, and to recommend on future development. Nevertheless, contributions to community services cannot always be quantified and measured in a short time span, especially for cases that involve improvement in the quality of educational outcomes in schools and helping the Government in setting education policies.

3.29 **The President, The Hong Kong Polytechnic University** has said that:

- (a) the PolyU's Strategic Planning Committee has been conducting annual reviews to ensure that departmental and faculty activities would lead to the achievement of the University Strategic Plan. It also monitors the progress against targets and initiates any further action required to achieve the plan; and
- (b) the PolyU agrees with Audit's recommendations on the strategic planning of the institutions and will further promulgate its efforts and achievements in this area.

3.30 **The President, The Hong Kong University of Science and Technology** has said that:

- (a) as led by its Council, in 1999, the HKUST formed a Task Force on Strategic Development. In early 2000, after a series of meetings, the Task Force adopted an elaborate statement based on the one proclaimed in the HKUST Ordinance, which is known as the Mission, Vision and Objectives. The statement lays down the guiding principles by which the HKUST will pursue its next phase of development;
- (b) in mid-2000, the Task Force formed five sub-groups, namely sub-group on resource and land, talents and leadership, areas of excellence, government/business/community connectivity and non-local connectivity. In early 2001, the five sub-groups conducted a comprehensive study and formulated some recommendations. The sub-groups' recommendations, when integrated, will form the basis for the development of a strategic plan to translate the Mission, Vision, and Objectives statement into reality; and
- (c) the HKUST will give careful consideration to Audit's recommendation on the preparation of a strategic plan, having regard to the fact that, in the current changing circumstances, further thought is likely to be given to an elaboration of the HKUST's role.

3.31 **The Vice-Chancellor, The University of Hong Kong** has said that:

- (a) following one of the periodic reviews of the HKU's organisational and management structures and the publication of a new Vision and Mission statement, the HKU appointed a new Pro-Vice-Chancellor in December 2000 with the specific responsibility of coordinating the HKU's strategic planning and development activities. A Strategic Planning Unit was established in February 2001 to provide support to the Pro-Vice-Chancellor concerned, which works closely with the Management Information

Unit of the Registry in analysing the underpinning management information needed to inform executive decisions. A key project undertaken by the Strategic Planning Unit in the last 18 months or so has been the formulation of an Institutional Strategic Plan. The Pro-Vice-Chancellor (Planning and Resources) has been working with the Working Group on Strategic Planning in identifying key strategic issues that have to be developed, based on the HKU's Vision and Mission, through wide consultations and open forums with members of the HKU and the wider communities which it serves;

- (b) the HKU in fact prepared a "Strategic Priorities and Objectives of the University" document in 1996, setting out the University's development plan and objectives. This document was submitted to the UGC in December 1996, and was discussed by the University with the UGC in January 1997. The HKU is now preparing its Plan for Strategic Development for 2003-08 which is about to be submitted for consideration and consultation. However, in view of the strategic importance of the plan, the processes will necessarily involve other stakeholders, and proper deliberations and consultations will have to be carried out before it is finalised. The plan will be uploaded onto the HKU's website in due course;
- (c) Audit's recommendations on developing an operational plan and producing a progress report to present the achievements have been built into the new strategic planning process. The HKU is prepared to upload these plans and progress reports onto the HKU's website; and
- (d) regarding Audit's recommendation on enhancing the HKU's role in the provision of community services, the HKU has always been actively doing this and intends to continue doing so in the future. However, sometimes it is not easy to lay down targets for community services, as the value provided by such services is not always measurable by quantitative targets or performance indicators.

PART 4: FINANCIAL REPORTING OF INSTITUTIONS

4.1 This PART examines the financial reporting of the institutions with reference to the generally accepted accounting principles and practices of advanced countries.

Statutory requirements on institutions' preparation of financial statements

4.2 Each of the institutions is an autonomous body established under its own Ordinance. In relation to accounts and external audits, the relevant Ordinances have generally laid down the requirements that:

- (a) the institutions shall maintain proper accounts and records of all income and expenditure;
- (b) after the end of a financial year, the institutions shall prepare statements of income and expenditure for the financial year and of the assets and liabilities of the institutions on the last day of the financial year; and
- (c) the institutions shall appoint auditors, who shall audit the institutions' financial statements and shall report thereon to the institutions.

Audit observations on financial reporting of institutions

Objectives of financial statements

4.3 As defined by the HKSA, the primary objective of financial statements of an enterprise is to provide information that is useful to users for the purpose of assessing:

- (a) the financial position at a particular point in time;
- (b) the performance and cash flows during a specified period of time; and
- (c) the accountability of the management for the resources entrusted to it during that period.

Accounting Standards issued by HKSA

4.4 As the statutory body which is responsible for regulating the practice of the accountancy profession in Hong Kong, the HKSA develops and issues Statements of Standard Accounting

Practice of Hong Kong (HKSSAPs) as authoritative statements on accounting practices. The primary aim is to narrow the areas of difference and variety in the accounting treatments in the preparation of financial statements by different organisations.

4.5 **Requirements on compliance with HKSSAPs.** In relation to compliance with the HKSSAPs, the HKSA states that:

- (a) **HKSSAPs are authoritative statements of how particular types of transaction and other events should be reflected in the financial statements and, accordingly, compliance with HKSSAPs will normally be necessary for the financial statements to give a true and fair view;**
- (b) the HKSA envisages that only in extremely rare circumstances will departure from the requirements of an HKSSAP be necessary in order for financial statements to give a true and fair view;
- (c) financial statements should not be described as complying with the HKSSAPs nor as having been prepared in accordance with accounting principles generally accepted in Hong Kong unless they comply with all the requirements of each applicable HKSSAP; and
- (d) inappropriate accounting treatments are not rectified either by disclosure of the accounting policies used or by notes or explanatory materials.

Statement of Recommended Practice developed and issued by institutions

4.6 **Statement of Recommended Practice.** In 1993, a Task Group on Uniform Accounting Policies and Practices consisting of the finance directors of the seven institutions (Note 7) was formed with a view to formulating a Statement of Recommended Practice (SORP) for the preparation of financial statements of the institutions. In 1994, the Task Group sent a draft SORP to the HKSA, UGC and the institutions' external auditors for comments. Comments from the HKSA, UGC and external auditors were discussed and, where appropriate, incorporated into the draft. In February 1996, the HKSA commented that the SORP clearly represented a significant step forward in ensuring comparability among the financial statements of the institutions. However, the HKSA could not give a formal endorsement to the SORP, unless the SORP complied with the HKSSAPs.

Note 7: *The HKIEd was established in 1994.*

4.7 In 1996, the Task Group issued a SORP for reference by the institutions for the preparation of their financial statements. The objective was to provide a standard to enhance the usefulness and comparability of the published financial information among the institutions. In the preface of the SORP, it is stated that:

- (a) the SORP takes into account the generally accepted accounting practices as detailed in the HKSSAPs and International Accounting Standards;
- (b) where full compliance with the HKSSAPs and International Accounting Standards is considered inappropriate, such departures are highlighted in the SORP and required to be disclosed in the financial statements of the reporting institution;
- (c) in developing the SORP, reference was made to the Statement of Recommended Accounting Practice: Accounting in Higher Education Institutions of the UK, and the Financial Accounting and Reporting Manual for Higher Education of the USA; and
- (d) a detailed review of the practical application will be undertaken after three years (i.e. in 1999) from the first year of implementation.

4.8 ***Areas of departure from the HKSSAPs.*** The SORP states that the institutions' financial statements should be prepared on the basis of assumptions in accordance with the generally accepted fundamental concepts as set out in the HKSSAPs, except the following:

- (a) ***Recognition of expenses earlier than in accordance with the HKSSAPs.*** Expenditure should include all purchase orders placed with suppliers for goods/services not yet received. This principle should also be applied to research projects and staff training programmes;
- (b) ***Amortisation of the value of fixed assets on a basis other than in accordance with the HKSSAPs.*** Capital expenditure (including the purchase of furniture and equipment), except that financed by credit facilities and finance leases or for an activity with a clear objective for profit, should be written off against the related funds in the year of expenditure; and
- (c) ***Treatment of stock different from the HKSSAPs.*** Stock items, except those held for self-financing activities, are written off in the year of purchase.

4.9 ***Reasons for SORP to depart from HKSSAPs.*** It is stated in the SORP that:

- (a) while the financial statements of the institutions are prepared as far as possible on a similar basis as the financial statements of other corporate organisations, the peculiarities of the institutions have rendered some of the commonly accepted accounting standards inapplicable; and
- (b) the institutions are entities distinguishable from other corporate bodies and, in some unique circumstances, will give rise to the need for specific accounting treatments in some selected topics.

4.10 ***Disclosure requirements and effective date of SORP.*** The SORP states that the details of grounds for any material deviations from the HKSSAPs and the SORP should be disclosed in the notes to the institutions' financial statements, and that the SORP should be implemented for such financial statements with accounting periods ending on or after 30 June 1996.

Audit examination of the institutions' financial statements

4.11 Audit examined the financial statements of the eight institutions for the year ended 30 June 2002. It was noted that the institutions had adopted accounting treatments which were at variance with the HKSSAPs, as indicated in paragraphs 4.12 to 4.33 below.

Institutions' accounting treatments depart from HKSSAPs (which are explicitly recommended in the SORP)

4.12 The institutions had stated in their financial statements that the statements had been prepared on the accrual basis of accounting, and that the institutions generally complied with the SORP on the three areas where the SORP has explicitly recommended that institutions should adopt accounting treatments which are at variance with the HKSSAPs (see para. 4.8 above). The three areas are as follows:

- (a) ***Recognition of expenses.*** Expenses are recognised at the time of placing orders instead of receipt of goods or services (see para. 4.15 below);
- (b) ***Property, plant and equipment.*** Capital expenditures are written off instead of being capitalised as assets (the value of assets is not amortised over their useful life by means of depreciation — Note 8) (see para. 4.16 below); and

Note 8: *The HKUST has adopted an accounting policy of capitalising assets and amortising their value by annual depreciation.*

- (c) **Recognition of assets.** Stock items are written off in the year of purchase instead of being capitalised as assets (see paras. 4.17 to 4.19 below).

**Institutions' accounting treatments depart
from HKSSAPs (which are not mentioned in the SORP)**

4.13 The SORP states that it takes into account the HKSSAPs and that where full compliance with the HKSSAPs is considered inappropriate, such departures are highlighted in the SORP and are required to be disclosed in the financial statements of the reporting institution (see para. 4.10 above). It implies that, in general, the institutions need to comply with the HKSSAPs in all accounting treatments, except the three areas as mentioned in paragraph 4.8 above. However, Audit's examination of the institutions' financial statements for the year ended 30 June 2002 revealed that, apart from the three areas covered by the SORP, some of the institutions did not comply with the accounting treatments laid down in some other HKSSAPs. The major areas of departure from the other HKSSAPs by the institutions are as follows:

- (a) **Presentation of consolidated financial statements.** With the exception of the LU which did not have any subsidiary (Note 9) or associate (Note 10), all the other seven institutions did not prepare consolidated financial statements to present their financial affairs and those of their subsidiaries and associates together (see paras. 4.20 to 4.25 below); and
- (b) **Related-party transactions.** All the eight institutions did not disclose transactions with related parties in their financial statements (see paras. 4.29 to 4.33 below).

Recommended accounting treatments promulgated in HKSSAPs

4.14 The HKSSAPs lay down standard accounting practices for the areas of accounting stated in paragraphs 4.12 and 4.13 above, which are further described in paragraphs 4.15 to 4.33 below. The current accounting treatments by the institutions are at variance with the standard accounting practices.

Note 9: *A subsidiary is an enterprise that is controlled by another enterprise. Control is the power to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities.*

Note 10: *An associate is an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.*

Accounting treatment of recognition of expenses

4.15 ***HKSSAP on recognition of expenses.*** The Framework (Note 11) of the HKSSAPs (HKSA's Statement 2.01) states that the definition of expenses encompasses losses as well as those expenses that arise in the course of the activities of an enterprise. Expenses that arise in the course of the activities of the enterprise include, for example, cost of sales, wages and depreciation. They usually take the form of an outflow or depletion of assets such as cash and cash equivalents, stocks and work in progress, property, plant and equipment. The recognition of expenses at the time of placing orders does not match with the definition of expenses stated in the HKSSAPs (cf. paras. 4.8(a) and 4.12(a) above).

Accounting treatment of property, plant and equipment

4.16 ***HKSSAP on property, plant and equipment.*** HKSSAP 17 states that the depreciable amount of an item of property, plant and equipment should be allocated on a systematic basis over its estimated useful life. The depreciation method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise (cf. paras. 4.8(b) and 4.12(b) above).

Accounting treatment of recognition of assets

4.17 ***HKSSAP on recognition of assets.*** The Framework of the HKSSAPs (HKSA's Statement 2.01) states that an asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise. Hence, the institutions should account material stock items such as library books and periodicals as assets and adopt the accounting treatments as stated in paragraph 4.16 above (cf. paras. 4.8(c) and 4.12(c) above).

4.18 ***Writing off of library books and periodicals in the year of acquisition.*** Regarding paragraph 4.12(c) above, some institutions (LU, CUHK and HKUST) stated in their financial statements for the year ended 30 June 2002 that stationery stock, library books and periodicals were written off to the Income and Expenditure Statements in the year of acquisition. In 2001-02, as reflected in their financial statements/records, the institutions incurred substantial expenditure in purchasing library books and periodicals, which are shown in Table 10 below.

Note 11: *The Accounting Framework of the Accounting Standards sets out the concepts that underlie the preparation and presentation of financial statements under accounting principles generally accepted in Hong Kong.*

Table 10

**Institutions' expenditure on
library books and periodicals in 2001-02**

| Institution | Expenditure on library books and periodicals |
|--------------------|---|
| | (\$ million) |
| HKU | 75.1 |
| CityU | 38.1 |
| HKUST | 27.2 |
| HKIEd | 16.5 |
| HKBU | 16.2 |
| LU | 5.7 |
| CUHK | (Note) |
| PolyU | (Note) |

Source: Institutions' financial statements/records

Note: The institutions did not separately show their expenditure on library books and periodicals in their financial statements.

4.19 In view of the substantial amounts of expenditure incurred in purchasing library books and periodicals, Audit considers that it is desirable for the institutions to treat them as assets in compiling their financial statements. This accounting treatment is generally adopted by universities in advanced countries.

**Accounting treatment and
presentation of consolidated financial statements**

4.20 *HKSSAP on presentation of consolidated financial statements.* HKSSAP 32 states that a parent entity that has one or more subsidiaries should present consolidated financial statements, in which intra-group balances and intra-group transactions and resulting unrealised profits should be eliminated in full (cf. para. 4.13(a) above).

4.21 *Institutions did not prepare consolidated financial statements.* Regarding paragraph 4.13(a) above, in their financial statements for the year ended 30 June 2002, of the eight institutions, six stated that they had a number of subsidiaries and associates, as shown in Table 11 below.

Table 11

**Number of institutions' subsidiaries and associates as shown
in institutions' financial statements for the year ended 30 June 2002**

| Institution | Number of subsidiaries | Number of associates |
|--------------------|-----------------------------------|---------------------------------|
| CityU | 13 | – |
| HKU (Note 1) | 8 | – |
| HKBU | 7 | – |
| HKUST | 3 | – |
| PolyU | 2 | 1 |
| HKIEd (Note 2) | 1 | – |
| LU | – | – |
| CUHK | – | – |

Source: Institutions' records

Note 1: Three of the HKU's subsidiaries were companies limited by guarantee.

Note 2: The HKIEd's subsidiary was a company limited by guarantee.

4.22 In the CUHK's financial statements for the year ended 30 June 2002, the CUHK did not make disclosures of its subsidiary or associate. However, in December 2002, in response to Audit's enquiries, the CUHK provided Audit with the financial statements of its subsidiary which was limited by guarantee. Therefore, of the eight institutions, except the LU, seven had subsidiaries and/or associates as at 30 June 2002.

4.23 ***Institutions' comments on presentation of consolidated financial statements.*** In response to Audit's observations in paragraphs 4.13(a), 4.20 to 4.22 above, CityU, the HKIEd and the HKUST stated that:

- (a) in view of the immateriality of the transactions of the subsidiaries involved, consolidated financial statements were not prepared. This was in line with the immateriality provisions in the HKSSAPs; and
- (b) the institutions had made disclosure in their financial statements that no consolidated financial statements were prepared in view of the immateriality of the amounts involved.

4.24 In response to Audit's observations in paragraph 4.22 above, the CUHK stated that compared to the account of the CUHK, the account of its subsidiary in question was not material. Therefore, no disclosure of the account of its subsidiary was made in the CUHK's financial statements. This was a generally accepted accounting practice.

4.25 **In order to enhance public accountability, Audit considers that it is desirable for the institutions to, as far as possible, prepare consolidated financial statements to present their financial affairs and those of their subsidiaries and associates together. This practice is in line with the practices adopted by universities in advanced countries.**

4.26 ***The HKU and its subsidiaries.*** In its financial report for the year ended 30 June 2002, the HKU stated that:

- (a) except for the HKU School of Professional and Continuing Education (HKU-SPACE), the HKU had not consolidated its subsidiary companies due to their transactions not being material in the context of the HKU;
- (b) the whole year results and the assets and liabilities of the HKU-SPACE at the year end were included in the financial statements of the HKU; and
- (c) due to the special UGC funding nature of the HKU, no transactions made between the HKU and the HKU-SPACE had been eliminated from the financial statements.

4.27 ***Audit comments on the HKU and its subsidiaries.*** The HKU-SPACE was incorporated in October 1999 under the Companies Ordinance (Cap.32) and is limited by guarantee to take over

and manage the assets, responsibilities and mission of the HKU's former School of Professional and Continuing Education. The HKU-SPACE is exempted from using the word "Limited" under Section 21 of the Companies Ordinance. As required by the Companies Ordinance, the HKU-SPACE prepares its annual financial statements which are audited by certified public accountants under the Professional Accountants Ordinance (Cap. 50).

4.28 As required under Sections 5 and 6 of Statute XXI of the University of Hong Kong Ordinance, the HKU needs to prepare a balance sheet and an income and expenditure account, which are to be audited, for submission to the HKU Council every year. **Therefore, Audit considers that it is undesirable for the HKU to include the financial results, and the assets and liabilities of the HKU-SPACE in its financial statements. This is because the HKU and the HKU-SPACE are separate legal entities which are individually required under different Ordinances to prepare their own financial statements. Therefore, there is a need for the HKU to prepare a set of financial statements of its own every year (without including the financial data of another legal entity) which will only show the HKU's financial performance.** Furthermore, as transactions made between the HKU and the HKU-SPACE had not been eliminated from the HKU's financial statements for the year ended 30 June 2002, the financial statements did not meet the requirements under HKSSAP 32 on the preparation of consolidated financial statements.

Accounting treatment of related-party transactions

4.29 ***HKSSAP on related-party transactions.*** HKSSAP 20 states that if there have been transactions between related parties, the reporting enterprise should disclose the nature of the related-party relationships as well as the types of transactions and the elements of the transactions necessary for an understanding of the financial statements. Parties are considered related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions (cf. para. 4.13(b) above).

4.30 ***Institutions did not disclose related-party transactions.*** Regarding paragraph 4.13(b) above, at the request of Audit, the seven institutions, which had subsidiaries and/or associates, provided Audit with the recent financial statements of their subsidiaries and associates. Audit conducted an examination of the financial statements of the subsidiaries and associates of the seven institutions for the years ended 30 June 2001 and 30 June 2002. In the examination, Audit noted that some of the subsidiaries and associates had made disclosures in their financial statements of transactions with their parent institutions. Some examples of the related-party transactions are shown in Table 12 below.

Table 12

**Examples of related-party transactions
disclosed in institutions' subsidiaries' financial statements
for the year ended 30 June 2001 or 30 June 2002**

| Institution | Related-party transaction disclosed in subsidiary's financial statements |
|--------------------|--|
| CityU | In the consolidated balance sheet of a subsidiary of CityU for the year ended 30 June 2001, it showed that the group owed \$1,240,377 to CityU with no fixed term of repayment (Note 1). |
| HKBU | As at 30 June 2002, a subsidiary owed \$3,097,815 to the HKBU, which was interest-free and had no fixed term of repayment. |
| CUHK | As at 30 June 2002, the CUHK had made capital donations amounting to \$4,082,231 to a subsidiary. |
| HKIED | As at 31 August 2001, a subsidiary owed \$696,199 to the HKIED, which was interest-free and had no fixed term of repayment (Note 2). |
| PolyU | In the consolidated balance sheet of a subsidiary of the PolyU for the year ended 30 June 2002, it showed that the group owed \$890,816 to the PolyU with no fixed term of repayment. |
| HKUST | As at 30 June 2002, a subsidiary owed \$6,514,381 to the HKUST, which was interest-free and repayable on demand. |
| HKU | In a subsidiary's financial statements for the year ended 30 June 2002, it showed that there was an unsecured and interest-free loan of \$5,200,000 from the HKU. The loan was repayable over eight years. |

Source: Institutions' records

Note 1: Up to the time of finalising this report in late December 2002, the audited financial statements of the subsidiary for the year ended 30 June 2002 was not available for Audit's examination.

Note 2: The financial year of the HKIED's subsidiary was from 1 September to 31 August.

4.31 In response to Table 12 in paragraph 4.30 above:

- (a) the **HKBU** stated that the amount of \$3,097,815 owed by its subsidiary had been written off in the books of the HKBU in 1997-98 against private fund income;
- (b) the **CUHK** stated that the capital donations of \$4,082,231 was the capital fund account balance of its subsidiary, which was a holding company carrying investment in subsidiary and associated companies related to technology transfers from the CUHK to the commercial sector. The amount represented capital injection from the CUHK to the subsidiary, which was derived from licence income arising out of such technology transfers. The CUHK stated that the capital fund would be channeled to viable and worthy investment projects when the right opportunities arose;
- (c) the **HKIEd** stated that its subsidiary was established to oversee the operation of an early childhood learning centre and a primary school; and
- (d) the **HKU** stated that the interest-free loan of \$5,200,000 was related to the interim funding provided by the HKU to enable the subsidiary to maintain its non-commercial but academic commitments to provide executive training and consultancy services to the industrial and commercial sector. Such funding was made on an understanding at the time that a pledged donation of \$30 million for supporting the operations of the subsidiary would be honoured by a prominent donor. The donor had made a total payment of \$21 million during the period from 1990-91 to 2001-02 and intended to continue with the pledged donation. The schedule of these payments was being negotiated at this point in time. It was expected that with the donor's pledged donation there should be no difficulty in repaying the loan. In addition, actions had been taken by the subsidiary to restructure its activities in order to increase income and reduce its operating costs, as well as to repay the outstanding loan to the HKU. A total of \$1.3 million had been repaid by the subsidiary to the HKU since 2001-02.

4.32 *Institutions' comments on related-party transactions.* In response to Audit's observations in paragraphs 4.13(b), 4.29 and 4.30 above, CityU, the HKIEd and the HKUST stated that, because the amounts due from the institutions' subsidiaries were immaterial, they were not disclosed in the institutions' financial statements. The institutions considered that this was in line with the immateriality provisions in the HKSSAPs.

4.33 **In order to enhance public accountability, Audit considers that the institutions should make disclosure of related-party transactions with their subsidiaries and associates in their financial statements. This practice is in line with the practices adopted by universities in advanced countries.**

Need to comply with the HKSSAPs

4.34 ***HKSA's recommendations.*** According to the HKSA:

- (a) financial statements are frequently described as showing a true and fair view of (or as presenting fairly) the financial position, performance and cash flows of an enterprise;
- (b) the application of appropriate accounting standards normally results in financial statements that convey what is generally understood as a true and fair view of such information; and
- (c) financial statements prepared on the accrual basis of accounting provide the type of information about past transactions that is most useful to users in making economic decisions.

4.35 **Audit considers that, in order that the institutions' financial statements show a true and fair view of their financial affairs, the institutions' financial statements need to comply with the HKSSAPs.**

4.36 ***Showing full costs of operation.*** Audit considers that compliance with the HKSSAPs will help the institutions show the full costs of operation in a financial period. For example, the adoption of depreciation accounting will help the institutions allocate the costs of the assets acquired throughout their useful lives, which matches the costs of operation with the service output in a financial period. This will better reflect the amount of resources consumed in the period.

Comparison of institutions' financial statements with those of overseas universities

4.37 ***Compliance with SSAPs.*** Audit conducted a research on the financial statements of some universities in advanced countries. In the research, Audit selected the largest university (in terms of student population) in Australia, Canada, New Zealand, UK and USA (see para. 3.13 above) for examination. Audit noted that the five selected universities complied with the accounting standards of their countries in presenting their financial statements. However, as described in paragraphs 4.12 to 4.33 above, the eight institutions did not comply with some of the HKSSAPs. **Audit considers that there is a need for the institutions to follow the practice of their counterparts in advanced countries in preparing their financial statements.**

4.38 ***Basis of presentation of financial statements.*** Audit’s research found that the five selected universities stated that their financial statements had been prepared in accordance with the generally accepted accounting practices (i.e. accounting standards) of their countries. In addition, the selected university in the UK also complied with the UK Statement of Recommended Practice on Accounting in Further and Higher Education Institutions in preparing its financial statements.

4.39 However, Audit noted that the eight institutions had adopted different bases of presentation of their financial statements. In their financial statements for the year ended 30 June 2002, the institutions stated that their financial statements had been prepared in accordance with:

- the accounting policies generally adopted by higher educational (or UGC-funded) institutions in Hong Kong (CityU, HKBU, CUHK, HKIEd, PolyU, HKUST and HKU); or
- the accounting policies generally adopted by higher educational institutions in Hong Kong as expressed in the SORP for the institutions (LU).

4.40 In February 2003, in response to Audit’s observations in paragraphs 4.37 to 4.39 above, CityU stated that:

- (a) the accounting standards in the quoted five overseas countries contained an “applicability” clause which identified those statements which, with appropriate amendments, should be applied by all, or particular classes of, reporting entities in the public sector. Separate series of private and public-sector statements of accounting standards were also issued in some countries. However, there were no similar arrangements in Hong Kong; and
- (b) the revision of HKSSAP 17 for property, plant and equipment in April 2001, and the issue of HKSSAP 35 for accounting for government grants and disclosure of government assistance in March 2002 were useful in providing some guidance for public-sector institutions in the preparation and presentation of their financial reports.

4.41 **Audit considers that the users (both local and overseas) of the financial statements of the institutions have a legitimate expectation that the financial statements are presented in accordance with the generally accepted accounting principles. It would be desirable for the institutions, which are the highest academic institutions for advancing accounting knowledge, to adhere to the international best practices on the preparation of financial statements.**

Comparison of institutions' auditors' reports with those of overseas universities

4.42 Audit's research of the auditors' reports on the financial statements of the five selected universities (see para. 3.13 above) revealed that their auditors generally expressed the opinion that the financial statements presented fairly (or gave a true and fair view of) the financial position and the results of operations of the universities in accordance with:

- (a) the generally accepted accounting principles or accounting standards (Australia, Canada, New Zealand and USA); and
- (b) the Statement of Recommended Practice on Accounting in Further and Higher Education Institutions (UK).

The auditors' opinions on the above universities' financial statements are summarised in Appendix E.

4.43 Audit's examination of the auditors' reports on the institutions' financial statements for the year ended 30 June 2002 revealed that auditors' opinions on the institutions' financial statements are similar, as follows:

- (a) for CityU, the HKBU, the CUHK, the HKIEd, the PolyU and the HKUST, the auditors stated that, in their opinion, the financial statements had been properly prepared in accordance with the accounting policies generally adopted by higher-education institutions in Hong Kong and, on that basis, gave a true and fair view of the state of the institution's affairs as at 30 June 2002 and of its results and cash flows for the year then ended;
- (b) for the LU, the auditors stated that, in their opinion, the financial statements gave a true and fair view of the state of affairs of the LU as at 30 June 2002 and of its income and expenditure and cash flows for the year then ended and had been properly prepared in accordance with the Lingnan University Ordinance; and
- (c) for the HKU, the auditors stated that, in their opinion, the financial statements, which had been prepared in accordance with the accounting policies generally adopted by the UGC-funded institutions in Hong Kong, gave a true and fair view of the state of the University's affairs as at 30 June 2002 and of its surplus and cash flows for the year then ended.

4.44 **Audit considers that the institutions' financial statements should be presented in a way that they are on a par with internationally accepted accounting practices for higher-education institutions. This will enable users of the financial statements to compare the financial performance of the institutions with that of overseas universities. Audit also considers that there is a need for the institutions to revise the SORP so that it will comply with the HKSSAPs. The institutions also need to comply with the SORP in preparing their financial statements (see para. 4.13 above).**

Institutions' recent review of SORP

4.45 In early 2002, a Task Force on Review of SORP was formed comprising members from the eight institutions. The terms of reference of the Task Force was to review and revise the SORP for the preparation of financial statements of the institutions. The objective was to ensure that the financial statements will give a true and fair view of the financial affairs of the institutions. At its first meeting held in March 2002, members of the Task Force agreed that the review would take into account the following materials:

- (a) the HKSA's HKSSAPs;
- (b) the UK Statement of Recommended Practice on Accounting in Further and Higher Education Institutions;
- (c) Accounting Standards and publications issued by the Financial Accounting Standards Board;
- (d) International Accounting Standards; and
- (e) UGC's Guidance Notes.

4.46 The main areas to be covered by the review of the Task Force included the following:

- (a) leave provisions;
- (b) reserves;
- (c) valuation of investment portfolios;

- (d) capital projects;
- (e) consolidation of accounts;
- (f) fixed assets and depreciation;
- (g) commitments; and
- (h) disclosures and presentation of financial statements.

4.47 **Audit noted that there was a delay in conducting the review of the SORP. According to the SORP, the review should have been conducted by the institutions in mid-1999 (see paras. 4.7(d) and 4.10 above). Audit considers that the institutions need to expedite action to revise the SORP, taking into account Audit's observations stated in paragraphs 4.3 to 4.44 above. The revised SORP should comply with the HKSSAPs and international good practices. Furthermore, to ensure that the SORP complies with the HKSSAPs, the HKSA should be consulted and requested to endorse it.**

Audit recommendations on financial reporting of institutions

4.48 **In order to enhance the accountability of the institutions in their use of public funds, Audit has *recommended* that the Secretary-General, University Grants Committee should:**

- (a) **request the HKU to prepare a separate set of its own financial statements, which will not include the financial data of the HKU-SPACE, which is another legal entity (see para. 4.28 above);**
- (b) **collaborate with the eight institutions and the HKSA to develop a set of revised SORP for compiling the institutions' financial statements. The SORP should comply with the HKSSAPs (see para. 4.44 above); and**
- (c) **request the eight institutions to strictly comply with the revised SORP in preparing their financial statements (see para. 4.44 above).**

Response from the Administration and the institutions

4.49 The **Secretary for Education and Manpower** agrees with Audit that there is scope for improvement in the institutions' financial statements, and that the HKSSAPs and international practices should be the necessary references for the current review of the SORP undertaken by the institutions.

4.50 The **Secretary-General, University Grants Committee** has said that:

- (a) the UGC notes that the Task Force commissioned by the finance directors of the institutions has been reviewing the SORP for the sector, which will take into account the need for compliance with the generally acceptable accounting practices as set out in the HKSSAPs; and
- (b) the UGC will work together with the institutions to ensure that their financial statements will comply with the generally acceptable accounting practices and the revised SORP as appropriate.

4.51 The **Heads of Institutions** have said that:

- (a) all the institutions are required by law to produce statements of income and expenditure for each financial year and of their assets and liabilities as at the last day thereof, and have the same audited by auditors. Throughout the past, all the institutions have appointed auditors, who are certified by the HKSA, to have their annual published financial statements audited. All such audited financial statements prepared by the institutions were certified by their auditors to have presented a true and fair view of the state of their financial affairs for the financial year concerned. To date, the auditors' report has consistently expressed an unqualified opinion in this respect;
- (b) the existing accounting practices adopted by the institutions have evolved over time from the accounting practices of the Government and the funding rules prescribed by the then University and Polytechnic Grants Committee back in the 1970s. The major users of the financial statements were the University and Polytechnic Grants Committee, the funding bodies and the governing bodies of the institutions. Nonetheless, all cost-benefit analyses behind major decisions of the institutions were made on management account data on which the accounting practices in question have little or no relevancy at all;

- (c) in recognition of the development in accounting over the years and the need for accountability of public funds, the institutions have taken initiatives to develop a set of recommended uniform accounting practice for the UGC-funded sector in 1992-93. The recommended accounting practices embodied in the SORP were adopted for use by all the institutions, greatly enhancing the comparability of the financial statements among the institutions;
- (d) the recommendations in the SORP took into account, inter alia, the funding rules of the UGC, the accounting practices in the past, the practice in the UK and USA in the early 1990s and the needs and the preparedness for change for the major users of the financial statements of the institutions at that time. On the premise that the process should be evolutionary, the focus of the 1992-93 exercise was more on harmonisation of practices. The appropriateness and relevancy of the recommended practices must be examined in that context;
- (e) in view of other developments of the institutions taking priority, the review of the SORP was postponed to commence in late 2001. The postponement of the review was timely as a similar SORP revision was completed by the UK higher-education institutions in late 1999 and the HKSA has most recently issued HKSSAP 35 on “Accounting for government grants and disclosure of government assistance” in March 2002. A Task Force was commissioned and worked through the whole of 2002. A report was produced and a revised SORP was submitted to the finance directors of the institutions in January 2003. Comments from the auditors of the institutions, the HKSA, the UGC Secretariat and the management of the institutions will be sought and incorporated into the SORP, where appropriate, before adoption for implementation; and
- (f) they believe that the recommended revised SORP will have addressed all the concerns raised by Audit on financial reporting of the institutions.

4.52 **The President, City University of Hong Kong** has said that:

- (a) examination of the existing accounting practices adopted by most UGC-funded institutions needs to be made with regard to the historical development of the institutions and the UGC funding system;
- (b) regarding the recognition of expenses at the time of placing orders instead of receipt of goods or services, the adoption of an accounting practice which deviates from the relevant HKSSAP is acceptable as long as the true and fair value of the financial statements is not adversely affected;

- (c) regarding the writing off of the expenditures on properties, plants and equipment in the year of purchase, CityU has made disclosure of its accounting policy on dealing with these items in its financial statements; and
- (d) regarding the writing off of library books and periodicals in the year of purchase, this accounting treatment represents a more appropriate balance between costs and benefits.

4.53 **The President, The Hong Kong Polytechnic University and the Vice-Chancellor, The University of Hong Kong** have said that:

- (a) the annual audited accounts have been historically referred to by the UGC for assessing whether any unspent balance at the end of a triennium is required to be refunded by the institutions to the UGC. It was for this reason that the institutions could not adopt certain HKSSAPs, such as those on depreciation of fixed assets, the recognition of expenses based on goods/services received instead of orders placed, etc.; and
- (b) the PolyU and the HKU will consider to adopting all HKSSAPs if the UGC is agreeable to change its funding model and surplus assessment method for the institutions.

4.54 Regarding Audit's recommendation on requesting the HKU to prepare a separate set of its own financial statements, the **Vice-Chancellor, The University of Hong Kong** has said that:

- (a) in view of the income of the HKU-SPACE accounted for 7.6% of the consolidated income of the HKU as a whole in 2001-02, the inclusion of the financial results and assets and liabilities of the HKU-SPACE in the HKU's accounts is desirable, since this would enable the Council to better understand the HKU's overall financial positions. The "University" as defined in The University of Hong Kong Ordinance does not exclude the HKU's subsidiary companies, and these companies are all accountable to the Council. The preparation of the financial statements in the current format therefore does comply with The University of Hong Kong Ordinance and its statutes; and
- (b) unlike private corporations, the HKU did not prepare a set of financial statements for the University per se because of the low value expected to be contributed by this process. However, in order to comply with both the relevant HKSSAPs and facilitate the UGC in assessing the funding positions of the HKU, two sets of financial statements for the University per se and the HKU as a whole will be prepared when the revised SORP is implemented by no later than 2003-04, if this arrangement is approved by the relevant parties, namely the HKU Council, the UGC and the HKSA.

PART 5: PERFORMANCE REPORTING OF INSTITUTIONS

5.1 This PART examines the efficiency and effectiveness of the institutions' arrangements for compiling and reporting their performance information to the public, and the conduct of opinion surveys among the eight institutions.

Pledges for greater openness and accountability of higher-education sector

Government's pledge

5.2 In a speech in the Legislative Council on 26 June 2002, the then Secretary for Education and Manpower said that:

- (a) the improvements and reform of higher education must be based on quality intake, and universities must improve their governance and quality assurance, seek to serve society and build up better links with the real working world; and
- (b) while enjoying autonomy and freedom, higher-education institutions must be accountable to society and members of the public, so as to strike a balance between rights and obligations.

UGC's pledge

5.3 In its "*Triennial Report 1998-2001*", the UGC said that, during that triennium, the UGC:

- responded to the community's increasing demands for greater openness and accountability by taking a more active role in promoting public understanding about the higher-education sector, its achievements and the role of the UGC; and
- took steps in the reporting triennium to reach out to its stakeholders through different channels.

Audit observations on performance reporting of institutions

Annual performance information collected and disclosed by UGC and institutions

5.4 *Annual UGC common data collection exercises.* Every year, the eight institutions are required to compile data based on the Common Data Collection Format (CDCF) for submission to

the UGC. The CDCF is designed to collect statistical data from the institutions in a common, computer-processable form for use by the UGC and the Research Grants Council (Note 12). The primary purpose of collecting the data is to facilitate planning and monitoring of the higher-education sector by the UGC. A list of data for submission by the institutions to the UGC every year (in CDCF format) is shown in Appendix F.

5.5 Disclosure of institutions' performance information in UGC's annual reports and website. Every year, the UGC publishes a report named "*Facts and Figures*" which includes information and statistics of the UGC and the eight institutions. Most of such information and statistics are also available on the UGC's website. The following is the major information and statistics included in the UGC's "*Facts and Figures*" and website:

- (a) in respect of the eight institutions taken as a whole:
 - (i) full-time equivalent (FTE) student enrolment numbers of sub-degree programmes, undergraduate programmes, taught postgraduate programmes and research postgraduate programmes;
 - (ii) first-year-first-degree places;
 - (iii) percentage of people in relevant age group (age 17 to 20) provided with first-year-first-degree places;
 - (iv) graduate numbers of sub-degree programmes, undergraduate programmes, taught postgraduate programmes and research postgraduate programmes;
 - (v) amount of approved recurrent grants, earmarked grants (Note 13) and capital grants made to institutions;
 - (vi) total amount of approved grants as a percentage of total government expenditure;

Note 12: *The Research Grants Council is an advisory body within the organisational structure of the UGC on research matters.*

Note 13: *The earmarked grants are for financing the Home Financing Scheme and other housing-related benefits.*

- (vii) total amount of approved grants as a percentage of total government expenditure on education; and
 - (viii) the approved salary scales of academic staff in the eight institutions; and
- (b) in respect of each of the eight institutions:
- (i) FTE student enrolment numbers of sub-degree programmes, undergraduate programmes, taught postgraduate programmes and research postgraduate programmes;
 - (ii) student enrolment numbers by academic programme category (APC) of UGC-funded programmes;
 - (iii) graduate numbers by APC of UGC-funded programmes;
 - (iv) FTE departmental academic and research staff numbers (in each of the staff grade) with salary wholly funded from general funds; and
 - (v) approved grants for the triennium.

5.6 ***Disclosure of institutions' performance information in their annual reports and websites.*** In late December 2002, Audit reviewed the information in the websites of the eight institutions. Audit's examination revealed that all the eight institutions had uploaded their annual reports onto their websites to facilitate the dissemination of the institutions' performance information to the public.

5.7 Audit's examination of the 2000-01 annual reports and websites of the eight institutions revealed that some of the institutions had included in their annual reports and/or websites some performance information as shown in paragraph 5.5(b) above. For example, at the time of Audit's examination of the institutions' annual reports and websites in late December 2002, Audit noted that the HKBU, the LU, the CUHK, the HKIEd, the PolyU, the HKUST and the HKU had included in their annual reports/websites information on the annual salaries of their graduates.

5.8 ***Some significant performance information collected by the UGC but not disclosed.*** A comparison of the data collected by the UGC every year (see Appendix F) and the data disclosed by the UGC and the institutions in their annual reports and websites revealed that the UGC and the

institutions only disclosed some of the institutions' performance information compiled in the annual CDCF exercises. At the time of Audit's examination in late December 2002, Audit noted that the following significant performance information had been collected but was not disclosed by the UGC and the eight institutions to the public:

- (a) student retention rates;
- (b) admission qualifications of programmes;
- (c) language examination results of newly admitted students;
- (d) student admission ratios; and
- (e) student unit costs.

5.9 ***Audit observations.*** Audit considers that the performance information compiled by the institutions for submission to the UGC is very useful to the stakeholders and its disclosure to the public will help enhance the institutions' public accountability (see para. 5.2(b) above). **Therefore, the UGC and the institutions should as far as possible disclose all the relevant and useful performance information to the public.**

UGC's study on performance indicators for higher education in mid-1999

5.10 In July 1999, the Secretary for Education and Manpower invited the UGC to explore the possibility of further improving its funding methodology by making it more transparent, while at the same time increasing the extent to which it rewarded performance and enhanced quality.

5.11 In mid-1999, the UGC engaged a researcher of one of the institutions to conduct a study on performance indicators used by overseas higher-education institutions and the ways by which the indicators were applied in relation to funding. In his report of August 1999 submitted to the UGC, the researcher stated that:

Merits of performance indicators for higher-education institutions

- (a) performance indicators could provide understandable information to both insiders and outsiders of higher education for improvement and accountability. Better information in

the hands of consumers, including parents, students and industrial leaders, would bring about better choice, effectiveness and efficiency in higher education;

- (b) the provision of better information to the public would help strengthen the sense of responsibility of and competition among academic staff and departments;
- (c) comparison of performance could move to an international level. The performance indicators of different institutions such as unit costs, time to complete a degree course, retention rates, graduation rates, graduates' employment patterns, research publications, citing of research work, relevance of research results for trade and industry, etc. could be compared across regions and nations. Higher-education institutions and systems, which were striving to reach world-class quality and status, had to assess themselves with performance indicators that were valid in different countries;
- (d) in respect of a system, a programme or an institution, performance indicators could be used for:
 - (i) monitoring the development;
 - (ii) evaluating the degree of goal attainment;
 - (iii) facilitating the communication among stakeholders on performance;
 - (iv) providing information for policy making, planning and implementation; and
 - (v) allocating manpower and funding resources;

Challenges of performance indicators for higher-education institutions

- (e) universities are different in context and reputation, hence simple comparisons among them based on performance indicators might not be acceptable by some scholars;
- (f) there was no assurance of the validity and reliability of the performance data compiled by institutions;

Use of performance indicators for ranking and resource allocation

- (g) many overseas newspapers and magazines had used performance indicators for ranking colleges and universities, e.g. those in the Mainland, USA, etc.;
- (h) some governments had taken initiatives to rank colleges and universities based on performance indicators, e.g. those in Australia, UK, etc.;
- (i) most governments in developed countries had applied performance indicators for resource allocation partly or mainly for research work, e.g. those in Australia, New Zealand, UK, USA, etc.; and

Performance indicators adopted by overseas higher-education institutions

- (j) higher-education institutions in the UK generally adopted 16 performance indicators (see Appendix G).

5.12 As stated in paragraph 5.11 above, the UGC's researcher found that there were merits for the institutions to compile useful performance indicators. The significant merits of useful performance indicators are that they would:

- (a) bring about better choice, effectiveness and efficiency in higher education (see para. 5.11(a) above);
- (b) strengthen the sense of responsibility of and competition among academic staff and departments (see para. 5.11(b) above);
- (c) help the institutions compare their performance with their overseas counterparts (see para. 5.11(c) above); and
- (d) facilitate the monitoring and evaluation of the institutions' development and performance (see para. 5.11(d) above).

UGC's initiatives on performance information in 2000

5.13 *UGC's request for performance information in May 2000.* Based on a detailed examination of a wide range of possible performance indicators, which were drawn from international experiences and practices, the UGC identified a list of performance indicators (see Appendix H) which were generally relevant in the Hong Kong context and appropriate to be included in a menu of performance indicators for the institutions. In May 2000, the UGC wrote to the eight institutions and invited them to examine the performance indicators and to present information on those that they considered relevant to their particular circumstances. In its letter, the UGC stated that:

- (a) it realised that many aspects of institutions' performance could not be captured by these or other list of performance indicators, and that the institutions had different roles and missions and were at different stages of development;
- (b) the list of performance indicators was not intended to be prescriptive or exhaustive, and institutions were invited to present additional indicators or information that they considered relevant to their circumstances as part of their returns;
- (c) the UGC would draw on the information included in institutions' returns in exercising its judgement in the 2001-04 triennial recurrent funding assessment exercise;
- (d) the UGC did not expect that the return of individual institution would necessarily cover all the items stated in the list of proposed performance indicators; and
- (e) the UGC would be interested to know whether institutions would feel that the institutional returns in this exercise should be made public.

5.14 *Institutions' returns on performance information in June 2000.* In response to the UGC's above request for performance information, in June 2000, the eight institutions submitted returns to the UGC. In their returns, the eight institutions provided information in the following areas:

- (a) quality assurance processes, such as student/staff consultations, use of external advisory panels and staff development;

- (b) outcome assessments, such as satisfaction levels of graduates and employers and income of graduates;
- (c) collaboration with other institutions, such as use of research and library facilities by members of other institutions, and share of resources and services with other institutions;
- (d) input measures, such as share of expenditure on information services and academic programmes;
- (e) response to public policy priorities, such as number of students admitted to second or subsequent years and the introduction of self-financing taught-postgraduate programmes; and
- (f) mission-related activities, such as industrial contributions and collaboration, and faculty involvement in public and professional services.

5.15 ***Institutions' comments on UGC's proposed performance indicators.*** In response to the UGC's request for institutions' comments on the UGC's proposed performance indicators, some institutions made some comments, which are summarised below.

- (a) ***CityU:*** supported in principle the use of performance indicators to inform funding but remained mindful of their complexity and limitation;
- (b) ***HKBU:*** suggested that there should be consultation before submission of data on the performance indicators;
- (c) ***LU:*** had strong support of placing emphasis on the mission-related performance indicators. In general, the LU agreed with the UGC's suggested performance indicators except those related to income level of graduates, collaboration with other institutions, and share of expenditure on information services and academic programmes;
- (d) ***CUHK:*** fully endorsed the importance of quality teaching and learning, but would like to stress that there were areas of an institution's performance that could not be readily and adequately measured by performance indicators. For this reason, the emphasis of the funding exercise should be on the assessment of an institution's teaching and learning quality process;

- (e) **HKUST:** fully supported the concept that institutional mission, and performance in achieving that mission, should be factors in decisions on funding. There should be guidelines for drawing up each of the indicators to ensure consistency and comparability in reporting; and
- (f) **HKU:** was supportive of performance indicators. The feasibility and desirability of using a wide range of indicators, as well as the relevance, reliability and validity of some of the indicators which had been proposed should receive more careful consideration, especially in the Hong Kong context. The UGC might think it prudent to consider setting up a task force to study the issue in depth.

The **HKIEd** and the **PolyU** did not make specific comments on the UGC's proposed performance indicators.

5.16 **Institutions' views on disclosing their performance information to the public.** In their returns to the UGC, some institutions expressed views on making public their performance information included in their returns to the UGC (see para. 5.13(e) above). **CityU** and the **LU** said that they had no objection to the UGC's proposal. The **HKBU**, the **CUHK** and the **HKUST** made no specific comments on the issue. The views of the other three institutions were as follows:

- (a) **HKIEd:** in view of the sensitivity of some of the information supplied, the disclosure of the information to the public would require further consideration;
- (b) **PolyU:** had no objection in principle on the understanding that similar information to be provided by other institutions were also released to the public at the same time; and
- (c) **HKU:** had no objection to the information being made available to the public, save for that which contained comparative data involving other tertiary institutions.

5.17 **Audit observations.** Audit considers that the UGC's initiatives in 2000 to request the institutions to supply additional performance information was a positive step forward in performing one of the UGC's functions to monitor the efficiency and effectiveness of the institutions' activities (see para. 1.4(d) above). **In order to enhance public accountability, Audit considers that the performance information should be made public.**

Performance information disclosed by overseas universities

5.18 Audit conducted a research on overseas universities' disclosure of performance information in their annual reports and websites. In the research, Audit selected the largest university (in terms of student population) in Australia, Canada, New Zealand, UK and USA for examination (see para. 3.13 above). Audit noted that, in all the five universities selected, they had uploaded their annual reports onto their websites. Audit also noted that the five selected universities had included in their annual reports a variety of useful performance data. The key performance data included in these five universities' websites are summarised in Appendix I.

5.19 It can be seen from Appendix I that overseas universities generally disclose to the public much more performance information than that disclosed by the local institutions. **In Audit's view, the UGC should consider requesting the institutions to adopt the good practices of overseas universities of disclosing the useful performance information of the institutions to the public.**

5.20 In February 2003, in response to Audit's observations in paragraphs 5.18 and 5.19 above, CityU stated that as universities in different countries used different performance indicators (see Appendix I), it would be helpful if Audit could recommend a set of useful performance indicators for use by the institutions. Audit considers that, as the highest academic institutions in Hong Kong, the institutions could conduct research on this subject, making reference to the performance indicators adopted by overseas universities as described in Appendices G and I.

Satisfaction surveys conducted by institutions

5.21 In a speech in the Legislative Council on 26 June 2002, the then Secretary for Education and Manpower said that:

- (a) since 1999-2000, the Government had been conducting annual surveys on employers' satisfaction with university graduates. Generally, about 70% of the employers sampled for survey were satisfied with the performance of their graduate employees;
- (b) about 13% of the employers were very satisfied, while 6% were not satisfied; and
- (c) employers in general were more satisfied with the information technology knowledge, Chinese language standards and work attitude of their graduate employees, but they were most dissatisfied with the graduates' Putonghua, English and analytical power.

5.22 From time to time, the eight institutions conducted opinion surveys of their stakeholders on the effectiveness of their services. The stakeholders included students, parents, teaching and non-teaching staff, graduates, employers, etc. The institutions conducted the surveys either by themselves or by engaging independent firms. The major surveys conducted in the past two years relating to teaching, learning and research activities are shown in Appendix J.

5.23 **Audit considers that satisfaction surveys of stakeholders provide useful information for the institutions to make improvements on their delivery of effective tertiary education. Furthermore, the disclosure of the survey results to the public will help enhance the public accountability of the institutions. In order to enable meaningful comparisons of the stakeholders' levels of satisfaction on different aspects of the delivery of tertiary education among the eight institutions, Audit considers that the eight institutions need to collaborate to conduct the surveys together.** The engagement of one independent firm to conduct common opinion surveys for the eight institutions will ensure the consistency of the survey methodologies and the comparability of the survey results among the eight institutions. Furthermore, this approach is more cost-effective and will lead to cost saving.

Audit recommendations on performance reporting of institutions

5.24 **In order to improve the institutions' disclosure of useful performance information to stakeholders and enhance their public accountability, Audit has *recommended* that the Secretary-General, University Grants Committee should:**

- (a) **based on good overseas practices, discuss and work out with the eight institutions a revised set of clear and quantifiable performance indicators for assessing and reporting the performance of the institutions (see para. 5.11 above);**
- (b) **based on the agreed performance indicators, request the eight institutions to provide the UGC with their annual performance data (see para. 5.17 above);**
- (c) **publish the performance data provided by the eight institutions in the UGC's annual reports (see para. 5.17 above);**
- (d) **upload the institutions' performance data onto the UGC's website (see para. 5.17 above);**

- (e) **collaborate with the eight institutions with a view to jointly engaging an independent firm to conduct common satisfaction surveys of the stakeholders of the institutions (see para. 5.23 above); and**
- (f) **disclose the results of the common satisfaction surveys in the UGC's annual reports and website (see para. 5.23 above).**

Response from the Administration and the institutions

5.25 The **Secretary for Education and Manpower** has said that:

- (a) the UGC has planned, in the context of the Higher Education Review, to enhance the transparency of its monitoring and assessment exercises of the tertiary institutions. The EMB agrees with Audit's recommendations on the performance reporting of the institutions, which are in line with the above objective;
- (b) the EMB agrees that the institutions should disclose performance information to enhance their public accountability. It is necessary for the institutions to be accountable to the public, as bulk of the resources in their budgets come from public funds; and
- (c) the disclosure of performance information would help potential students make their choice of study, facilitate the Government and the UGC in providing funding to reward performance, strengthen stakeholder monitoring and provide useful information to prospective donors and sponsors.

5.26 The **Secretary-General, University Grants Committee** has said that:

- (a) the UGC generally welcomes Audit's recommendations on the performance reporting of the institutions, and agrees in principle the need to enhance transparency of the institutions' performance data;
- (b) the UGC will consider the recommendations to develop a set of quantifiable performance indicators with the institutions and to publish such indicators as appropriate in the context of the forthcoming performance-based funding exercise. However, the point must be made that there is a limit to the utility of common indicators since the institutions differ in their orientation and some important achievements cannot be measured quantitatively.

Performance indicators, if applied mechanically, might distort institutional behaviour and lead to misconceptions;

- (c) to enhance transparency of the institutions' performance, the UGC, with the kind assistance of the Commissioner for Census and Statistics, is conducting a review on the data collection and reporting system; and
- (d) the UGC sees the benefits of the institutions joining hands in conducting common satisfaction surveys of stakeholders, but notes that on an annual basis the EMB is already conducting an opinion survey which covers the employers of graduates.

5.27 **The President, City University of Hong Kong** has said that:

- (a) CityU supports the use of proper measures and indicators to measure quality and performance. CityU believes that reliable measures of performance are the foundation of sound decision-making. CityU's objective is to increase the range and effectiveness of value-added measures of success in education. However, as a university is a large complex organisation with a broad range of objectives, reliable and comprehensive measures of performance are difficult to develop; and
- (b) all performance measures and indicators should have an international reference for comparison purpose, and some performance measures and indicators should also be subject specific. Indicators are also time dependent, as good indicators for today may not be good indicators for tomorrow. Furthermore, good coordination on the survey and data collection is necessary and essential.

5.28 **The President and Vice-Chancellor, Hong Kong Baptist University** has said that the HKBU:

- (a) looks forward to working with the other institutions and the UGC to agree on a set of clear and quantifiable performance indicators for assessing and reporting the performance of the institutions; and
- (b) will consider whether Audit's recommendations on the performance reporting of the institutions are feasible and if so, how to put them into implementation.

5.29 **The President, The Hong Kong Institute of Education** has said that:

- (a) the HKIEd welcomes the sharing of performance data on the UGC website for public information, provided that the data have been collected based on clear and common definitions; and
- (b) the HKIEd also welcomes the opportunity to discuss with the other institutions to arrive at a common set of clear and quantifiable performance indicators for assessing and reporting the performance of an institution. However, as each institution carries a distinct mission, any performance assessment must be made only after giving due consideration to its mission. Moreover, the HKIEd would like to caution against over-relying on quantitative indicators, which are often too simplistic for measuring educational outcomes. It is common for such indicators to be quoted out of context and being misinterpreted.

5.30 **The President, The Hong Kong Polytechnic University** has said that:

- (a) having developed and implemented some performance indicators as part of its quality assurance framework, the PolyU is pleased to discuss and develop with the UGC and other institutions a refined set of clear and quantifiable performance indicators for assessing and reporting the performance of the institutions; and
- (b) the PolyU will continue to provide the UGC with annual performance data on the agreed performance indicators, and support the upload of such onto the UGC's website. However, being an independent and autonomous institution, the PolyU considers it appropriate to develop and implement its own performance indicators in addition to those identified for uniform application among the institutions in Hong Kong. Furthermore, the PolyU also considers it appropriate to conduct independent surveys on these additional performance indicators in addition to the collaborative common satisfaction surveys, whenever necessary.

5.31 **The President, The Hong Kong University of Science and Technology** has said that:

- (a) the HKUST fully supports the concept that institutional mission, and performance in achieving that mission, should be factors in decisions on funding;

- (b) the HKUST supports the need for guidelines for drawing up each of the performance indicators to ensure consistency and comparability in reporting; and
- (c) the HKUST sees no difficulty of principle in adopting Audit's recommendations on performance reporting that bear upon the institutions.

5.32 **The Vice-Chancellor, The University of Hong Kong** has said that:

- (a) the HKU is a strong supporter, and indeed advocate, of transparency and openness. The HKU is keen to provide the general public and stakeholders with the performance measures that are deemed appropriate, which in any case are facts of life in the higher-education systems in the USA, UK, Canada, Australia, etc., and especially if all other institutions are also happy to do so. For instance, the HKU has previously urged the UGC to make available the full results of the Research Assessment Exercise;
- (b) the HKU stands ready to work with the UGC and other institutions in drawing up and producing a list of performance indicators to inform the community on the HKU's performances. The University in fact submitted two very detailed papers to the UGC in 2000 giving its views and suggestions on performance indicators; and
- (c) regarding Audit's recommendation on engaging an independent firm to conduct common satisfaction surveys and disclosing the results in the UGC's annual reports and website, the HKU is of the view that the idea should be supported, but details and parameters must be very carefully worked out and agreed upon.

THE UNIVERSITY OF HONG KONG

General statement on the value for money audit reports

The Government of the HKSAR has recognised the importance of investing in education, and this has to be a long term commitment as far as Hong Kong's future is concerned. This was articulated by the Chief Executive in his Policy Address in October 2001,

‘... one of the Government's most fundamental tasks is to make significant investments in education to prepare each of us for the advent of the knowledge-based economy’.

A Value for Money (VFM) audit, which is designed to look at the returns for such investments, is by its very nature and the methodology it employs, a unidimensional process. Such audits always beg a fundamental question — by what parameters has ‘value’ been judged? A VFM audit is essentially an analysis of costs, that seeks external benchmarks in making comparisons and judgments. Such comparisons must be valid and appropriate in their application to the specific circumstances of any particular VFM audit if they can be considered well-founded.

Although The University of Hong Kong (HKU) accepts that a VFM audit is a mechanism of addressing issues of cost-effectiveness, it questions whether it should be regarded as a basis for policy decisions that can well have far-reaching and potentially deleterious effects. Consideration of the recommendations and their impact must be viewed with caution and circumspection in the light of their effects upon an institution of the stature and reputation of HKU, or indeed, any of its sister institutions.

Even from the Audit Report itself, it is clearly apparent that HKU has, by its prior actions, been proactive in pre-empting many of the recommendations. Examples include the governance and management structure, strategic planning efforts and internal resourcing methodology. This point was made repeatedly to the Audit Team during their nine months at the University, but there seems to be no observable effect upon some of the recommendations made. Discrepancies like these between findings and recommendations as they recur in the VFM Report inevitably raise questions about the validity and appropriateness of a number of those recommendations, and these are addressed in the University's detailed response. Although it is entirely reasonable, given the expertise of the members involved, for an Audit Team to derive opinions which stem from a fiscal and financial analysis, to jump from these to policy recommendations which impact upon the whole tertiary education sector in Hong Kong is a hazardous step.

‘Value’ has far greater implications than a study of costs. It just as much embraces the concept of wealth — that property which gives rise to desirable, useful, sought-after qualities. In this regard, the ‘value’ that this university and its sister institutions provide is multifaceted. The University of Hong Kong fulfils its academic mission of discovering and transmitting human knowledge and human understanding at the highest possible level; it continues to produce leaders in society and in the professions for Hong Kong. A great deal of the innovation and creativity of Hong Kong is supported by the intellectual achievements and the societal contributions of HKU graduates. Infrastructure, improvements in data processing and communication as well as improvements in health and quality of life are all sustained through the University’s scientific and technological advances. These are criteria which must be incorporated in any determination of ‘value’.

Hong Kong has set itself upon the path to become a world city in Asia. To achieve such an end, the standing and calibre of its premier universities must be nurtured, and not damaged, as may well be the effect of a number of the VFM recommendations. HKU fully accepts the requirement for transparency and accountability, and relevant recommendations will be acted upon appropriately. However, the University must seek to safeguard those qualities which make it a world-class institution capable of functioning in the fiercely competitive global environment in which it currently has to operate.

The ‘advent’ referred to by the Chief Executive is over; the knowledge-based economy is central to Hong Kong’s future. HKU is poised to play a pivotal role in supporting Hong Kong in the achievement of its aspirations. A narrow and clinical analysis of costs, a task properly executed by auditors, must not lead to circumstances which compromise or debase the true ‘value’ of *this* university to Hong Kong.

The University of Hong Kong

March 4, 2003

**Average attendance rates of external members
of the Councils of the eight institutions for three years**

| Period | Attendance rates of external members of the Councils (Note 1) | | | | | | | |
|---------------------------------------|---|------------|------------|------------|------------|------------|------------|------------------|
| | PolyU | LU | CityU | HKUST | HKBU | HKIEd | HKU | CUHK (Note 2) |
| 2000-01 (7/2000 to 6/2001) | | | | | | | | |
| 1st meeting | 75% | 72% | 61% | 61% | 53% | 81% | 57% | 37% |
| 2nd meeting | 78% | 92% | 88% | 72% | 82% | 56% | 79% | 55% |
| 3rd meeting | 74% | 72% | 60% | 72% | 82% | 44% | 71% | 47% |
| 4th meeting | - | 76% | - | - | 56% | - | 63% | - |
| 5th meeting | - | 68% | - | - | - | - | 59% | - |
| 6th meeting | - | - | - | - | - | - | 44% | - |
| 7th meeting | - | - | - | - | - | - | 46% | - |
| 8th meeting | - | - | - | - | - | - | 46% | - |
| Average | 76% | 76% | 70% | 68% | 68% | 60% | 58% | 46% |
| 2001-02 (7/2001 to 6/2002) | | | | | | | | |
| 1st meeting | 84% | 72% | 83% | 67% | 63% | 56% | 68% | 50% |
| 2nd meeting | 75% | 74% | 79% | 72% | 61% | 63% | 56% | 52% |
| 3rd meeting | 85% | 83% | 61% | 56% | 56% | 75% | 67% | 52% |
| 4th meeting | 85% | 83% | - | - | - | 56% | 61% | 59% |
| 5th meeting | - | 61% | - | - | - | 63% | 57% | - |
| 6th meeting | - | - | - | - | - | 81% | - | - |
| Average | 82% | 75% | 74% | 65% | 60% | 66% | 62% | 53% |
| 2002-03 (7/2002 to 11/2002) | | | | | | | | |
| 1st meeting | 85% | 55% | 53% | 67% | - | 44% | 36% | 53% |
| 2nd meeting | - | - | - | - | - | 75% | 48% | 47% |
| 3rd meeting | - | - | - | - | - | 56% | 68% | - |
| Average | 85% | 55% | 53% | 67% | - | 58% | 51% | 50% |
| Average for three years | 80% | 73% | 69% | 67% | 65% | 63% | 58% | 50% |

Source: Institutions' records

Note 1: Unfilled vacancies of external members were excluded in the computation.

Note 2: Life members were included in the computation.

Number of external members who did not
attend any of the Council meetings held in 2000-01 or 2001-02

| Institution | 2000-01 (July 2000 to June 2001) | 2001-02 (July 2001 to June 2002) |
|-------------|-------------------------------------|-------------------------------------|
| CUHK (Note) | 12 | 10 |
| HKU | 2 | 4 |
| HKBU | - | 2 |
| CityU | - | 1 |
| LU | - | 1 |
| HKIEd | 1 | - |
| PolyU | - | - |
| HKUST | - | - |
| | <u>15</u> | <u>18</u> |

Source: *Institutions' records*

Note: *Life members were included in the computation.*

**Attendance rates of external members of the Courts
 in 2000-01, 2001-02 and 2002-03
 (July to November 2002)**

| Institution | 2000-01 (July 2000 to June 2001) | | | 2001-02 (July 2001 to June 2002) | | | 2002-03 (July to November 2002) | |
|---------------|-------------------------------------|----------------|--------------------------|-------------------------------------|----------------|--------------------------|------------------------------------|--------------------------|
| | 1st meeting | 2nd meeting | Average attendance rates | 1st meeting | 2nd meeting | Average attendance rates | 1st meeting | Average attendance rates |
| HKBU | 16/25 (64%) | 19/24 (79%) | 72% | 13/18 (72%) | 14/19 (74%) | 73% | 14/24 (58%) | 58% |
| LU | - | - | - | 19/29 (66%) | - | 66% | - | - |
| HKUST | 14/39 (36%) | - | 36% | 11/36 (31%) | - | 31% | 14/36 (39%) | 39% |
| HKU (Note) | 19/56 (34%) | - | 34% | 16/59 (27%) | - | 27% | - | - |

Source: Institutions' records

Note: Life members were included in the computation.

**Auditors' opinion on the financial statements
of five universities in advanced countries**

| Country | Auditors' opinion on university's financial statements |
|----------------|--|
| Australia | <p>In my opinion, the financial report of the University complies with section 41B of the Public Finance and Audit Act 1983 and presents fairly, in accordance with applicable Accounting Standards, the mandatory disclosure requirements of the Guidelines (Note) and other mandatory professional reporting requirements, the financial position of the University and the consolidated entity as at 31 December 2001 and the results of their operations and their cash flows for the year then ended.</p> |
| Canada | <p>In our opinion, these financial statements present fairly, in all material respects, the financial position of the University as at April 30, 2002 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.</p> |
| New Zealand | <p>In our opinion, the financial statements of the University and group:</p> <ul style="list-style-type: none">• Comply with generally accepted accounting practice in New Zealand; and• fairly reflect:<ul style="list-style-type: none">— the University and group's financial position as at 31 December 2001;— the results of their operations and cash flows for the year ended on that date; and— the service performance achievements in relation to the performance targets and other measures adopted for the year ended on that date. <p>Our audit was completed on 18 March 2002 and our unqualified opinion is expressed as at that date.</p> |

Country

Auditors' opinion on university's financial statements

UK

In our opinion:

- (a) the financial statements give a true and fair view of the state of affairs of the University and the group at 31 July 2001 and of the group's surplus of income over expenditure and cash flows for the year then ended and have been properly prepared in accordance with the Statement of Recommended Practice on Accounting in Further and Higher Education Institutions;
- (b) income from the Higher Education Funding Council for England grants and income for specific purposes and from other restricted funds administered by the University have been applied for the purposes for which they were received; and
- (c) income has been applied in accordance with the University's Statutes and, where appropriate, with the Financial Memorandum dated August 2000 of the Higher Education Funding Council for England.

USA

In our opinion, the financial statements of the University present fairly, in all material respects, the financial position and plans' fiduciary net assets of the University and the University's Retirement System (the Plans) respectively, at June 30, 2002 and 2001, and the revenues, expenses and changes in net assets and cash flows of the University and the changes in Plans' fiduciary net assets for the years then ended in conformity with accounting principles generally accepted in the USA.

Source: Universities' websites

Note: This refers to the Guidelines for the Preparation of Annual Financial Statements for the 2001 Reporting Period by Australian Higher Education Institutions.

Data submitted by institutions to UGC every year

General Tables

List of UGC-funded Long Programmes, excluding Research Postgraduate Programmes and Mapping to APC

List of UGC-funded Short Programmes and Mapping to APC

List of UGC-funded Research Postgraduate Programmes and Mapping to APC

Planned List of UGC-funded Long Programmes, excluding Research Postgraduate Programmes

List of Self-financed Long Programmes Leading to Formal Qualification & Mapping to APC

List of Academic Departments and Mapping to Departmental Cost Centre

Staff Tables

Staff Numbers

Staff Movement of UGC-funded Academic Staff (Grades A to I)

Research Related Staff

Student Tables

Student Enrolment on UGC-funded Long Programmes, excluding Research Postgraduate Programmes

Student Enrolment on UGC-funded Short Programmes (Provisional)

Student Enrolment on UGC-funded Short Programmes (Final)

Student Enrolment on Self-financed Long Programmes Leading to Formal Qualification

Student Load for UGC-funded Long Programmes, excluding Research Postgraduate Programmes

Student Load for UGC-funded Short Programmes (Provisional)

Student Load for UGC-funded Short Programmes (Final)

Research Postgraduate Student Enrolment Summary

Research Postgraduate Student Enrolment and Student Load by Programme by Departmental Cost Centre

Research Studentships

Research Postgraduate Student Enrolment by Category

List of Self-financed Short Programmes Leading to Formal Qualification and Student Enrolment

Non-local Students on Long Programmes Leading to Formal Qualification by Place of Origin (Nationality)

Age Profile for Students on Long Programmes Leading to Formal Qualification

Student Wastage for UGC-funded Programmes

First Year Intakes for Long Programmes Leading to Formal Qualification

Main Admission Qualification of full-time sub-degree/undergraduate First Year Intakes for UGC-funded Long Programmes

Student Tables (Cont'd)

Language Examination Results of full-time sub-degree/undergraduate First Year Intakes for UGC-funded Long Programmes

Admission Ratio for UGC-funded Long Programmes

Non-academic Information on full-time First-year sub-degree and undergraduate Student Intakes

Graduates, excluding Research Postgraduate Programmes

Research Postgraduate Graduates

Graduate Projection

Employment/Occupation of full-time Graduates

Annual Salary by Salary Category of full-time Graduates who are in full-time Employment

Average and Median Annual Salary of full-time Graduates who are in full-time Employment

Provisional Employment Situation of full-time Graduates of UGC-funded Programmes

Finance Tables

Total Income

Total Expenditure

Central Activity Expenditure and Reserves

Departmental Expenditure — Expenditure from General Funds

Departmental Expenditure — Research Expenditure from Specific Funds

Departmental Expenditure — Other Expenditure from Specific Funds

Reconciliation Statement — CDCF tables vs audited account

Reconciliation Statement — CDCF expenditure tables vs student unit cost table

Student Unit Cost by APC by level for UGC-funded Programmes

Relative Cost of Teaching by APC by level by mode for UGC-funded Programmes

Research Tables

Research Output

Prizes and Awards Received

Research Grants/Contracts

Research Postgraduate Students by Cohort

Patent Applications

Patents Granted

Start-up/Spin-off and/or Other Companies with Technology Transfer

Source: UGC's records

**Performance indicators
generally adopted for higher-education institutions in the UK**

- (a) Number of applications per undergraduate place
- (b) Undergraduates' entry scores
- (c) Classification or number of honours degrees awarded
- (d) Wastage rates of students
- (e) Staff workload
- (f) Employability of graduates
- (g) Postgraduate completion rates
- (h) Research grants and contracts
- (i) Research studentships awarded by prominent bodies, such as research councils
- (j) Records of publications
- (k) Students' loads
- (l) Staff/student ratios
- (m) Unit costs
- (n) Staff size by type
- (o) Institutional revenues and expenditures
- (p) Departmental equipment and recent grants and expenditures

Source: UGC's records

UGC's proposed performance indicators

Quality assurance processes (Note)

- (a) **Performance against Teaching Learning Quality Process Review criteria/indicators/ good practices — e.g. value added and outcome measurement (including language), effective student/staff consultation, etc. and the extent to which this information is made available within the institutions**
- (b) Special recognition of outstanding teachers
- (c) **Use of external advisory panels for course content at departmental level, etc.**
- (d) **Staff development, e.g. fraction of academic staff who have been through a teaching staff development programme (specify)**

Outcomes assessment

- (e) Satisfaction levels of graduates
- (f) **Employers' satisfaction with graduates — employment status, employer surveys, etc.**
- (g) **Income of graduates — by field**
- (h) Accreditation of professional programmes
- (i) **Graduate student completions**

Collaboration

- (j) Levels of usage of research facilities, library facilities, etc. by members of other institutions
- (k) Courses at other institutions taken by students of own institution and vice versa
- (l) Collaborative activities in teaching (e.g. co-teaching with colleagues from other institutions), administration (e.g. shared resources/services), research (e.g. number of co-authored papers with members of other institutions within or outside Hong Kong), etc.

Input measures

- (m) **Share of expenditure on information services including library**
- (n) **Share of expenditure on academic programmes**

Response to public policy priorities

- (o) Numbers of students admitted to second or subsequent years
- (p) Numbers of mature students admitted
- (q) Success in introducing self-financing taught postgraduate programmes

Mission-related

- (r) **Adherence to mission**
- (s) **If it is the institution's stated policy to teach courses in English, proportion of classes actually taught in English**
- (t) Industrial contributions and collaboration (in teaching and research)
- (u) Faculty involvement in public and professional service

Source: UGC's records

Note: Those indicators highlighted in bold face were considered "core indicators".

**Key performance data included
in the websites of five selected universities in advanced countries**

| Country | Key performance data included in the websites |
|----------------|---|
| Australia | <ul style="list-style-type: none">(a) Graduates' employment statistics(b) International student population(c) Collaborations by staff with other countries(d) Exchange student statistics(e) Contributions to community services |
| Canada | <ul style="list-style-type: none">(a) The number of students who register in a programme as a percentage of the number of applications received(b) Distribution of newly admitted students' average examination grades(c) Proportion of students graduating in a programme(d) Gross commercialisation revenues(e) Total number of books in libraries and per student(f) Usage of electronic resources(g) Library user surveys(h) Class size statistics(i) Employment rates of graduates |
| New Zealand | <ul style="list-style-type: none">(a) Number of departmental and school reviews completed(b) Number of publications and creative works(c) Number of staff participated in continuous professional development courses(d) Number of students identified with a disability(e) Number of community education courses and total enrolments(f) Number of exchange agreements with overseas universities and number of exchange students (both incoming and outgoing) |
| UK (Note 1) | <ul style="list-style-type: none">(a) <i>Performance in teaching:</i> Periodically, the Quality Assurance Agency in the UK conducts reviews of higher-education institutions' performance in teaching. In respect of each teaching programme of an institution, the Agency makes assessments on six aspects (Note 2) and grades each aspect from 1 to 4 (Note 3). Reports on the reviews are published which provide a helpful source of information for potential students applying to universities or colleges. The college selected by Audit for examination disclosed in its 2000-01 annual report the grades between 2 and 4 on the six aspects of teaching in respect of each of its teaching programme. |

Major opinion surveys conducted by eight institutions relating to their teaching, learning and research activities in 2000-01 and 2001-02

| Institution | Surveys |
|--------------------|--|
| CityU | (a) Graduate employment survey (b) Survey on the perception of the image of City University of Hong Kong, 2000 (c) Survey of first-year students (d) Student experience survey |
| HKBU | (a) Graduate employment survey (b) Service evaluation survey (c) Programme evaluation survey |
| LU | (a) Graduate employment survey 2001 (b) Survey of employers 2002 (c) Alumni survey 2002 |
| CUHK | (a) Graduate employment survey (b) Sexual Harassment Prevention and Awareness Training: A Quick Survey of the Committee on Sexual Harassment Policy (c) Customer Survey of the Estates Management Office (d) Survey on the Service of the Electronic Helpdesk System of the Information Technology Services Centre (e) Survey on Intra-campus Transport Services and Parking Arrangements (f) Client Satisfaction Survey 2001-02 of the University Health Services (g) The Occupational Safety and Health (Display Screen Equipment) Regulation Survey of the University Safety and Environment Office |

| Institution | Surveys |
|--------------------|--|
| HKIEd | <ul style="list-style-type: none">(a) HKIEd image survey 2000(b) Institutional survey on graduates(c) Institutional survey on personal tutor system(d) User satisfaction survey(e) Survey on profile of Year One full-time students 2001-02(f) Survey on graduate employment 2001(g) Survey on the effectiveness of modules and teaching |
| PolyU | <ul style="list-style-type: none">(a) Graduate employment survey(b) Survey on background of new students 2001-02 |
| HKUST | <ul style="list-style-type: none">(a) Graduate employment survey(b) A profile of undergraduate students(c) Teaching experience survey(d) Survey of academic reviewers(e) Student evaluation of teaching report(f) Estates Management Office customer survey |
| HKU | <ul style="list-style-type: none">(a) Graduate employment survey(b) The issues and challenges confronting the University(c) Annual opinion survey on Students' Evaluation of Teaching(d) Annual survey on the "Profile of New Full-time undergraduate students" |

Source: Institutions' records

Acronyms and abbreviations

| | |
|-----------|---|
| APC | Academic Programme Category |
| CDCF | Common Data Collection Format |
| CityU | City University of Hong Kong |
| CUHK | Chinese University of Hong Kong |
| EMB | Education and Manpower Bureau |
| FTE | Full-time equivalent |
| HKBU | Hong Kong Baptist University |
| HKIED | Hong Kong Institute of Education |
| HKSA | Hong Kong Society of Accountants |
| HKU | University of Hong Kong |
| HKU-SPACE | HKU School of Professional and Continuing Education |
| HKUST | Hong Kong University of Science and Technology |
| LU | Lingnan University |
| PolyU | Hong Kong Polytechnic University |
| SORP | Statement of Recommended Practice |
| HKSSAPs | Statements of Standard Accounting Practice of Hong Kong |
| UGC | University Grants Committee |
| VFM | Value for Money |