

Report No. 43 of the Director of Audit — Chapter 4

CORPORATE GOVERNANCE AND HEADQUARTERS ADMINISTRATION OF THE ENGLISH SCHOOLS FOUNDATION

Summary

1. The English Schools Foundation (ESF) was established under the English Schools Foundation Ordinance (Cap. 1117) in 1967. It operates 15 primary and secondary schools which receive recurrent government subsidies (totalling \$299 million in the 2002-03 school year, representing 29% of ESF income), and 1 primary school without such subsidies.

Audit review

2. The Audit Commission (Audit) has recently conducted a value for money audit of the ESF. The audit covered three major topics, namely: (a) government subsidies to the ESF; (b) corporate governance and Headquarters administration of the ESF; and (c) school administration of the ESF. This report deals with corporate governance and Headquarters administration of the ESF.

Corporate governance

3. **Membership size of the Foundation.** Audit notes that the membership size of the Foundation (the supreme governing body of the ESF) of 132 as at 1 April 2004 was large when compared with that of the supreme governing bodies of the eight University Grants Committee funded institutions, which ranged from 20 to 57. *Audit has recommended that the ESF should conduct a review with a view to reducing the membership size of the Foundation, with reference to the best practices of similar educational institutions.*

4. **Composition of the Foundation.** Audit notes that external members of the Foundation did not constitute a majority at any of the Foundation's four annual general meetings held in the 2000-01 to 2003-04 ESF financial years. *Audit has recommended that the ESF should conduct a review of the composition of Foundation members with a view to ensuring that external members will constitute a majority at Foundation meetings.*

Financial management

5. **High net current liabilities at financial year end.** Audit notes that, as at 31 August 2003, ESF current liabilities of \$355 million were more than 11 times of its current assets of \$31 million. As at the same date, the ESF used a bank overdraft of \$99 million to finance its expenditure. *Audit has recommended that the ESF should take action to reduce its net current liabilities.*

6. **Bank deposits held by ESF schools.** Audit notes that, as at 31 August 2003, while the ESF had a bank overdraft of \$99 million, its Foundation Office and schools held bank deposits of \$17 million. *Audit has recommended that, in order to reduce its bank overdrafts at its financial year end, the ESF should adopt an arrangement under which its schools would transfer a part of their bank deposits for which they do not have immediate needs to the Foundation Office, and the Foundation Office would refund to individual schools the money deposited with it when the need arises.*

Staff remuneration and recruitment

7. **ESF senior staff remuneration.** Audit notes that the salaries of most of the senior staff of the Foundation Office were set based on the salary of a Civil Service Directorate Grade officer, and the salary scale of ESF school principals was set 14 years ago based on a similar salary scale in the United Kingdom. *Audit has recommended that the ESF should conduct a review of the remuneration packages of its senior staff with a view to ensuring that they are broadly in line with those of similar posts in other local educational organisations.*

8. **ESF teaching staff remuneration.** Audit survey revealed that, in the 2003-04 school year, the estimated average annual remuneration of \$947,400 per ESF teaching staff member was the highest when compared with the corresponding figures of seven other largest local international schools (in terms of student number). Audit survey also revealed that, when compared with these schools, ESF teaching staff received the highest contract gratuity and responsibility allowance benefits. *Audit has recommended that the ESF should conduct a review of the remuneration packages of its teaching staff with a view to setting new packages, having regard to those of other major local international schools.*

9. **Extra payments to senior staff leaving the ESF.** Audit could not find records of the Executive Committee of the Foundation's decisions regarding extra payments made to two senior staff upon their leaving the ESF in the 2002-03 ESF financial year. *Audit has recommended that the ESF should ensure that the approval of the Executive Committee of the Foundation is obtained before making extra payments to ESF senior staff upon their leaving the ESF.*

10. **Staff recruitment.** Audit notes that, in the 2002-03 and 2003-04 ESF financial years, eight ESF interview teams travelled to the United Kingdom and Australia to conduct interviews for recruiting ESF school principals and teaching staff. *Audit has recommended that the ESF should review its recruitment practices with a view to reducing recruitment costs.*

Staff housing benefits

11. **Senior Staff Rental Scheme.** Audit notes that, as at 1 April 2004, the ESF leased 10 staff quarters for its senior staff at a total annual rent of \$6.8 million. However, as at the same date, it had 13 vacant ESF-owned staff quarters with an estimated total annual rental value of \$2.6 million. *Audit has recommended that the ESF should as far as possible accommodate eligible staff in the staff quarters it owns, instead of leasing quarters for them.*

12. **Rents of leased staff quarters exceeding entitlements.** Audit notes that it is ESF practice that, so long as the monthly rent (excluding rates and management fee) of a leased quarters does not exceed the rent entitlement of the staff member concerned, the ESF will pay the rent, rates and management fee (without a specified maximum amount) of the quarters, irrespective of the rent entitlement of the staff member. Audit could not find records of approval for this ESF practice. *Audit has recommended that the ESF should seek the approval of the Executive Committee of the Foundation for paying the rates and management fees of ESF-leased quarters for its senior staff, irrespective of their rent entitlements.*

13. **Quarters for teaching staff on overseas terms of employment.** Audit notes that, as at 1 April 2004, the ESF had 56 surplus ESF-owned Teaching-staff Grade staff quarters (30 being leased to ineligible staff and 13 to people other than ESF staff, and 13 being left vacant). Audit estimates that, if the ESF does not take action to reduce its number of quarters, the surplus requirements will progressively increase to 199 in the 2030-31 school year due to the retirement of teaching staff eligible for staff quarters. *Audit has recommended that the ESF should formulate a plan for disposing of its surplus staff quarters.*

14. **Leasing of surplus staff quarters to ineligible staff.** Audit notes that, as at 1 April 2004, of the 30 ESF-owned staff quarters leased to ineligible staff, 21 (70%) were let below market rent. Audit estimates that the difference between the market rent and actual rent of these 21 staff quarters amounted to \$1.1 million a year. *Audit has recommended that the ESF should seek and document professional advice obtained on the market rental values of its staff quarters for letting to ineligible staff.*

15. **Sale of surplus quarters.** Audit could not find records showing that prior approval had been given by the Executive Committee of the Foundation or by the Chairman or the Vice-chairman of the Executive Committee of the Foundation, before the sale of four ESF staff quarters in June and July 2002. *Audit has recommended that the ESF should obtain the prior approval from the Executive Committee of the Foundation before selling its staff quarters.*

Staff medical benefits

16. **Medical scheme for ESF non-teaching staff and their dependants.** Audit notes that the ESF ran an in-house medical scheme for reimbursing medical expenses incurred by

its non-teaching staff and their dependants. The staff of the Foundation Office did not have the medical expertise to assess the medical claims, and this arrangement required substantial staff resources. *Audit has recommended that the ESF should engage a medical insurance company to provide a medical scheme for its non-teaching staff and their dependants, with reference to similar schemes of other local educational institutions.*

17. ***Reimbursement of medical expenses exceeding entitlement.*** In mid-2001, an ESF senior staff member was admitted to a first-class ward in a hospital. For the purpose of reimbursement of medical expenses by the ESF, the written confirmation from the doctor concerned and the approval from the Foundation Office were required before an ESF staff member could receive treatment in this hospital. Audit could not find records of such confirmation and approval. This staff member was only entitled to reimbursement of expenses relating to treatment in a second-class ward. *Audit has recommended that the ESF should seek and record the approval of the Executive Committee of the Foundation if the medical benefits received by an ESF staff member exceed his entitlement.*

Entertainment expenses

18. ***Arrangements for reimbursing entertainment expenses.*** In the 2002-03 ESF financial year, six senior staff of the Foundation Office and the principals and heads of the schools operated by the ESF each had an annual budget ranging from \$8,288 to \$28,411 for reimbursement of entertainment expenses. Audit notes that most of these staff used up all, or a large portion of, their budgets for entertainment expenses. *Audit has recommended that the ESF should abolish the existing arrangement for setting annual individual budgets for entertainment expenses for some ESF staff, and set up a new system so that only designated ESF staff may submit claims for reimbursement of entertainment expenses on a need basis.*

19. ***Guidelines on claims for reimbursement of entertainment expenses.*** Audit examination revealed that, in the 2002-03 ESF financial year, of the total \$291,639 entertainment expenses reimbursed to eligible ESF staff, 77% were related to staff functions. In a dinner function held in that year which was attended by eight ESF staff, the expenditure was \$1,000 per participant. *Audit has recommended that the ESF should strictly enforce its revised policy on reimbursement of entertainment expenses which prohibits reimbursement of entertainment expenses relating to staff functions, and set a maximum limit on reimbursable entertainment expenses allowed for each participant in each function.*

Response from the English Schools Foundation

20. The ESF has accepted the audit recommendations.

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