

LEGISLATIVE COUNCIL BRIEF

CIVIL SERVICE PROVIDENT FUND SCHEME

INTRODUCTION

At the meeting of the Executive Council on 10 July 2001, the Council ADVISED and the Acting Chief Executive ORDERED that the Civil Service Provident Fund (CSPF) Scheme should be set up under the Mandatory Provident Fund Schemes Ordinance (MPFSO) (Cap. 485) and that it should be applied to officers who joined the civil service on or after 1 June 2000 and when they progress onto permanent terms. The CSPF Scheme is to be based on the following design features –

- (a) the normal retirement ages should be the same as under the New Pension Scheme (NPS);
- (b) the Government's contributions under the CSPF, including mandatory and voluntary contributions, should follow a progressive contribution rates schedule starting from 5% and increasing up to 25% of the basic salary;
- (c) disciplined services officers should be provided with, in addition to (b) above, a Special Disciplined Services Contribution (SDSC) at 2.5% of the basic salary;
- (d) the overall financial commitment of the CSPF, inclusive of the contributions in (b) and (c) above, should be kept within 18% of the salary cost;
- (e) the Government's contribution rate in respect of an officer upon his joining the CSPF should be the rate corresponding to his years of continuous service from first civil service appointment either on probation or on agreement. Where an officer is directly appointed to a promotion post/rank on agreement and subsequently progresses to permanent terms,

the Government's contribution for him will start at the rate on the progressive contribution rates schedule corresponding to the years of experience required for the promotion post/rank plus his years of continuous service on civil service appointment;

- (f) the Government's voluntary contribution (i.e. excluding the mandatory contributions under the MPFSO) should be fully vested in an officer on completion of ten continuous years of service since first civil service appointment or on reaching the normal retirement age, whichever is the earlier, with 0% vesting in the interim;
- (g) the SDSC should be fully vested in an officer on reaching age 55, with 0% vesting in the interim; and
- (h) both the Government's voluntary contribution and the SDSC should be fully vested in an officer on death or retirement on permanent incapacity.

2. There should be provisions in the CSPF Scheme to enable the forfeiture and reduction of benefits attributable to the Government's voluntary contribution and the SDSC on disciplinary grounds, and withholding of such benefits in case of doubt. Special additional benefits for death, incapacity and injury should be provided through lump-sum payments outside the CSPF Scheme. Serving officers on permanent and pensionable terms of appointment should not be provided with an option for transfer to the CSPF, and new recruits should not be allowed an option for the NPS.

BACKGROUND AND ARGUMENT

3. In the Civil Service Reform Consultation Document issued in March 1999, we proposed, among other things, to study the feasibility of setting up a CSPF Scheme for recruits on permanent terms. The Scheme is to be a replacement of the pension system to complement the new entry system for the civil service, which provides for a more flexible and competitive appointment system while maintaining a structured career framework that provides stability, continuity and a high degree of integrity among civil servants.

4. At the Executive Council meeting on 16 January 2001, the Council advised and the Chief Executive ordered that the consultants' recommendation on the design options of the proposed CSPF Scheme should be presented for consultation. The public consultation on the CSPF proposal ended on 30 April, and the Panel on Public Service was provided with an information note on the outcome of the consultation for its meeting on 18 June 2001. There is no objection in principle to the CSPF proposal. Views on the design options, the contribution rates, the SDSC, the vesting schedules in particular, are diverse.

DESIGN FEATURES OF THE CSPF SCHEME

Legal Framework

5. As the consultants have pointed out in their Consolidated Report on the consultancy study, "Creating the CSPF under the MPFSO would show support for that ordinance as the retirement protection scheme for the working population of Hong Kong." In fact, it would be difficult to justify why the provident fund for civil service recruits, a new retirement benefits system yet to be set up, should be in a form other than a Mandatory Provident Fund (MPF) scheme.

Retirement Age

6. The proposal to maintain the existing retirement ages under the NPS, i.e. 60 for all civilian staff, 55 for disciplined services staff in general or 57 for certain prescribed disciplined ranks, has received divergent views in the consultation. Slightly over half of the respondents on this subject agreed with maintaining the existing retirement ages, while some others considered that the retirement ages should be extended to 65 for civilians and 60 for disciplined services staff. We do not consider it appropriate to introduce changes to the normal retirement ages in the civil service at this juncture in the absence of an in-depth review of implications over the staffing situation of the service.

Contribution Rates

7. The consultants have recommended two options on the Government contribution rate (inclusive of the mandatory MPF contribution) for staff in general –

- (a) uniform contribution rate; and
- (b) progressive contribution rates based on service.

8. Views received during the public consultation on this subject are divided. Most of the staff associations and submissions from the private sector support uniform contribution rate whereas the departmental management and a few disciplined services unions support progressive contribution rates based on service length.

9. Apart from introducing more flexibility in the civil service entry and exit system, one of the objectives of the new entry system is to ensure that permanent terms are offered only to those with proven performance and potential. Continuity and stability of the civil service remain important factors in our human resource management policy. Although the uniform rate option is simple, easy to administer and would enhance the ability to attract candidates if higher initial contributions are provided, we are mindful of the investment the Government puts in on staff training and development. In our view, a progressive set of contribution rates based on service would enhance the retention value of the scheme as it provides higher rewards for long service. We will further discuss with the Staff Sides on the progressive contribution rates schedule within the range of Government's contribution rates from 5% to 25% of the basic salary, subject to keeping the overall financial commitment of CSPF (inclusive of mandatory, voluntary and SDSC contributions) at a level not higher than 18% of the salary cost.

Application of Contribution Rates Schedule

10. The CSPF Scheme is to be a replacement of the pension system for career civil servants who joined the civil service on or after 1 June 2000 after they have proved their suitability for a long-term career in the service. During the consultation, some respondents have suggested that the services on probationary or agreement terms should also be given recognition and retrospective contributions should be made in respect of such services once a recruit is appointed on permanent terms and join the CSPF Scheme. Some have suggested that the CSPF Scheme should apply to recruits from their first day of appointment, irrespective of terms.

11. Similar to the pension schemes, the CSPF Scheme should be applied

only to civil servants who have reached permanent terms. As regards determination of the contribution rates, the consultants' proposal on the progressive contribution rates option assumes that Government's contribution rate for an officer would be based on his continuous years of service in the Government since first appointment on civil service terms. We consider this to be a reasonable and equitable arrangement as it means all staff, whether disciplined or non-disciplined, will have their years of service on civil service terms recognized once they progress onto permanent terms of appointment, which is normally after three years of probation for disciplined staff and after six years (three-year probation and a three-year agreement) for most civilian staff. In other words, as soon as the officer is confirmed on permanent terms, the Government's contribution rate is the rate applicable for the fourth year or the seventh year, whichever the case may be. For officers on probationary terms, they will be provided with the mandatory MPF contributions as required by the MPFSO. For officers on agreement terms as part of the normal entry system, they will receive in addition a contract gratuity on satisfactory completion of the contract. We intend to pitch their contract gratuity rate plus the mandatory MPF contribution at the level of the contribution rate under the CSPF for the corresponding years of service. In this way, the officers' benefits and the Government's contribution will be kept at broadly the same level as estimated by the consultants. These officers can choose to deposit the contract gratuity received into the CSPF as employee's voluntary contribution.

12. For direct appointments to higher ranks, the contribution rate for the appointees should, in addition, recognize the years of experience specified and required for the post/rank, i.e. apart from the years of continuous service from their first appointment on civil service terms, the years of experience specified and required for the post/rank that they first join should also be counted. In other words, if a person is appointed from outside to say a Senior Administrative Officer post requiring at least seven years of working experience initially on a three-year agreement, when he is confirmed on permanent terms, the Government's contribution rate will be set at the rate for the 11th year. This is based on the principle that the progressive contribution rates schedule would mirror the career progression of an officer, and an officer who is appointed in the middle of the career pathway would receive a higher contribution as recognition.

Special Disciplined Services Contribution (SDSC)

13. The SDSC at 2.5% of salary, when paid over the career of a typical disciplined services officer, would accumulate to a value which is roughly equivalent to five years of CSPF contributions from age 55 to 59, after allowing for investment return for the five years. During the consultation, there is a suggestion from the disciplined services that a higher level of contribution should be made to reflect the full pension benefits under the existing pension schemes for disciplined staff. We have difficulties to support this suggestion as the rate of 2.5% for SDSC has been proposed to maintain the overall relativity in terms of CSPF benefits receivable by the civilian and disciplined staff having regard to the differences in their respective normal retirement ages.

Vesting Schedule

Government Voluntary Contribution

14. There is general consensus that ten years is a reasonable time limit for full vesting of CSPF benefits due to voluntary contributions. However, views are divergent on whether partial vesting should be allowed in the interim for less than ten years' service. As the civil service should maintain a more permanent and stable workforce and provide a longer-term career for civil servants in general, a **10-year cliff-vesting**, i.e. no partial vesting in the interim for less than ten years' service, would be appropriate. This is also in line with the current NPS design which does not provide for a deferred pension to officers who leave with less than ten years' service. We consider the suggestion of progressive vesting between 11 and 20 years of service not appropriate as it would mean a substantially longer vesting scale than private sector practice and a major deviation from the existing NPS.

Special Disciplined Services Contribution

15. Most disciplined service staff and management are in favour of the option of allowing partial vesting before reaching the prescribed retirement ages. However, one of the purposes served by the SDSC is to retain disciplined services staff for a permanent career in the disciplined services until the prescribed retirement ages. Thus in the interest of maintaining the stability of the disciplined services, the SDSC should be fully vested only upon

reaching age 55. This is in line with the existing arrangements under NPS whereby disciplined staff who leave early before reaching 55 would not enjoy enhancement to their pension benefits.

Counting of the Vesting Schedule

16. On the counting of the vesting schedule, we follow the consultants' recommendation that the vesting schedule should be based on years of continuous service since first appointment on civil service terms.

Penalty Provision

17. The consultants have recommended that provisions dealing with the withholding, forfeiture, cancellation or reduction of benefits arising from Government's voluntary contributions, including the SDSC, should be included in the CSPF scheme design in order to help maintain a high standard of integrity and probity in the civil service. Feedback obtained through the consultation exercise suggests that the public and the retirement business sector are in support of the consultants' recommendation. Views from the Staff Sides vary. Some support the recommendation and suggest that clear rules and guidelines should be formulated in consultation with staff; that "misconduct" should be clearly defined and should only include job-related allegations; and that there should be an appeal and arbitration mechanism. Others consider that retirement benefits should be forfeited only if an officer commits a criminal offence and is sentenced to jail immediately. There is also the view that forfeiture of retirement benefits would amount to double penalty.

18. From the discipline policy angle, we consider that there is a need to preserve the ability to withhold and forfeit (wholly or in part) the accrued benefits attributable to Government's voluntary contributions (i.e. including the SDSC) towards the CSPF as a deterrent against misconduct. There should be enabling provisions in the rules of the CSPF which empower the Administration to withhold payment of the accrued benefits attributable to Government's voluntary contributions where an officer is subject to investigations relating to misconduct during his government service, and to forfeit either wholly or in part the accrued benefits where an officer is awarded a punishment of removal from office after due disciplinary process.

Transfer Option

19. Views on transfer option for serving pensionable officers are divided. Those who suggest that a transfer option should be provided to serving officers are of the view that serving officers should be allowed to enjoy the flexibility afforded under the CSPF Scheme to receive their retirement benefits on leaving service.

20. We remain in agreement with the consultants' recommendation not to allow transfer from the pension schemes to the CSPF Scheme, given that the two schemes are based on entirely different design logic, resulting in difficult settlement over the appropriate transfer value and transfer would entail significant financial implications and administrative and legislative complexities. This is also in line with the arrangements for all other changes to the civil service appointment terms and fringe benefits package under the current Civil Service Reform which are applicable to new recruits only and serving officers are not allowed an option for the new package.

21. There is a suggestion from a civil service union that new recruits should be allowed the option to choose between the pension scheme and the CSPF Scheme. However, given that the CSPF Scheme is proposed as a modernised retirement benefits scheme for new recruits in place of the existing pension scheme to complement the new civil service entry system, it is not appropriate to provide these recruits with the option to join the pension scheme. To allow such an option would also give rise to significant uncertainties in the cash flow, financial commitment and administrative arrangements for the retirement benefits for new recruits and defeat one of the main purposes of introducing the CSPF Scheme.

Death, Incapacity and Injury Benefits

22. Apart from the CSPF Scheme design options, we have also put forward proposals for death, incapacity and injury benefits for recruits appointed on or after 1 June 2000 on permanent terms to the Staff Sides and departmental management for consultation. The proposals are set out at the

Annex Annex.

23. The proposals are designed with the aim of providing benefits for death, incapacity and injury at a level broadly comparable in overall terms to those for existing staff on pensionable terms. However, given the fact that the existing benefits are integrated into the pension schemes which are fundamentally different in design principles, it would not be possible to match the level of benefits in all circumstances.

24. The majority of the Staff Sides and departmental management find the principles and proposed level of death, incapacity and injury benefits acceptable. In particular, they support the provision of additional benefits for death, incapacity and injuries through payments outside the defined contribution provident fund scheme. Some also suggest that the duty-related death and incapacity benefits for new recruits on probationary and agreement terms should be brought up to match those for permanent terms staff. Given the compassion that the management should show in such tragic cases, we support the extension of the package to new recruits on probationary and agreement terms. The number of death or incapacity cases in the civil service has been small (our records show there were 41 cases of duty-related death and incapacity in the past five years).

BASIC LAW IMPLICATIONS

25. Since the proposed CSPF Scheme is intended for officers who join the service on permanent terms after May 2003 and does not affect the previous system of employment, the proposal is consistent with the Basic Law provisions and in particular Article 103.

FINANCIAL AND STAFFING IMPLICATIONS

26. We shall keep to the long term financial commitment ceiling of 18% of basic salary in refining the progressive contribution rates schedule recommended by the consultants, taking into account also the financial implication of the SDSC.

27. On staffing, CSB will require a small team of staff headed by an AOSGC to co-ordinate the development of detailed rules of the CSPF Scheme and the implementation of the scheme with departments and the Treasury until March 2004. The long-term staffing requirements will be reviewed in due course. The Treasury will require additional recurrent computer support and a

team of five staff at Accounting Officer and clerical staff ranks to oversee the operation of the CSPF.

ECONOMIC IMPLICATIONS

28. The amount of assets built up under the CSPF can be expected to stimulate the demand for, and hence the supply of long-term financial instruments to match the maturity structure of the CSPF liabilities corresponding to the retirement benefits pay-outs.

PUBLIC CONSULTATION

29. Public consultation on the proposed CSPF Scheme commenced on 16 January 2001 and ended on 30 April. We are issuing a press release on the subject. We will continue with our discussions with the Staff Sides to refine the detailed design of the CSPF and work with the consultants on the implementation of the scheme. The target is to have the CSPF Scheme in place by early 2003.

Civil Service Bureau
10 July 2001

**Summary of Proposed Death, Incapacity and Injury Benefits
for Recruits Appointed on or after 1 June 2000**

| Circumstances | New Recruits on Permanent Terms | New Recruits on Probationary/Agreement Terms |
|--|---|---|
| Death on Duty | (a) accrued CSPF benefits + (b) ECO compensations + (c) death payment of 36 months' final salary (may be enhanced up to 48 months in exceptional circumstances) | (a) MPF benefits and/or gratuity + (b) ECO compensations + (c) same as (c) for permanent terms |
| Death in Service (non-duty-related) | (a) accrued CSPF benefits + (b) death payment of 16 months' final salary | (a) MPF benefits and/or gratuity + (b) death payment of 12 months' final salary |
| Incapacity for Injury on Duty | (a) accrued CSPF benefits + (b) ECO compensations + (c) incapacity payment at a minimum rate of 24 months' final salary, plus additional 1.8 month for 1% incapacity (proportional to percentage of permanent incapacity) | (a) MPF benefits and/or gratuity + (b) ECO compensations + (c) same as (c) for permanent terms |
| Incapacity for Ill-health (non-duty-related) | (a) accrued CSPF benefits + (b) incapacity payment of 24 months' final salary | MPF benefits and/or gratuity |
| Injury on Duty (remain in service) | ECO compensations | ECO compensations |

Notes

ECO Compensations

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|----------------------------------|---|
| Death on Duty | Monthly earning (capped at \$21,000) x Age factor (84 for <40; 60 for \geq 40 and <56; 36 for \geq 56) (subject to a minimum of \$303,000) |
| Incapacity for Injury on Duty | Monthly earning (capped at \$21,000) x Age factor (96 for <40; 72 for \geq 40 and <56; 48 for \geq 56) x % of permanent incapacity (subject to a minimum of \$344,000) |
| Injury on Duty | - ditto - |