

## **LEGISLATIVE COUNCIL BRIEF**

### **2008-09 CIVIL SERVICE PAY ADJUSTMENT**

#### **INTRODUCTION**

At the meeting of the Executive Council on 3 June 2008, the Council ADVISED and the Chief Executive ORDERED that the following pay offers should be made to the staff sides of the four central consultative councils –

- (a) a pay increase of 6.30% (equal to the net pay trend indicator (PTI) for the upper salary band) for civil servants in the directorate and upper salary band with effect from 1 April 2008;
- (b) a pay increase of 5.29% (equal to the net PTI for the middle salary band) for civil servants in the middle salary band with effect from 1 April 2008; and
- (c) a pay increase of 5.29% (equal to the net PTI for the middle salary band) for civil servants in the lower salary band, by invoking the “bring-up” arrangement, with effect from 1 April 2008.

#### **JUSTIFICATIONS**

##### **(A) Civil service pay policy**

2. The Government’s policy is to offer remuneration sufficient to attract, retain and motivate staff of a suitable calibre to provide the public with an effective and efficient service; and such remuneration is to be regarded as fair by both civil servants and the public they serve. For the latter, the Government accepts that broad comparability with the private sector should be an important factor in setting civil service pay.

## **(B) Improved civil service pay adjustment mechanism**

3. Under the improved civil service pay adjustment mechanism, civil service pay is checked against the prevailing market situation on a regular basis through three different kinds of surveys, namely (i) a pay trend survey (PTS) every year to ascertain the year-on-year pay adjustment movements in the private sector; (ii) a starting salaries survey every three years to compare civil service starting salaries with those of the private sector requiring similar academic qualifications and/or experiences; and (iii) a pay level survey (PLS) every six years to ascertain whether civil service pay is broadly comparable with private sector pay.

## **(C) The PTS mechanism**

4. The annual PTS is commissioned by the tripartite PTS Committee, comprising staff sides representatives, management representatives, and members of the Standing Commission on Civil Service Salaries and Conditions of Service and the Standing Committee on Disciplined Services Salaries and Conditions of Service. Under the supervision of the PTS Committee, the annual PTS is conducted by the Pay Survey and Research Unit under the Joint Secretariat for the Advisory Bodies on Civil Service and Judicial Salaries and Conditions of Service. The survey findings are collated and condensed into three gross pay trend indicators (PTIs), one each for the upper, middle and lower salary bands<sup>1</sup>. The payroll cost of increments incurred for civil servants in each salary band (expressed as a percentage of total salary payment) is then deducted from the relevant gross PTI to arrive at the net PTI<sup>2</sup>.

5. Upon the completion of a PTS, the Administration will seek the Chief Executive (CE)-in-Council's decision on the pay offers to be made to the staff sides of the four central consultative councils, having regard to six factors, namely (i) the net PTIs, (ii) the state of the economy, (iii) changes in the cost of living, (iv) the Government's fiscal position, (v) the pay claims of the staff sides, and (vi) the state of the civil service morale. If the pay offers decided by the CE-in-Council are different from the staff sides' pay claims, the staff sides will be consulted again and the CE-in-Council will then make a final decision.

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<sup>1</sup> The pay ranges of the three salary bands are -

- Upper : Above Master Pay Scale (MPS) 33 to General Disciplined Services (Officer) Pay Scale (GDS(O)) 38 or equivalent, i.e. \$45,971 to \$91,765;
- Middle: From MPS 10 to 33 or equivalent, i.e. \$14,990 to \$45,970; and
- Lower : Below MPS 10 or equivalent, i.e. below \$14,990.

<sup>2</sup> The deduction of payroll cost of increments from the gross PTIs to arrive at the net PTIs was recommended by the Committee of Inquiry in 1989 in view of its other recommendation to include private sector merit pay and increments in the annual PTS. The Committee considered that for the sake of fairness, if all take-home pay in the private sector was taken into account in the PTS, the increment payment made to civil servants who had not yet reached the maximum point of their rank should also be taken into account.

#### **(D) The 2008 PTS**

6. Starting from last year, with the agreement of the staff sides and the CE-in-Council, the annual PTS collects pay adjustment data from both larger (i.e. with 100 or more employees) and smaller (i.e. with 50-99 employees) companies, which are assigned a 75% and 25% weighting respectively. This year's PTS, covering the 12-month period from 2 April 2007 to 1 April 2008, has collected the pay adjustment data (including basic pay and variable pay such as bonuses) of 141 289 employees in 97 companies (consisting of 139 502 employees in 72 larger companies and a total of 1 787 employees in 25 smaller companies). The data collected are collated under three salary bands according to the basic pay levels of the surveyed employees. For each salary band, the gross PTI is compiled through a two-stage process: firstly the pay adjustment data for larger companies and those for smaller companies are consolidated separately on a simple weighted average basis, and secondly these two figures are combined to produce the gross PTI by applying a gross-up factor of 0.75 to the larger companies figure and another gross-up factor of 0.25 to the smaller companies figure. A net PTI is then compiled for each salary band by deducting the 2007-08 actual payroll cost of increments incurred for civil servants in that salary band from the relevant gross PTI.

7. The gross PTIs, the payroll cost of increments incurred for civil servants in 2007-08, and the net PTIs are as follows -

<u>Salary Band</u>	<u>Gross PTI</u> [A]	<u>Payroll cost of</u> <u>increments</u> [B]	<u>Net PTI</u> [A] - [B]
Upper	6.90%	0.60%	<b>6.30%</b>
Middle	5.87%	0.58%	<b>5.29%</b>
Lower	4.47%	0.57%	<b>3.90%</b>

#### **(E) State of the economy**

8. The Hong Kong economy enjoyed a robust and broad-based expansion in 2007, when the Gross Domestic Product (GDP) registered a growth of 6.4% in real terms and 9.5% in nominal terms. The Government is cautiously optimistic about the economic outlook for 2008. While the external environment remains uncertain and challenging given the weak US economy and the unsettled global financial markets, the local economy should continue to benefit from the vibrant growth momentum in the emerging and developing economies, including the Mainland. Also the solid expansion in domestic demand is expected to continue, and remain a key driver in economic growth going forward. With the relatively strong GDP

growth of 7.1% in real terms in the first quarter of 2008, and barring any abrupt external shocks, it is likely that GDP growth in 2008 would be close to the upper end of the forecast 4-5% growth range in real terms.

9. With regard to the labour market, the latest (February – April 2008) seasonally-adjusted unemployment rate and underemployment rate edged down to 3.3% and 1.8% respectively, and were the lowest levels for more than ten years. Labour earnings and wages were on the rise. The latest available statistics published by the Census and Statistics Department<sup>3</sup> showed an increase of basic pay (i.e. excluding variable pay) of 2.7% and 3.8% respectively for workers up to the supervisory level and those in the personal services sector for December 2007 over a year earlier; and an increase of basic pay (i.e. excluding variable pay) of 4.9% and 6.4% respectively for managerial and professional employees and staff in the financial and insurance sector for June 2007 over a year earlier. The overall prospect remains positive amidst the continuation of economic growth and the solid expansion in domestic demand.

#### **(F) Changes in the cost of living**

10. The underlying Composite Consumer Price Index (CCPI) registered an annual increase of 2.8% (after netting out all one-off concessions) in 2007<sup>4</sup>. Consumer price inflation picked up further, to 4.9% (after netting out all one-off concessions) in the first quarter of 2008 (and at 5.4% in April 2008), as the creeping up in local inflation was compounded by the surge in food prices amidst the global food inflation. The outlook is rather uncertain as global food and crude oil prices, as well as exchange rate, are volatile. High commodity prices and the strength of the local economy are likely to continue to exert inflationary pressure in the coming months. In view of the high degree of uncertainties in the external environment, the risk to the stated forecast of a CCPI increase of 4.5% (after netting out all one-off concessions) for 2008 is on the upside.

#### **(G) Government's fiscal position**

11. As at 31 March 2008, Government's consolidated fiscal reserves amount to \$492.9 billion. For 2008-09, total public expenditure is estimated at 19.2% of GDP, operating deficit at \$6.3 billion, and consolidated deficit at \$7.5 billion. Premised on a forecast annual GDP trend growth rate of 4.5% in real terms and an annual trend CCPI rate of 4% over the medium term, the Government is projected to enjoy annual surpluses for the operating and

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<sup>3</sup> The salary adjustment statistics compiled by the Census and Statistics Department are confined to changes to the basic pay of the concerned categories of employees. This is different from the PTS methodology, which captures changes to both basic and variable pay.

<sup>4</sup> This refers to the 2007 calendar year. The inflation rate, after netting out all one-off concessions, increased to 3.4% for the 2007-08 financial year.

consolidated accounts for each of the years from 2009-10 to 2012-13.

**(H) Staff sides' pay claims**

12. The pay claims from the staff sides of the four central consultative councils are summarized below -

<u>Staff Side</u>	<u>Upper Band</u>	<u>Middle Band</u>	<u>Lower Band</u>
(I) Senior Civil Service Council			
(a) HK Chinese Civil Servants' Association (HKCCSA)	6.30%	6.30%	6.30%
(b) Association of Expatriate Civil Servants of Hong Kong	6.30%	5.29%	5.29%
(c) HK Senior Government Officers Association	6.30%	5.29%	5.29%
(II) Police Force Council	6.90%	5.87%	4.47%
(III) Disciplined Services Consultative Council	6.30%	5.29%	3.90%
(IV) Model Scale 1 Staff Consultative Council	no claim received	no claim received	equivalent to the adjustment rate for the middle salary band <sup>5</sup>

**(I) State of staff morale**

13. With a pay rise of 4.62%/4.96% for 2007-08 and renewed open recruitment to ease the very tight manpower situation, civil service morale has remained stable. Nonetheless, the rising inflation, in particular the escalation in prices for basic necessities, weighs heavily on the junior to middle level civil servants.

**(J) Pay offers for 2008-09**

14. The CE-in-Council decided that the following pay offers be put to the staff sides of the four central consultative councils for further consultations for the reasons explained in paragraphs 15 to 21 below -

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<sup>5</sup> The MOD 1 Council is divided on the pay claim. Two of its members, both belonging to the HKCCSA, demand that all civil servants should be awarded with a pay rise of 6.30% (i.e. the net PTI for the upper salary band).

<u>Salary band</u>	<u>No. of civil servants<sup>6</sup></u> (as at 31.3.2008)	<u>Net PTI</u>	<u>Pay offer</u>
Directorate	1 204	n.a.	<b>6.30%</b>
Upper	17 499	6.30%	<b>6.30%</b>
Middle	113 152	5.29%	<b>5.29%</b>
Lower	21 895	3.90%	<b>5.29%</b>

**(i) Directorate civil servants**

15. The coverage of the annual PTS does not include directorate civil servants. Following the practice adopted since 1990, the CE-in-Council decided that the pay offer for them should be set at the net PTI for the upper salary band (i.e. an increase of 6.30%)

**(ii) Upper and middle salary band civil servants**

16. The CE-in-Council decided that the pay offer for the upper and middle salary bands should follow strictly the relevant net PTIs, i.e. an increase of 6.30% and 5.29% respectively. In the past 20 years, whenever there was an annual pay rise for the civil service, the rates endorsed by the CE-in-Council for these two salary bands were equivalent to the relevant net PTIs except for five years. They were: in 1990-91 and 1991-92 when the pay increase rates were lower than the net PTIs due to budgetary and economic reasons; in 1992-93 when the pay increase rates were higher than the net PTIs to preserve the purchasing power of civil service pay; and in 1999-00 and 2000-01 when civil service pay was frozen even though the net PTIs for each of the two years showed small increase/decrease for different salary bands. There are no such or other special circumstances this time round. While inflation is rising, the extent and impact are moderate as compared to the rampant situation in the early 1990's. In addition, the economy and the Government's fiscal position are in a healthy state.

**(iii) Lower salary band civil servants**

17. The net PTI for the lower salary band is 3.90%, and is 1.39 percentage points lower than that of the middle salary band. The CE-in-Council has carefully considered whether or not to invoke the "bring-up" arrangement<sup>7</sup> (i.e. to align the pay adjustment for the lower salary band to

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<sup>6</sup> Including around 20 000 civil servants seconded to/working in trading funds, subvented and other public bodies.

<sup>7</sup> The "bring-up" arrangement was introduced in 1989 upon the recommendation of the 1988 Committee of Inquiry.

the net PTI of the middle salary band if the net PTI for the lower salary band is less than that for the middle salary band). This is a decision, where applicable, made each year by the CE-in-Council in the context of the annual civil service pay adjustment exercise.

18. The CE-in-Council is aware that the pay of civil servants in Job Level one<sup>8</sup> is 3% higher than their private sector counterparts as revealed by the 2006 PLS. The invocation of the “bring-up” arrangement last year means that an additional 0.71 percentage point over and above its 2007 net PTI (i.e. 3.91%) has been embedded into the pay of civil servants in the lower salary band. If the “bring-up” arrangement is invoked again this year, the pay increase for the lower salary band would be brought up by 1.39 percentage points, from 3.90% to 5.29%, and this extra element could increase the risk of a pay cut for junior civil servants upon the conclusion of the next PLS (which will take place in 2012). Under the established framework for the application of PLS results to the civil service, the pay of a defined group of civil servants would be adjusted if it deviates from that of its private sector counterparts by more than plus/minus 5%.

19. The Administration has clearly explained this risk to the staff sides of the four central consultative councils and other relevant staff representatives. Most of them consider that the “bring-up” arrangement should be adopted in 2008-09 because the net PTI for the lower salary band (3.90%) is not enough to offset the forecast inflation for 2008 (4.5%). They urge the Administration to take steps to provide relief to the lower paid staff. They contend that it is pre-mature to speculate on the results of the 2012 PLS, and that it will be a blow to civil service morale and stability if the “bring-up” arrangement is not invoked this year.

20. The additional recurrent cost for invoking the “bring-up” arrangement for 2008-09 is estimated at \$43 million for the civil service and \$53 million for the subvented sector<sup>9</sup>.

21. Taking all the considerations set out in paragraphs 17 to 20 above into account, and having regard to the forecast increase in cost of living, the healthy state of the economy and of the Government’s fiscal position, the CE-in-Council decided to make an offer of a pay rise of 5.29% (i.e. invoking the “bring-up” arrangement) for the lower salary band, on the clear understanding that –

(a) the invocation of the “bring-up” arrangement in 2008-09 does

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<sup>8</sup> Job Level one refers to civil servants remunerated on or below MPS 10 or equivalent.

<sup>9</sup> This is calculated on the assumption that the weighted average of the civil service pay adjustment rates will be applied to the portion of subvention which is priced-adjusted on the basis of formulae including a factor of civil service pay adjustment. Please see paragraphs 27 and 28 below for details.

not imply that it will necessarily be applied in future years, and the staff sides should have no expectation that it will be; and

- (b) should the next (or subsequent) PLS reveal a differential of more than plus/minus 5% in the pay (inclusive of the embedded “bring-up” portion) between a particular group of civil servants and their counterparts in the private sector, then the pay for the concerned civil servants would be adjusted according to the agreed mechanism.

**(K) Effective date for the pay offer**

22. In line with the established practice, the CE-in-Council decided that the pay offers should take effect retrospectively from 1 April 2008.

**OTHER RELATED ISSUES**

**(A) Judges and judicial officers**

23. On 20 May 2008, the CE-in-Council decided to accept all the major recommendations of the Standing Committee on Judicial Salaries and Conditions of Service in respect of the institutional framework and mechanism for the determination of judicial remuneration. The CE-in-Council also decided that in considering any adjustments to be offered to the Judiciary this year and in the future, the pay reductions applied to the civil service in 2002-03, 2003-04 and 2004-05 should be set aside permanently for JJOs. The CE-in-Council further decided that as an interim measure pending the establishment of the institutional framework for the determination of judicial remuneration, if the 2008-09 adjustment rate for the upper salary band and directorate civil servants results in civil service pay being higher than that of JJOs at comparable level(s), a pay rise for JJOs should be offered to bring their pay to the same level as their civil service counterparts in dollar terms. If the civil service pay for 2008-09 is adjusted according to the pay offers in paragraph 1 above, then in accordance with the interim measure, the pay for JJOs equivalent to or above D3 would be increased by 6.25% to 6.29%, and that for JJOs below D3 would be increased by 0.19% to 0.24%.

**(B) Political appointees**

24. The pay policy and pay adjustment mechanism for politically appointed officers (including Principal Officials (POs), Deputy Directors of Bureau and Political Assistants to POs) are distinct and separate from those for the civil service. The CE-in-Council’s decision on the pay offers (if implemented) does not apply to them.

**(C) Non-civil service contract staff**



25. Non-civil service contract staff (NCSC) are recruited by individual bureaux and departments for work that is seasonal or time-limited or part-time in nature, or work where the mode of delivery is under review or likely to be changed (for example, through outsourcing), etc. They are not civil servants. Their employment package is separate and different from that for the civil service. For example, the recruiting bureaux and departments are authorized to determine, and adjust as necessary, the pay of their NCSC staff, having regard to a host of factors, including condition of the employment market, recruitment results and staff retention needs, cost of living, civil service pay adjustment, etc.<sup>10</sup> The experience last year is that bureaux and departments decided to increase the pay of some 76% of their NCSC staff at rates comparable to or higher than those for the civil service. Another 13% of NCSC staff received pay rise at rates less than those for the civil service. In line with the established policy that the employment of NCSC staff is subject to availability of funding, the associated additional financial implications were met from within the concerned bureaux and departments' own resources.

26. As the pay of NCSC staff is managed differently from that of the civil service, the CE-in-Council's decision on the pay offers and the final pay adjustment decision to be made for the civil service will not be applied to this category of staff. Should bureaux and departments consider there is a case to adjust the pay of some/all of their NCSC staff in 2008, the same arrangement as followed last year will apply.

**(D) Subvented sector staff**

27. Generally speaking, remuneration of the staff of subvented bodies is a separate matter from the subventions granted by the Administration to these bodies. With the exception of the staff in the aided school sector who are paid according to the civil service pay scales, the Administration is generally not involved in the determination of the pay or pay adjustment of staff working in subvented bodies. These are matters between the concerned bodies as employers and their employees. The Administration therefore will not directly impose any pay adjustment applicable to the civil service in the subvented sector. That said, it has been our established practice that following a civil service pay adjustment, the Administration will adjust generally the subventions for those bodies with funding price-adjusted on the basis of formulae including a factor of civil service pay adjustment. This arrangement covers the majority of bodies receiving recurrent subventions from the Government, including the Hospital Authority, social welfare non-governmental organisations, and institutions funded by the University Grants Committee.

28. Subject to a final decision by the CE-in-Council and approval by the Finance Committee of the Legislative Council, we will increase the

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<sup>10</sup> The only restriction is that the pay of a NCSC staff cannot be more than the notional mid-point salary of a civil servant doing similar work.

subventions to the relevant bodies in line with the established practices. In general, the additional amounts of subventions will be calculated in accordance with the weighted average of the pay rise decided for the civil service (as was done in previous years). The weighted average of the 2008-09 civil service pay adjustment rates is 5.59%. It would be up to the individual subvented bodies, as employers, to decide whether to adjust the salaries of their own employees and, if so, the rate of adjustment. However, we would, through the relevant controlling officers, remind the relevant subvented bodies that the additional amounts of subventions from the Government are meant for pay adjustments for their staff, and that they should so spend the money.

**IMPLICATIONS**

29. The pay offers are in conformity with the Basic Law, including the provisions concerning human rights. They have no sustainability, productivity and environmental implications.

30. The financial implications for the civil service and subvented sector arising from the pay offers (if finally implemented) are as follows –

	\$ million
(a) Civil Service	3,105 <sup>11</sup>
(b) ICAC staff <sup>12</sup>	28
(c) Subvented Organizations	3,665 <sup>13</sup>
(d) Auxiliaries	10
(e) Judges and Judicial Officers	10
<b>Total</b>	<b>6,818</b>

31. The 2008 PTS findings, on which the pay offer is based, reflect the extent of pay increase generally awarded by employers in the private sector to their employees in the preceding year of 2 April 2007 to 1 April 2008 when labour market conditions had tightened. The Government, just like any other employer, has to compete for the manpower and expertise it needs, through offering appropriate salaries and other terms of employment. Currently, the civil service accounts for about 4% of the total workforce and

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11 The figure includes about \$365 million additional cost arising from pay adjustment for around 20 000 civil servants seconded to/working in trading funds, subvented and other public bodies. It also includes an estimated increase of \$169 million in pension payments for those who retire in 2008-09.

12 ICAC staff are not civil servants. However, it has been the Government's policy to extend the civil service pay adjustment to the ICAC.

13 This figure has excluded the financial implications arising from pay adjustment for civil servants seconded to/working in subvented bodies, which have been incorporated under item (a) above.

civil service emoluments account for about 8% of the overall employment remuneration in the economy. The civil service and employees in subvented organizations together account for around 16% of the overall employment remuneration in the economy.

32. The pay offers are broadly in line with the growth trend of overall labour productivity in the economy over the past five years 2003-2007, averaging at 4.7% per year (in real terms), and also the year-on-year labour productivity increase of about 4.8% (in real terms) in the first quarter of 2008. From the economic perspective, the inflationary implications of the pay offers (if implemented) would be small as it is supported by productivity improvements.

### **PUBLICITY**

33. The Secretary for the Civil Service has made the pay offers to the staff sides of the four central consultative councils earlier today (3 June 2008). A press release will be issued later today and a spokesperson will be available to answer media enquiries.

### **SUBJECT OFFICER**

34. Enquiries on this brief should be addressed to Mr. Chris Sun, Principal Assistant Secretary for the Civil Service (tel. 2810 3112).

Civil Service Bureau  
3 June 2008