

LEGISLATIVE COUNCIL BRIEF

Second Voluntary Retirement Scheme

INTRODUCTION

At the meeting of the Executive Council on 14 January 2003, the Council ADVISED and the Chief Executive ORDERED that the second Voluntary Retirement (VR) Scheme as set out in paragraphs 4 to 18 below should be approved.

JUSTIFICATIONS

2. As part of the collective efforts to tackle the budget deficit situation, Directors of Bureau (DoBs) have been critically examining various measures to identify savings. Some of their initiatives which involve re-engineering, re-organising and re-prioritising operations and service delivery will inevitably result in less staff positions required. With civil service personal emolument accounting for around 25% of Government's operating expenditure, any measures which help to reduce the civil service establishment will significantly contribute to reducing the fiscal deficit. Against this background, the Chief Executive (CE) announced in his 2003 Policy Address on 8 January 2003 a package of measures to reduce civil service expenditure. They include reducing the size of the civil service by 10% to around 160 000 by 2006-07; imposing a general recruitment freeze on the civil service with effect from 1 April 2003 and introducing a 2nd VR Scheme.

3. In 2000, we launched the first VR Scheme which enabled 59 designated grades with identified or anticipated surplus staff to retire from the service voluntarily with immediate retirement benefits and VR compensation. The approval of some 9 800 VR takers under the Scheme has helped reduce the civil service establishment, thereby assisting us in achieving a leaner civil service.

4. In view of the positive results of the first VR Scheme, a 2nd VR Scheme will be launched under Section 6A of the Pensions Ordinance and Section 13 of the Pension Benefits Ordinance in the first half of 2003 to provide an exit mechanism for identified or anticipated surplus staff in the civil service to leave voluntarily in order to facilitate DoBs to meet their target reduction in civil service establishment. These sections empower the Chief Executive in Council to approve a compensation scheme for the purposes of Section 6(1)(h) of the Pensions Ordinance and Section 11(1)(i) of the Pension Benefits Ordinance respectively. Such a compensation scheme -

- (a) shall apply to such officers as are specified in the scheme;
- (b) may provide for the payment of compensation, pension benefits and additional benefits to officers on their retirement, the commutation of pension benefits, the payment of death gratuities to dependants of officers, and for other matters relating thereto, other than in accordance with the pensions legislation; and
- (c) shall provide for the circumstances in which compensation and other benefits are payable under the scheme.

5. Based on initial indications to date from DoBs, there are some 200 grades with a strength of over 100 000 which they propose to include in the 2nd VR Scheme. However, we expect some fine-tuning to the number of proposed VR grades because some bureaux and departments are still working on further ways to re-engineer, re-organise and re-prioritise their operations with a view to further reducing their establishment. We will invite updated returns from DoBs again on the proposed list of VR grades before implementing the Scheme.

Features of the 2nd VR Scheme

6. The features of the 2nd VR Scheme will generally follow that of the first VR Scheme with some modifications. An outline of the general features of the 2nd VR Scheme are set out below.

Eligibility

7. The following eligibility criteria will be adopted as follows :
- (a) the Scheme will only apply to officers to whom Section 6A of the Pensions Ordinance (Cap.89) and Section 13 of the Pension Benefits Ordinance (Cap.99) apply and in the grades to be specified by the Secretary for the Civil Service (SCS) ^{Note 1}. Agreement officers are not eligible ^{Note 2};
 - (b) the Scheme will not apply to those officers who have tendered notice to retire or resign, have applied for early retirement or who have notified the Government in any manner of their intention to leave the service, or in the case of an officer on trial applied to revert to his former grade to which the Scheme does not apply;

^{Note 1} For the avoidance of doubt, an officer is an eligible officer only if he is in one of the following groups of officers :

- (a) an officer to whom Cap. 89 applies who is holding an established office as declared in the Pensions Ordinance (Established Offices) Order, Cap. 89;
- (b) an officer to whom Cap. 99 applies who is appointed to, and confirmed in, an established post as declared in the Pension Benefits Ordinance (Established Offices) Order, Cap. 99;
- (c) an officer to whom Cap. 99 applies who is holding, and who is not confirmed in, an established office as declared in the Pension Benefits Ordinance (Established Offices) Order, Cap. 99; and
- (d) an officer to whom Cap. 99 applies who is holding a non-established office.

^{Note 2} The following groups of officers are not eligible officers for the purposes of the Scheme:

- (a) an officer who is serving under an agreement, whether or not it is an agreement expressly providing for the payment of a gratuity; and
- (b) an officer appointed on month to month terms to fill time-limited or supernumerary posts or on terms of service which do not attract pension, gratuity or other allowance, or any other pension benefits under the pensions legislation.

- (c) the Scheme will not apply to those officers against whom disciplinary proceedings have been instituted or are contemplated to be taken, and the proceedings or actions may lead to the removal of the officers from the service or those officers who are to be dismissed or compulsorily retired from the service; and
- (d) the Scheme will not apply to those officers with five or less than five years active service before reaching normal retirement age. Active service shall be counted from the end date of the VR application period to the date the officer reaches his normal retirement age in accordance with the relevant pensions legislation applicable to the officer.

8. In essence, the Scheme will only be open to officers of grades specified by the SCS and whom SCS deems to be eligible to participate in the Scheme. Such officers may retire under the Scheme and receive benefits as provided for by the Scheme upon being invited to apply and being approved to retire under it.

Compensation Package

9. In the first VR Scheme, officers joining the Scheme received one month's final salary for every two complete years of service plus nine months' final salary, up to a maximum amount equivalent to 20 months' salary. This VR payment was also subject to the ceiling that the total package in lump sum, including the lump sum VR payment and the lump sum pension payment, should not exceed the commuted value of the pension benefits for which the officer would be eligible upon normal retirement plus six months' final salary. In view of Government's latest fiscal position, we consider it necessary to adjust downward the compensation package in the 2nd VR exercise. Notwithstanding this, the compensation package should be sufficiently attractive to encourage civil servants to apply.

10. The compensation package to be provided for the 2nd VR Scheme is recommended as follows-

- (a) the pension benefits for which an officer would be eligible as at the date of voluntary retirement, irrespective of whether or not he has attained the minimum age of retirement but subject to completion of the minimum qualifying length of service. This includes a commuted pension gratuity payable on the date of retirement and a monthly pension payable immediately after the officer's retirement;
- (b) a lump-sum payment (VR payment) to the officer on the date of his retirement. This is calculated on the basis of one month's salary for every two complete years of service ^{Note 3} of the officer; and
- (c) the VR payment is also subject to the ceiling that the amount of the VR payment ^{Note 4}, when added to the commuted value of the pension benefits for which the officer would be eligible upon retirement under the VR Scheme, will not exceed the commuted value of the pension benefits for which the officer would be eligible at his normal retirement age ^{Note 5}.

11. A table showing the amount of VR compensation in terms of months of salary is at **Annex A**.

12. It is further recommended that pension payment should not be granted to those VR takers who have less than 10 years of service counted

^{Note 3} As at the date of retirement under the Scheme after the officer has exhausted his accrued leave.

^{Note 4} For the purpose of calculating the VR payment, the amount of the officer's last substantive monthly salary will be used. The VR payment will be calculated only for every 2 complete years of service. No pro-rata payment for remainder of service less than 2 years will be provided. The compensation shall be calculated to the nearest HK\$1 dollar and all payment of compensation shall be made to the nearest HK\$1.

^{Note 5} For the purpose of computing the ceiling, the commuted value of pension benefits will be taken as the lump sum when 50% of the pension benefits is commuted, and the officer's highest annual pensionable emoluments calculated in accordance with the applicable pensions legislation at the date of voluntary retirement will be used. Lump sum VR payment + lump sum pension gratuity at VR commuted at 50% should be < or = lump-sum pension gratuity at normal retirement commuted at 50%.

from the date of their retirement from the civil service as these officers are not qualified for pension payment under the prescribed pensions legislation under normal circumstances^{Note 6}. Compensation under the VR Scheme shall only be payable to an eligible officer if his application for voluntary retirement is approved by the Government. The compensation is payable to the officer on the date of his retirement under the Scheme or as soon as practical thereafter.

13. Whilst the package is less generous than that under the first VR Scheme, we assess that it should still be sufficiently attractive to officers with some 12 years of service or more as they can receive a lump sum of over two years of salary immediately upon their departure (including lump sum pension and VR payment) and a monthly pension thereafter. Younger officers may be less interested. The package is expected to be most attractive to officers with 20 to 30 years of service.

Compensation Cost

14. With the exception of civil servants working in some of the public sector bodies and Trading Funds ^{Note 7} (see paragraph 18 below), as in the first VR Scheme, the VR compensation for all bureaux/departments will be funded from the center.

Recruitment Freeze

15. To ensure the cost-effectiveness of the Scheme, there will be a **five-year civil service recruitment freeze to the VR grades** counting from the date when the VR Scheme comes into operation as designated by SCS. Even if the general civil service recruitment freeze (referred to in paragraph 2 above) is lifted in due course, recruitment freeze to the VR grades will still apply.

^{Note 6} In other words, an officer to whom the pensions legislation applies who has been approved to retire under this Scheme will be eligible to be granted pension benefits immediately in accordance with the provision of the applicable pensions legislation, only if he has attained the minimum qualifying length of service.

^{Note 7} A Trading Fund is an accounting framework established under the Trading Fund Ordinance to enable a Government department to operate on a self-financing basis. There are five Trading Funds at present, namely, Land Registry, Company Registry, Post Office, Electrical and Mechanical Services Department and Office of the Telecommunications Authority

Deletion of Post

16. In the first VR exercise, departments/grades were permitted to delete whatever posts in the grade when a VR taker retired from the civil service. This enabled departments/grades to release more staff and maintain an appropriate grade structure. Although we could not realize the full cost savings in all cases in the short term, this arrangement allowed for maximum release of staff and achievement in long term salary savings as we would not need to carry the surplus or potential surplus staff at a higher payroll cost. However, in view of the current fiscal situation, it is recommended to tighten up the post deletion arrangements to require that a VR taker's post or a post of the same rank of the VR taker has to be deleted upon the departure of a VR taker. If in the event there are more VR takers in a particular rank than the number of posts which DoBs can delete in that rank, it is recommended that some flexibility should be given to allow them to consider deleting posts one rank below to facilitate departure of staff on condition that they can demonstrate substantial savings can still be derived and subject to seeking exceptional approval from the center.

MOD I Officers on Old Pension Scheme

17. Section 6(1)(h) of the Pensions Ordinance, under which the proposed VR Scheme derives its authority, does not cover officers on the Old Pension Scheme who are holding non-established offices. There are less than 300 such officers. As in the first VR Scheme, we propose to introduce administrative measures outside the VR Scheme to facilitate some of these officers to retire early under the prevailing regulations, if they so wish, and to receive the same benefits as if they were retiring under the VR Scheme. Specifically, it is proposed that for the MOD I officers aged 45 or above, they may, if they belong to a designated VR grade, apply for early retirement in accordance with the Pensions Ordinance and prevailing regulations within the same period when we invite eligible officers to apply for VR. If they meet the same selection and eligibility criteria for the VR Scheme, they will, when their applications for early retirement are approved, receive retirement benefits provided for by the Pensions Ordinance and an ex-gratia payment equivalent to the VR payment. This exceptional arrangement will only apply concurrently with the 2nd VR Scheme on a one-off basis.

The Case of Civil Servants Working in Trading Funds and Public Sector Bodies

18. Some public sector bodies, including Hospital Authority, Housing Authority, Hong Kong Monetary Authority (HKMA), Vocational Training Council (VTC) and the five Trading Funds have identified surplus staff in civil service grades in their organizations which they would like to delete. In the first VR exercise, we only included Hospital Authority surplus civil servants when there was a corresponding civil service surplus in other government departments. To achieve the aim of reducing the size of the civil service, we recommend that in principle surplus civil servants working in Housing Authority, Hospital Authority, HKMA, VTC and Trading Funds should be included in the 2nd VR irrespective of whether the grades are featured in the corresponding government departments subject to -

- (a) further study on the grades involved; and
- (b) HKMA and Trading Funds will have to be responsible for the VR payment arising from the introduction of the VR Scheme to civil servants working thereat as they are financially autonomous while the Government will fund the commuted pension and monthly pension benefits. Housing Authority will also be required to be responsible for the VR payments for civil servants funded by the authority. Such pension costs that will be borne by the Government will broadly be offset by reduced pension liability in future. While expenditure of Housing Authority and the Trading Funds is not part of Government expenditure, it counts towards public expenditure, and any reduction in their expenditure is relevant to our fiscal target of keeping public expenditure at 20% of GDP or lower. As for HKMA, its expenditure is neither Government expenditure nor public expenditure. Hospital Authority's and VTC's expenditure is part of Government expenditure and for the present exercise should be treated as if the organizations were government departments.

Financial Implications

19. The 2nd VR Scheme would incur pension expenditure (both the

commuted gratuity and the monthly payments) and compensation cost in the form of one-off VR payment. Pensions are officers' earned benefits and since we are not enhancing pensions, the Scheme does not involve additional cost in this respect. Pension expenditure is a statutory charge on General Revenue as provided for under the pensions legislation.

20. The total cost of the VR payments will depend on the number of VR takers, their current pay and their years of service. We will further liaise with DoBs/HoGs to confirm the final list of VR grades. For the purpose of estimating the financial implications, if we assume 7% (about 7 000 officers) of all staff in the proposed list of grades (involving 100 000 staff) opt for VR, and the average service length to be 22 years, the total cost of the VR compensation payments would be in the region of \$2.1 billion. The related pension expenditure would be \$6.1 billion for the commuted pension gratuities and recurrent pension payments of \$0.43 billion annually. On the other hand, departure of staff under the Scheme could lead to savings in salaries and allowances. Assuming 7 000 departures, we estimate that the notional gross savings in such costs would be around \$2.4 billion per year.

21. We consider it justified to introduce the 2nd VR Scheme at an additional cashflow of \$10 billion (comprising one-off costs of about \$2.1 billion for compensation and earlier payment of \$6.1 billion for lump sum pension, plus monthly pension of \$0.43 billion per year for four years from 2003-04 to 2006-07). Given that the lump sum pension and monthly pension are civil servants' statutory entitlement and the Government's liability, and in that respect they are not regarded as additional costs, we would be spending an additional \$2.1 billion for one-off compensation which will result in savings of \$2.4 billion per year in salaries thereafter. We have also done an analysis on the impact of the 2nd VR Scheme on cashflow for the period up to the end of 2006-07. The total VR related expenditure is estimated to be \$10 billion, as compared to a total savings of \$9.6 billion, in that period. From this perspective, the 2nd VR Scheme would in terms of cashflow add pressure to the fiscal situation in that period. However, there would be savings thereafter. We would not have to continue carrying the surplus or potential surplus staff at a higher payroll cost. On this basis, the costs of compensation and the pension payments under the proposed VR

Scheme can be paid back in around five years if all the savings of \$2.4 billion are not then spent on other expenditure. We envisage that given the significant reduction in operating expenditure that we are requiring from bureaux/departments, they will probably have to use most if not all of the savings from the scheme to deliver the reduction in operating expenditure funding. We have therefore concluded that there is no need for a separate mechanism for the center to clawing back part of such savings.

Civil Service Implications

22. The Staff Side would welcome the introduction of the 2nd VR Scheme as a measure to reduce the size of the civil service and to reduce public expenditure. However, there would be anxiety among officers remaining in the civil service on the already strained staffing resources. There has been rising demands from the community in recent years and serving officers are already coping hard with the increasing workload. They will also worry that the post deletion arrangement would have a negative impact on their promotion prospect. To alleviate their concerns, we would encourage departments to arrange briefing and counseling sessions to provide necessary assistance to staff. More than \$10 million has also been set aside under the three-year Training and Development Programme to organise training programmes for remaining staff of the VR grades to facilitate their adjustment to the change.

Basic Law, Human Rights, Sustainability and Environmental Implications

23. In so far as the eligibility criteria, specification of grades and decision-making in respect of individual applications for VR will exclude some officers from the benefits of the Scheme. However, the criteria, specifications and decisions would be justifiable in human rights terms if they pursue a legitimate aim and are a proportionate means of realizing that aim.

24. The Department of Justice considers that the proposed eligibility criteria (see paragraph 7 above) are justifiable. The proposal does not have major sustainability implication but will help reduce the budget deficit by

reducing the Government's operating expenditure. There are no environmental implications.

PUBLIC CONSULTATION

25. The initiatives to reduce the size of the civil service; impose a general civil service recruitment freeze and introduce the 2nd VR Scheme have been announced in the 2003 Policy Address as a package of measures to reduce civil service expenditure. We shall brief the staff sides, departmental management and the LegCo Panel on Public Service on the proposals.

26. Separately, we would need to seek the approval of the Finance Committee of the Legislative Council for the requisite financial commitment on the basis of the list of grades specified by SCS for the application of the 2nd VR Scheme.

PUBLICITY

27. We will brief the LegCo Panel on Public Service on 15 January 2003. We shall have ready a line-to-take for deployment. A spokesman will also be available to answer enquiries.

OTHERS

28. Enquiries relating to this brief may be directed to Mr Vincent Liu, Principal Assistant Secretary for the Civil Service at 2810 2746.

Civil Service Bureau
14 January 2003

VR compensation package under
the Second VR Scheme

Years of Service	2 nd VR Package
	Monthly Salary
2	1 month
4	2 months
6	3 months
8	4 months
10	5 months
12	6 months
14	7 months
16	8 months
18	9 months
20	10 months
22	11 months
24	12 months
26	13 months
28	14 months
30	11 months
32	8 months
34	5 months
36	2 months

2nd VR Package : 1 month's final salary for every 2 complete years of service, capped at total package in lump sum not exceeding the lump sum pension at normal retirement (50% commutation)

Note: Assuming VR takers join the service at the age of 20 and are under the New Pension Scheme. In addition to the above VR payment, VR takers with not less than 10 years of service are eligible for pension benefits.