

## **CHAPTER 6**

### **Student Financial Assistance Agency**

**Financial assistance schemes for  
post-secondary and tertiary students**

**Audit Commission  
Hong Kong  
27 October 2009**

*This audit review was carried out under a set of guidelines tabled in the Provisional Legislative Council by the Chairman of the Public Accounts Committee on 11 February 1998. The guidelines were agreed between the Public Accounts Committee and the Director of Audit and accepted by the Government of the Hong Kong Special Administrative Region.*

Report No. 53 of the Director of Audit contains 11 Chapters which are available on our website at <http://www.aud.gov.hk>.

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# FINANCIAL ASSISTANCE SCHEMES FOR POST-SECONDARY AND TERTIARY STUDENTS

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## **PART 1: INTRODUCTION**

1.1 This PART describes the background to the audit and outlines the audit objectives and scope.

### **Background**

1.2 It is the Government's policy to ensure that no student is deprived of education due to lack of means. To achieve this policy objective, the Government has designed a variety of financial assistance schemes to assist all qualified students in need of financial assistance to achieve the education level they aspire to. Financial assistance is provided under various financial assistance schemes to students of different education levels, including attendees of primary and secondary schools, post-secondary and tertiary institutions, and training bodies providing continuing education.

1.3 The Student Financial Assistance Agency (SFAA) is responsible for administering the financial assistance schemes. It is the aim of the SFAA to administer the schemes efficiently and cost-effectively to ensure that timely and appropriate financial assistance is provided to the successful applicants. An organisation chart of the SFAA as at 30 June 2009 is shown at Appendix A.

### **Financial assistance schemes for post-secondary and tertiary students**

1.4 Five financial assistance schemes provide support to eligible students (Note 1) pursuing recognised courses in post-secondary and tertiary institutions, and persons pursuing specified continuing and professional education courses provided in Hong Kong by registered schools, non-local universities and recognised training bodies. The five financial assistance schemes are:

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**Note 1:** *Eligible students should have the right of abode in Hong Kong or have resided or have had a home in Hong Kong continuously for three complete years prior to the commencement of the course.*

*Means-tested grant and loan schemes*

- (a) **Tertiary Student Finance Scheme — Publicly-funded Programmes (TSFS)** for full-time students pursuing University Grants Committee-funded or publicly-funded programmes in specified institutions (Note 2);
- (b) **Financial Assistance Scheme for Post-secondary Students (FASP)** for full-time students aged 25 or below pursuing locally-accredited (Note 3) self-financing post-secondary education programmes;

*Non-means-tested loan schemes*

- (c) **Non-means-tested Loan Scheme (NLS)** for students covered under the TSFS;
- (d) **Non-means-tested Loan Scheme for Post-secondary Students (NLSPS)** for students covered under the FASP; and
- (e) **Extended Non-means-tested Loan Scheme (ENLS)** for students not covered under the TSFS and FASP, and persons pursuing specified continuing and professional education courses provided in Hong Kong by registered schools, non-local universities and recognised training bodies.

1.5 In the 2008-09 financial year, financial assistance provided under the five schemes amounted to \$2,665 million. Details are shown in Table 1.

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**Note 2:** *The institutions covered under the TSFS are the Chinese University of Hong Kong, the City University of Hong Kong, the Hong Kong Baptist University, the Hong Kong Institute of Education, the Hong Kong Polytechnic University, the Hong Kong University of Science and Technology, the Lingnan University, the University of Hong Kong, the Hong Kong Academy for Performing Arts, the Hong Kong Institute of Vocational Education and the Prince Philip Dental Hospital.*

**Note 3:** *Locally-accredited programmes refer to those included in the Register of Locally-accredited Programmes approved by the Secretary for Education.*

Table 1

**Financial assistance provided under five schemes  
(2008-09 financial year)**

Scheme	Grant (\$ million)	Loan (\$ million)	Total (\$ million)
TSFS	788	290	1,078
FASP	489	118	607
NLS	N.A.	201	201
NLSPS	N.A.	416	416
ENLS	N.A.	363	363
<b>Total</b>	<b>1,277</b>	<b>1,388</b>	<b>2,665</b>

*Source: SFAA records*

*Remarks: Expenditure for grants is funded under the General Revenue Account and expenditure for loans is funded under the Loan Fund.*

***Means-tested grant and loan schemes***

1.6 ***TSFS.*** The TSFS, formerly known as the Local Student Finance Scheme, was introduced in 1969 to provide financial assistance in the form of grants and/or loans to needy students. The grant is to cover the student's tuition fees, academic expenses and compulsory student union fees, and the loan is to cover the student's living expenses. The loan is interest-free during the study period but interest at the rate of 2.5% per annum will be charged as from the commencement of repayment after the student's graduation or termination of study (see para. 3.2).

1.7 ***FASP.*** To support students pursuing locally-accredited self-financing post-secondary education programmes, the Government introduced the FASP in the 2001/02 academic year (Note 4). The financial assistance provided under the FASP had changed on several occasions since its introduction, as follows:

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**Note 4:** *Unless otherwise specified, all years mentioned hereinafter refer to academic years.*

- (a) prior to 2006/07, students who passed the means test and were eligible for 100% assistance would be provided with a full grant to cover tuition fees subject to a specified ceiling. Those who passed the means test but were not eligible for 100% assistance would be provided with a loan according to a sliding scale to cover the tuition fees;
- (b) with effect from 2006/07, students who failed to obtain a full grant might receive a partial grant according to a sliding scale to meet tuition fees (subject to a specified ceiling) and academic expenses. However, they would not be provided with a loan; and
- (c) starting from 2008/09, loans at the same level as those under the TSFS were introduced to cover the students' living expenses with the same terms and conditions as those under the TSFS.

1.8 Applications for financial assistance under the TSFS or FASP are assessed by a two-tier means test to determine their levels of financial assistance, as follows:

- (a) ***Income test.*** The assessment is made according to an adjusted family income formula. The adjusted family income of an applicant is then applied to a ready reckoner to determine the amount of grant/loan which he may receive; and
- (b) ***Asset test.*** The amount of grant/loan calculated under the income test is further adjusted according to a sliding scale of discount factors based on the net asset value per family member of the applicant.

1.9 The applicant is required to sign an undertaking and arrange an indemnifier for taking out the loan. FASP applicants also need to do the same if they wish to accept the grant.

#### ***Non-means-tested loan schemes***

1.10 ***NLS.*** The Government introduced the NLS in 1998/99 to complement the TSFS. The NLS provides an alternative channel of finance to students who prefer to pursue their tertiary studies on their own without relying on family support, and those who do not wish to or fail to go through the means test under the TSFS. Students who receive financial assistance under the TSFS may apply for **NLS loan to settle tuition fees** up to the difference between the TSFS maximum financial assistance and the amount they may receive, subject to the NLS loan maximum (equivalent to the tuition fees payable) not being exceeded. Students who fail to obtain TSFS assistance or have not applied for it may apply for NLS loan up to the amount of their tuition fees. Borrowers are required to sign an undertaking and arrange an indemnifier for taking out the loans.



1.11 **ENLS.** To encourage adult and continuing education, the NLS was extended in 1998/99 and 2000/01 to cover students pursuing local post-secondary education programmes and persons pursuing specified continuing and professional education courses operated locally by registered schools, non-local universities and recognised training bodies (the extended scheme is referred to as the ENLS). They may apply for an **ENLS loan to settle tuition fees of eligible full-time or part-time courses.** Borrowers are required to sign an undertaking and arrange an indemnifier for taking out the loans.

1.12 **NLSPS.** The NLS was further extended in 2001/02 to provide non-means-tested loans to students covered under the FASP (the extended scheme is referred to as the NLSPS). Students who apply for assistance under the FASP may concurrently apply for **NLSPS loans to top up their assistance under the FASP to meet tuition fees, academic expenses and living expenses.** Students who fail to obtain FASP assistance or have not applied for FASP assistance may apply for NLSPS loans to cover the tuition fees, academic expenses and living expenses. Borrowers are required to sign an undertaking and arrange an indemnifier for taking out the loans.

1.13 The non-means-tested loan schemes are operated on a no-gain-no-loss and full-cost-recovery basis. On this basis:

- (a) interest on non-means-tested loans is charged at the Government's no-gain-no-loss rate (Note 5), plus a risk-adjusted factor (RAF) of 1.5% per annum. The RAF covers the Government's risk in disbursing unsecured loans. As at 1 June 2009, the interest rate for such loans was 3.599%;
- (b) interest is charged on the capital once the loan has been drawn down and on the reducing loan balance throughout the repayment period (see para. 3.2); and
- (c) an administrative fee, calculated on a full-cost-recovery basis, is charged upon application and annually thereafter until full repayment of the loan.

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**Note 5:** *The no-gain-no-loss interest rate is set with reference to the average best lending rate of the note-issuing banks. The Director of Accounting Services will review the no-gain-no-loss rate by the end of each month according to changes in the average best lending rate in the month and will adjust the rate with effect from the first day of the following month.*

## **Joint Committee on Student Finance**

1.14 In 1969, a Joint Universities Committee on Student Finance was established to advise on the operation of the TSFS. Subsequent to the changes in the scope of the TSFS, the Committee was renamed the Joint Committee on Student Finance (JCSF) in 1981. The JCSF advises the Government on the operation of the TSFS and NLS to ensure that their objectives and the needs of the community are met. The JCSF comprises members of the community, staff and student representatives of the institutions, the Controller, Student Financial Assistance Agency, and the Secretary-General, University Grants Committee.

## **Audit review**

1.15 The Audit Commission (Audit) has recently conducted a review of the SFAA's administration of the five financial assistance schemes, focusing on the following areas:

- (a) processing of applications (PART 2);
- (b) loan repayments (PART 3);
- (c) financial assistance of means-tested schemes (PART 4); and
- (d) interest rates on loans (PART 5).

The review has found that there is room for improvement in the above areas, and has made a number of recommendations to address the issues.

## **Acknowledgement**

1.16 Audit would like to acknowledge with gratitude the full cooperation of the staff of the SFAA during the course of the audit review.

## PART 2: PROCESSING OF APPLICATIONS

2.1 This PART examines the processing of applications for financial assistance and suggests measures for improvement.

### Processing procedures

2.2 Up to 31 March 2009, the SFAA had received 80,670 applications for 2008/09 under the five financial assistance schemes. A breakdown of these applications is shown in Table 2.

**Table 2**  
**Applications for financial assistance for 2008/09**  
**(31 March 2009)**

Scheme	Number	Percentage
TSFS	30,944	38%
FASP	21,938	27%
NLS	6,265	8%
NLSPS	11,356	14%
ENLS	10,167	13%
<b>Total</b>	<b>80,670</b>	<b>100%</b>

*Source: SFAA records*

### *Means-tested grant and loan schemes*

2.3 Applications for means-tested grants and loans under the TSFS and FASP are processed as follows:

- (a) **Preliminary checking.** Students submit application forms together with photocopies of supporting documents to their institutions. The institutions carry out preliminary checking to ensure that the forms are duly completed and photocopies of supporting documents are attached, and forward them to the SFAA for further processing;
- (b) **Vetting.** SFAA vetting staff comprise Processing Officers (ranked at Assistant Clerical Officer level) and Investigation Officers (ranked at Senior Clerical Officer level). Applications are vetted by Processing Officers. For complex applications, they are vetted by Investigation Officers. Vetting staff verify the family incomes and assets stated in the applications, and assess the financial

assistance to be offered to the applicants. Processing Officers perform “paper vetting” to verify information in the application forms. They may seek clarification from the applicants when necessary. In vetting applications, Investigation Officers interview the applicants and/or their parents;

- (c) **Counter-checking.** Monthly and year-end counter-checks, which mainly involve re-performing the vetting staff’s work, are conducted on selected applications as follows:
  - (i) **Monthly counter-checks.** Before issuing notifications of application results to the applicants, monthly counter-checks are conducted on selected applications by supervisors of the vetting staff (Note 6); and
  - (ii) **Year-end counter-checks.** Towards the end of each application cycle, usually in the period March to May, successful applications are randomly selected (Note 7) for counter-checking by Processing Officers;
- (d) **Payment.** Financial assistance is paid to the applicants who accept the offered assistance; and
- (e) **Authentication.** A number of successful applications are selected for authentication by Investigation Officers. They make home visits to assess directly the family conditions of the applicants, and to verify the information they have provided.

#### ***Non-means-tested loan schemes***

2.4 Applications for non-means-tested loans under the NLS, NLSPS and ENLS are processed in a simpler way because means test and authentication of applications are not necessary for assessing the loan amount to be offered to the applicants (see paras. 1.10 to 1.12). After the institutions’ preliminary checking of the applications (only for the NLS and NLSPS, since ENLS applications are submitted directly to the SFAA), vetting staff perform “paper vetting” to verify the information of the applicants (e.g. identity card, admission letter issued by the institution and the applicant’s bank account number). Applications are counter-checked and loans are paid to the applicants or their institutions.

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**Note 6:** *Vetting work performed by Processing Officers is counter-checked by Investigation Officers or clerical officers of the support team/authentication team. Vetting work performed by Investigation Officers is counter-checked by the leader of the vetting team (ranked at Executive Officer I level).*

**Note 7:** *The following applications are not selected for year-end counter-checking: (a) applications checked in the monthly counter-checks or by the Internal Audit Team; (b) applications for which Investigation Officers interviewed the applicants during the vetting stage or authentication stage; and (c) applications for which the applicants applied for a review of the application results by providing additional information or further justifications.*

## Vetting and counter-checking of TSFS and FASP applications

2.5 The results of monthly and year-end counter-checks indicated that there were errors (e.g. failure to include bonus as part of the income) in vetting TSFS and FASP applications for 2006/07 to 2008/09 by the vetting staff (i.e. vetting errors). Details are shown in Tables 3 and 4.

**Table 3**  
**Vetting errors identified in monthly counter-checks**  
**(31 March 2009)**

	2006/07		2007/08		2008/09	
	TSFS	FASP	TSFS	FASP	TSFS	FASP
(a) Number of applications received	35,831	17,826	32,413	20,064	30,944	21,938
(b) Number of applications counter-checked for the year	4,702	3,258	3,978	3,530	4,280	2,972
(c) Percentage of applications counter-checked (c) = (b)/(a) × 100%	13.1%	18.3%	12.3%	17.6%	13.8%	13.5%
(d) Number of applications with vetting errors	188	21	105	13	68	34
(e) Vetting error rate (e) = (d)/(b) × 100%	<b>4%</b>	<b>0.6%</b>	<b>2.6%</b>	<b>0.4%</b>	<b>1.6%</b>	<b>1.1%</b>
(f) Number of applications with incorrectly assessed assistance (Note)	3	3	9	5	3	15
(g) Percentage of applications with incorrectly assessed assistance (g) = (f)/(b) × 100%	0.1%	0.1%	0.2%	0.1%	0.1%	0.5%

Source: SFAA records

Note: Not every vetting error led to incorrect assessment of assistance because assessment was made according to the income and asset groups of the applicant which covered a range of income/asset levels.

**Table 4**  
**Vetting errors identified in year-end counter-checks**  
**(2006/07 to 2008/09)**

	2006/07		2007/08		2008/09	
	TSFS	FASP	TSFS	FASP	TSFS	FASP
(a) Number of successful applications	31,128	13,771	28,431	15,751	26,866	12,444
(b) Number of applications counter-checked for the year	3,145	1,736	2,821	603	2,842	(Note 1)
(c) Percentage of applications counter-checked (c) = (b)/(a) × 100%	10.1%	12.6%	9.9%	3.8%	10.6%	
(d) Number of applications with vetting errors	309	83	287	29	179	
(e) Vetting error rate (e) = (d)/(b) × 100%	<b>9.8%</b>	<b>4.8%</b>	<b>10.2%</b>	<b>4.8%</b>	<b>6.3%</b>	
(f) Number of applications with incorrectly assessed assistance (Note 2)	29	5	13	1	6	
(g) Percentage of applications with incorrectly assessed assistance (g) = (f)/(b) × 100%	0.9%	0.3%	0.5%	0.2%	0.2%	

Source: SFAA records

Note 1: According to the SFAA, the 2008/09 year-end counter-check was not conducted owing to manpower and time constraints.

Note 2: Not every vetting error led to incorrect assessment of assistance because assessment was made according to the income and asset groups of the applicant which covered a range of income/asset levels.

2.6 The Internal Audit Team of the SFAA also carries out counter-checks of selected TSFS and FASP applications. The results of the counter-checks for 2006/07 to 2008/09 are shown in Table 5.

**Table 5**  
**Vetting errors identified by Internal Audit Team**  
**(2006/07 to 2008/09)**

	2006/07		2007/08		2008/09	
	TSFS	FASP	TSFS	FASP	TSFS	FASP
(a) Number of applications counter-checked for the year	300	72	300	70	300	100
(b) Number of applications with vetting errors	8	3	14	5	16	4
(c) Vetting error rate (c) = (b)/(a) × 100%	2.7%	4.2%	4.7%	7.1%	5.3%	4%
(d) Number of applications with incorrectly assessed assistance (Note)	1	1	3	0	2	0
(e) Percentage of applications with incorrectly assessed assistance (e) = (d)/(a) × 100%	0.3%	1.4%	1%	0%	0.7%	0%

Source: SFAA records

Note: Not every vetting error led to incorrect assessment of assistance because assessment was made according to the income and asset groups of the applicant which covered a range of income/asset levels.

### **Audit observations and recommendations**

2.7 The purposes of counter-checks are to ensure that the vetting work is in compliance with the SFAA's guidelines, to maintain the consistency of processing of applications and to ensure the accuracy in assessing the amount of financial assistance. The results of the counter-checks (see Tables 3 to 5) indicate that there is room for improvement in the vetting and counter-checking work (see paras. 2.8 to 2.10).

*Effectiveness of vetting work*

2.8 The error rates for the vetting work were as high as 10.2% for the TSFS and 7.1% for the FASP. **The high vetting error rates indicate that there is room for improving the effectiveness of the vetting work performed by the vetting staff.**

*Need to conduct an overall review of counter-checks*

2.9 The objectives of the monthly and year-end counter-checks are to ensure that the applications are assessed fairly and correctly, and to monitor the effectiveness of the work of the vetting staff. The vetting error rates found in the monthly counter-checks (1.6% to 4% for the TSFS and 0.4% to 1.1% for the FASP) were substantially lower than those found in the year-end counter-checks (6.3% to 10.2% for the TSFS and 4.8% for the FASP). Upon enquiry, the SFAA informed Audit in August 2009 that:

- (a) monthly counter-checks emphasised on the monitoring of internal consistency and vetting standard of vetting staff. Not all mistakes were recorded as errors; and
- (b) year-end counter-checks were conducted by Processing Officers. They were required to record all the mistakes spotted. Therefore, the vetting error rates found in the year-end counter-checks were higher than those found in the monthly counter-checks.

2.10 **In view of the significant difference in the vetting error rates found in the two types of counter-checks, the SFAA needs to conduct an overall review of the counter-checks, covering aspects such as the cost-effectiveness in achieving the objectives and the recording of vetting errors.**

*Audit recommendations*

2.11 **Audit has recommended that the Controller, Student Financial Assistance Agency should:**

- (a) **investigate the reasons for the high rates of vetting errors and take measures to improve the effectiveness of the vetting work; and**
- (b) **conduct an overall review of the monthly and year-end counter-checks (e.g. by evaluating their cost-effectiveness in achieving the objectives).**



## Response from the Administration

2.12 The **Controller, Student Financial Assistance Agency** agrees with the audit recommendations. She has said that:

- (a) to ensure the vetting process is conducted in an accurate, fair and consistent manner, the SFAA has put in place several check points at different stages of the vetting process for internal monitoring. It is noted that the errors recorded in the monthly and year-end counter-checks as well as Internal Audit checks in Tables 3 to 5 consisted of failures to follow procedures (e.g. failure to seek supervisor's endorsement), vetting mistakes (e.g. failure to count bonus as income) and minor clerical errors (e.g. errors in transcribing figures). Generally, less than 1% of the total cases counter-checked in the past three years has led to wrong calculation of financial assistance. The SFAA will explore measures to retain experienced staff and to enhance the training programme for vetting staff to further improve the effectiveness of the vetting work; and
- (b) the SFAA will conduct an overall review of the monthly and year-end counter-checks with a view to enhancing their cost-effectiveness.

## Authentication of applications

2.13 The SFAA performs authentication work on selected successful TSFS and FASP applications (Note 8). The results of the authentication exercises conducted on applications for 2006/07 to 2008/09 are shown in Table 6.

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**Note 8:** *In performing authentication of an application, the Investigation Officer may need to extend the work to cover applications submitted by the applicant in previous years and/or applications submitted by his siblings in the current year and/or previous years.*

**Table 6**  
**Authentication of applications**  
**(31 March 2009)**

	2006/07		2007/08 (Note 1)		2008/09 (Note 1)	
	TSFS	FASP	TSFS	FASP	TSFS	FASP
(a) Number of successful applications	31,128	13,771	28,431	15,751	26,866	12,444
(b) Number of applications selected for authentication	1,679	1,074	1,494	1,147	1,368	1,172
(c) Percentage of applications selected for authentication (c)=(b)/(a)×100%	5.4%	7.8%	5.3%	7.3%	5.1%	9.4%
(d) Number of applications with completed authentication work (Note 2)	1,679	1,074	1,371	1,076	257	128
(e) Number of applications with discrepancies (Note 3)	255	132	197	197	38	26
(f) Discrepancy rate (f)=(e)/(d)×100%	<b>15.2%</b>	<b>12.3%</b>	<b>14.4%</b>	<b>18.3%</b>	<b>14.8%</b>	<b>20.3%</b>
(g) Financial assistance overpaid (\$'000)	<b>5,382</b>	<b>1,664</b>	<b>2,276</b>	<b>2,609</b>	<b>105</b>	<b>229</b>
(h) Number of cases referred to the Police for action	12	9	3	15	0	0

Source: SFAA records

Note 1: As at 31 March 2009, authentication work for 2007/08 and 2008/09 applications had not yet been fully completed.

Note 2: Authentication work for an application is classified as "completed" when the authentication report compiled by the Investigation Officer has been countersigned by the supervisor.

Note 3: Examples of discrepancies included understatement or omission of employment income or bank deposits.

## Audit observations and recommendations

### *High discrepancy rates*

2.14 **The discrepancy rates of over 10% as shown in Table 6 were on the high side.** For 2006/07 and 2007/08 applications, the rates for the TSFS were 15.2% and 14.4% respectively. For the FASP, the rates increased from 12.3% in 2006/07 to 18.3% in 2007/08 (Note 9).

### *Substantial amounts of overpaid financial assistance*

2.15 **As shown in Table 6, the amounts of overpaid financial assistance were substantial.** For 2006/07 and 2007/08 applications, the amounts for the TSFS were \$5.4 million and \$2.3 million respectively. For the FASP, the amounts increased from \$1.7 million in 2006/07 by 53% to \$2.6 million in 2007/08 (see Note 9).

2.16 At the JCSF meeting held in July 2003, the Chairman of the JCSF commented that if the discrepancies and overpaid amounts were projected to all the applications, the problem would be very serious. In May 2008, JCSF members were informed that the projected amount of overpaid assistance in respect of successful TSFS applications for 2005/06 was \$94.7 million (Note 10).

### *Need to review the authentication mechanism*

2.17 At the JCSF meeting held in January 2008, members expressed concern about the discrepancy rate and the amount of overpaid assistance found in the 2006/07 authentication exercise for the TSFS. The SFAA reported that since 2000/01, it had adopted the Independent Commission Against Corruption's recommendation of

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**Note 9:** *The data for 2008/09 applications were not included in this comparison because only 15% of the authentication work had been completed as at 31 March 2009.*

**Note 10:** *The projection, based on the results of the authentication work and the total number of successful applications, was calculated as follows:*

$$(A) \times (B) \times (C) = \$94.7 \text{ million}$$

where:

(A) = the total number of successful applications, which was 34,035

(B) = the discrepancy rate, which was 11.4%

(C) = the average amount of overpaid assistance per discrepancy case, which was \$24,395

authenticating more successful applications in each authentication exercise (Note 11). The SFAA considered that it was an opportune time to:

- (a) review the cost-effectiveness of the authentication work in safeguarding public money; and
- (b) consider whether to step up action to bring about a stronger deterrent effect against omission of information.

2.18 Since March 2008, a Senior Treasury Accountant has taken up the post of Deputy Controller and headed the new Default Unit. She was tasked to conduct a comprehensive review on the loan recovery procedures of the Default Unit and to put in place improvement measures. She was also tasked to review the authentication process. Upon enquiry, the SFAA informed Audit in July 2009 that, due to the need to accord higher priority to reviewing the loan recovery process and putting in place the streamlined procedures to expedite the referral of default cases to the Department of Justice (DoJ), the review on authentication mechanism had been temporarily deferred.

***Need to select more high-risk cases for authentication***

2.19 According to the SFAA guidelines:

- (a) 5% of the successful applications will be selected for authentication; and
- (b) the applications that will be selected are:
  - (i) all doubtful applications identified in the current year during vetting, review (see Note 7 to para. 2.3(c)(ii)) and year-end counter-checking; and
  - (ii) a random sample of all applications with assessed assistance over \$5,000 each, emphasising on the high-level assistance cases (i.e. the grant exceeds 50% of the tuition fees).

2.20 The numbers of 2008/09 applications selected for authentication using the above selection criteria are shown in Table 7.

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**Note 11:** *In 1999, after a study on the operation of the TSFS, the Independent Commission Against Corruption recommended that the SFAA should randomly select 3% to 5% of all successful applications for authentication. Since 2000/01, the SFAA has selected 5% (previously only 1% to 2%) of the successful applications for authentication after the reorganisation of the SFAA and the provision of additional staff.*

**Table 7**  
**Authentication of 2008/09 applications**  
**(31 March 2009)**

	TSFS		FASP	
	Number	Percentage	Number	Percentage
Doubtful applications	6	0.4%	1	0.1%
Randomly selected applications	1,362	99.6%	1,171	99.9%
<b>Total</b>	<b>1,368</b>	<b>100%</b>	<b>1,172</b>	<b>100%</b>

*Source: Audit analysis of SFAA records*

2.21 In its business process re-engineering report issued in October 2006, the Efficiency Unit recommended that the SFAA should collect data to enable risk profiling of applications and cost-efficient targeting of high-risk applications for authentication (Note 12). However, Audit noted that the SFAA had not adopted such a risk-based approach to selecting high-risk cases for authentication.

#### ***Timeliness of authentication work***

2.22 According to the SFAA guidelines:

- (a) applications are selected for authentication and assigned to Investigation Officers on a monthly basis;
- (b) the Investigation Officers should pay home visits without undue delay;
- (c) authentication reports should be compiled by the Investigation Officers within two weeks after the home visits. For complex cases requiring in-depth study and/or solicitation of further information, the authentication reports should be compiled within six weeks after the home visits; and

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**Note 12:** *The Efficiency Unit also recommended the development of a new computer system to replace the existing computer systems and an organisational restructuring. According to the implementation plan of the SFAA, subject to availability of funds, the new computer system and the organisational restructuring would be fully implemented by 2015.*

- (d) authentication reports should be countersigned by supervisors of the Investigation Officers within two weeks.

2.23 The progress of authentication work on applications for 2007/08 and 2008/09 is shown in Table 8.

**Table 8**  
**Progress of authentication work**  
**(31 March 2009)**

Progress of authentication work	Number of applications			
	2007/08		2008/09	
	TSFS	FASP	TSFS	FASP
Completed	1,371 (92%)	1,076 (94%)	257 (19%)	128 (11%)
Not completed	123 (8%)	71 (6%)	1,111 (81%)	1,044 (89%)
<b>Total</b>	<b>1,494</b> <b>(100%)</b>	<b>1,147</b> <b>(100%)</b>	<b>1,368</b> <b>(100%)</b>	<b>1,172</b> <b>(100%)</b>

Source: *Audit analysis of SFAA records*

2.24 As at 31 March 2009, authentication work for 6% and 8% of the 2007/08 applications, and 81% and 89% of the 2008/09 applications had not yet been completed (see Table 8). The SFAA did not have a detailed work plan specifying the expected completion date of the authentication work. Timeliness of authentication work is important to have an effective deterrent effect, in particular on current students who will submit applications in the coming years. **The SFAA needs to closely monitor the progress of the authentication work to ensure that it is completed in a timely manner.**

*Need to improve investigation skills of authentication staff*

2.25 The effectiveness of authentication work in identifying discrepancy cases is important in ensuring that financial assistance is properly assessed and paid to needy students. Authentication work is performed by Investigation Officers who are ranked at Senior Clerical Officer level. The SFAA issues guidelines to assist Investigation Officers in performing authentication work, and provides a training course and on-the-job training to new Investigation Officers. However, the SFAA does not have a training plan to regularly provide training to Investigation Officers to improve their investigation skills and techniques. **By devising a training plan to equip the authentication staff with better**

**investigation skills and techniques, the SFAA can improve the effectiveness of the authentication work and help ensure that public money is not abused.**

2.26 Audit has noted that the Social Welfare Department employs part-time investigation staff with experience in law enforcement departments for handling applications under the social security assistance schemes. The SFAA may consider drawing on the Department's experience to employ staff with suitable experience to help improve the authentication work.

#### *Audit recommendations*

2.27 **Audit has recommended that the Controller, Student Financial Assistance Agency should:**

- (a) **in view of the high discrepancy rates and the substantial amounts of overpaid financial assistance, step up efforts in conducting a review of the authentication mechanism;**
- (b) **take effective measures to enable risk profiling of applications and cost-efficient targeting of high-risk applications for authentication;**
- (c) **compile a detailed work plan for authentication of each year's applications, specifying the target completion date of the work;**
- (d) **identify the training needs of the authentication staff and devise a training plan to provide them with regular training to improve their investigation skills; and**
- (e) **consider employing staff with suitable investigation experience to assist in the authentication work.**

#### **Response from the Administration**

2.28 The **Controller, Student Financial Assistance Agency** agrees with the audit recommendations. She has said that:

- (a) to ensure the prudent use of public money, the SFAA has in place a mechanism to authenticate the applications for various financial assistance schemes. Recognising the need to review the present authentication process, a Senior Treasury Accountant has been deployed to undertake the review in addition to her other duties as head of the Default Unit. The review on the authentication process will be conducted in 2010;

- (b) to ensure the prudent use of public money, the SFAA will re-examine the sampling and selection processes of the existing authentication mechanism with a view to identifying high-risk applications;
- (c) the SFAA will formulate a detailed work plan for authentication, specifying the target completion date of the authentication exercise;
- (d) at present, training on authentication is incorporated in a structured 5-day induction training programme. Relevant manuals are provided. On-the-job training and experience sharing sessions are also arranged. The SFAA will review the training programme with a view to further enhancing the quality of the programme; and
- (e) the SFAA will consider the feasibility of employing staff with suitable investigation experience to assist in the authentication work.

### **Measures to ensure correctness and completeness of information**

2.29 Accuracy of the assessed financial assistance depends on the correctness and completeness of information provided by the applicants about their family incomes and assets. Omissions (including understatements) of family incomes and assets in the applications may be due to:

- (a) the applicants' carelessness in completing the application form or misunderstandings on the requirements of the SFAA about information to be provided; or
- (b) the applicants' intention to obtain extra financial assistance which they are not entitled to.

In addition to vetting and authentication of applications, the SFAA takes a number of measures to prevent applicants from providing incorrect or incomplete information (preventive measures) and to handle applications with incorrect or incomplete information (punitive measures).

### **Audit observations and recommendations**

#### ***Adequacy of preventive measures***

2.30 The SFAA has taken the following preventive measures:

- (a) information leaflets are distributed to students through the institutions to remind applicants to provide true and complete information for their applications. The same message is also highlighted in the application forms and guidance notes;



- (b) samples of correctly completed application forms are promulgated by the SFAA on its website; and
- (c) a checklist of the required documents and a list of the common omissions are issued to assist applicants in completing application forms.

2.31 The discrepancy rates found in the authentication work were consistently high (over 10%) and the amounts of overpaid assistance were substantial (see paras. 2.14 and 2.15). **The SFAA needs to take more proactive measures to ensure that applicants provide correct and complete information in the applications.** In this connection, the SFAA may consider performing more publicity work targeting at both the students and their parents to remind them of the importance of providing correct and complete information.

#### *Effectiveness of punitive measures*

2.32 According to the SFAA guidelines, for applications with incorrect or incomplete information, the SFAA will:

- (a) for serious omission cases, reject the applications and take recovery action for all assistance paid; and
- (b) for other cases, issue warning letters and take recovery action for the assistance overpaid due to incorrect or incomplete information.

For serious omission cases and cases involving suspected forged documents, the SFAA will consider referring them to the Police for investigation and prosecution.

2.33 ***Warning letters and recovery of overpaid assistance.*** Audit considers that the measure of simply issuing warning letters and recovering the overpaid assistance is rather lenient. There may not be sufficient deterrent effect since the students concerned would not need to bear any real cost for the omissions. **The SFAA needs to review the effectiveness of such measure in ensuring that applicants provide correct and complete information in their applications.**

2.34 ***Referral to the Police.*** If there is prima facie evidence of obtaining financial assistance by deception, the SFAA should refer the case to the Police for criminal investigation. This would impress upon potential applicants the seriousness of such acts that could result in legal proceedings against the offenders.

2.35 Audit noted that a total of 394 applications (i.e. 197 applications each for the TSFS and FASP) for 2007/08 had discrepancies found in the authentication stage

(see Table 6 in para. 2.13). However, only 18 (5%) cases (i.e. 3 cases for the TSFS and 15 cases for the FASP) were referred to the Police (see Table 6).

### *Audit recommendations*

2.36 **Audit has recommended that the Controller, Student Financial Assistance Agency should:**

- (a) **take more proactive measures to prevent applicants from providing incorrect or incomplete information in applications; and**
- (b) **improve the effectiveness of the punitive measures for handling applications with incorrect or incomplete information, for example:**
  - (i) **by streamlining the internal procedures of referring omission cases to the Police for investigation; and**
  - (ii) **by imposing charges on the applicants to cover the additional administrative costs due to the omissions in their applications.**

### **Response from the Administration**

2.37 The **Controller, Student Financial Assistance Agency** agrees with the audit recommendations. She has said that:

- (a) the SFAA has all along been taking proactive measures to remind applicants to provide correct and complete information, and has reviewed from time to time the measures to prevent information omissions. Based on the information gathered from the annual authentication exercise and daily operational experience, the SFAA will update all application-related documents before the commencement of each application cycle to remind applicants of the need to provide correct and complete information. In 2009/10, the SFAA has initiated a number of improvements to prevent information omissions, including beefing up the contents of informational VCDs distributed to institutions, checklists of commonly omitted items and letters to applicants. The SFAA will also enclose a checklist of commonly omitted items and required documents with the warning/rejection letters to reinforce the messages. The SFAA will continue with its efforts in taking more proactive measures to prevent applicants from providing incorrect or incomplete information; and
- (b) in October 2008, the SFAA reviewed and streamlined the internal procedures of referring omission cases to the Police for investigation. The SFAA will also explore ways to improve the effectiveness of punitive measures for handling applications with incorrect or incomplete information.

## **PART 3: LOAN REPAYMENTS**

3.1 This PART examines the SFAA's handling of loan repayments and suggests measures for improvement.

### **Loan repayment by quarterly instalments**

3.2 Borrowers of means-tested loans under the TSFS and FASP are required to repay their loans and the interest accrued by quarterly instalments within five or ten years upon graduation or termination of their studies. For the non-means-tested loans under the NLS, NLSPS and ENLS, the repayment period is ten years. Details of the loan repayment requirements are shown at Appendix B.

### **Deferment of loan repayment**

3.3 For borrowers who are unable to repay their loans owing to further full-time studies, financial hardship or serious illness, they may apply for deferment of loan repayment. In the 2008-09 financial year, the SFAA completed the processing of 7,072 deferment applications, of which 6,026 (85%) applications were approved. A breakdown of the approved applications is shown in Table 9.

**Table 9**

#### **Deferment applications (2008-09 financial year)**

<b>Scheme</b>	<b>Number of applications processed</b>	<b>Number of applications approved on grounds of</b>			
		<b>Further studies</b>	<b>Financial hardship</b>	<b>Serious illness</b>	<b>Total</b>
TSFS	2,351	1,224	860	12	<b>2,096</b>
FASP	561	267	228	0	<b>495</b>
NLS	620	275	262	4	<b>541</b>
NLSPS	1,901	1,017	602	5	<b>1,624</b>
ENLS	1,639	550	715	5	<b>1,270</b>
<b>Total</b>	<b>7,072</b>	<b>3,333</b>	<b>2,667</b>	<b>26</b>	<b>6,026</b>

*Source: SFAA records*

### *Processing of deferment applications*

3.4 Applications for deferment of loan repayment are processed by three different Units of the SFAA. Details are as follows:

- (a) the **Deferment Unit** of the Payment Section processes deferment applications submitted by borrowers of TSFS, NLS, NLSPS or ENLS loans which have **less than two instalments in arrears**;
- (b) the **Default Unit** processes deferment applications submitted by borrowers of TSFS, NLS, NLSPS or ENLS loans which have **two or more consecutive instalments in arrears**; and
- (c) the **Default/Deferment/Recovery Unit (DDR Unit)** of the Post-secondary Students Section processes deferment applications submitted by borrowers of **FASP loans**.

### **Audit observations and recommendations**

#### *Need to provide adequate guidelines for processing deferment applications*

3.5 The Deferment Unit and DDR Unit issued guidelines for processing deferment applications. However, up to July 2009, the Default Unit had not issued any such guidelines. Audit examination of ten deferment applications approved by the Default Unit revealed that the criteria adopted for approving the applications were not clear. Clear guidelines can help staff improve their efficiency and effectiveness in processing the deferment applications.

#### *Other areas for improvement in processing deferment applications*

3.6 Audit examined a sample of 30 deferment applications approved by the three Units (ten applications for each Unit). Audit found that there is room for improvement in the following areas:

- (a) ***Applications approved despite failure to provide necessary documents or information.*** Audit noted that there were two cases in which the applicants had not provided the necessary supporting documents or information. However, the applications were approved; and
- (b) ***Assets of applicants.*** For applications on the ground of financial hardship, the borrowers are required to submit a copy of all bank passbooks/statements for the past six months. However, they are not required to provide information on their other liquid assets (which do not appear on the bank passbooks/statements).

Without requiring the applicants to provide such information, it is difficult to ascertain whether they are suffering from genuine financial hardship.

#### *Audit recommendations*

**3.7 Audit has recommended that the Controller, Student Financial Assistance Agency should:**

- (a) **issue guidelines on the processing of deferment applications to staff of the Default Unit;**
- (b) **ensure that applicants have provided the necessary supporting documents and information before their applications are approved; and**
- (c) **consider requiring the applicants to provide information on other liquid assets in addition to those shown on bank passbooks/statements in ascertaining whether the applicants are suffering from genuine financial hardship.**

#### **Response from the Administration**

**3.8 The Controller, Student Financial Assistance Agency** agrees with the audit recommendations.

#### **Handling of defaulted loans**

**3.9** Borrowers who have failed to repay two or more consecutive instalments and have not applied for deferment of loan repayment are classified as defaulters. In June 2009, the SFAA informed the JCSF that as at 31 March 2009:

- (a) there were 137,407 repayment accounts with a total amount of outstanding principal of \$4,975.8 million;
- (b) the total amount of outstanding principal and arrears (i.e. interest and surcharge) in defaulted accounts was \$608.9 million, of which \$215.7 million was defaulted instalments; and
- (c) the default rates were 9.7% in terms of the number of repayment accounts and 12.2% in terms of the loan amount.

Details are shown in Table 10.

**Table 10**  
**Repayment accounts**  
**(31 March 2009)**

	<b>TSFS</b>	<b>FASP</b>	<b>NLS</b>	<b>NLSPS</b>	<b>ENLS</b>	<b>Overall</b>
(a) Number of repayment accounts	43,729	8,342	22,501	12,070	50,765	<b>137,407</b>
(b) Total amount of outstanding principal in repayment accounts (\$ million)	1,189.9	249.3	943.7	903.7	1,689.2	<b>4,975.8</b>
(c) Number of defaulters (Note)	2,663	347	1,586	1,095	<b>7,572</b>	<b>13,263</b>
(d) Defaulted instalments (\$ million)	65.1	2.5	36.6	31.9	79.6	<b>215.7</b>
(e) Total amount of outstanding principal and arrears in defaulted accounts (\$ million)	98.7	13.9	88.5	117.8	<b>290</b>	<b>608.9</b>
(f) Default rate in terms of number of repayment accounts (f) = (c)/(a)×100%	6.1%	4.2%	7%	9.1%	14.9%	<b>9.7%</b>
(g) Default rate in terms of loan amount (g) = (e)/(b) ×100%	8.3%	5.6%	9.4%	13%	<b>17.2%</b>	<b>12.2%</b>

Source: SFAA records

Note: A defaulter may default repayments in more than one loan scheme and has more than one defaulted account.

## **Audit observations and recommendations**

### ***Increasing loan default***

3.10 Audit noted that there was a large increase in the number of defaulters during the period 2007 to 2009 (see Table 11). It can be observed that the figures increased from 9,769 as at 31 March 2007 by 3,494 (36%) to 13,263 as at 31 March 2009.

**Table 11**  
**Increase in defaulted loans**  
**(2007 to 2009)**

	31 March 2007	31 March 2008	31 March 2009
Number of defaulters	9,769	10,962	13,263
Amount of outstanding principal and arrears in defaulted accounts (\$ million)	423.2	502.6	608.9
Default rate in terms of number of repayment accounts	7.7%	8.3%	9.7%
Default rate in terms of loan amount	10.3%	10.9%	12.2%

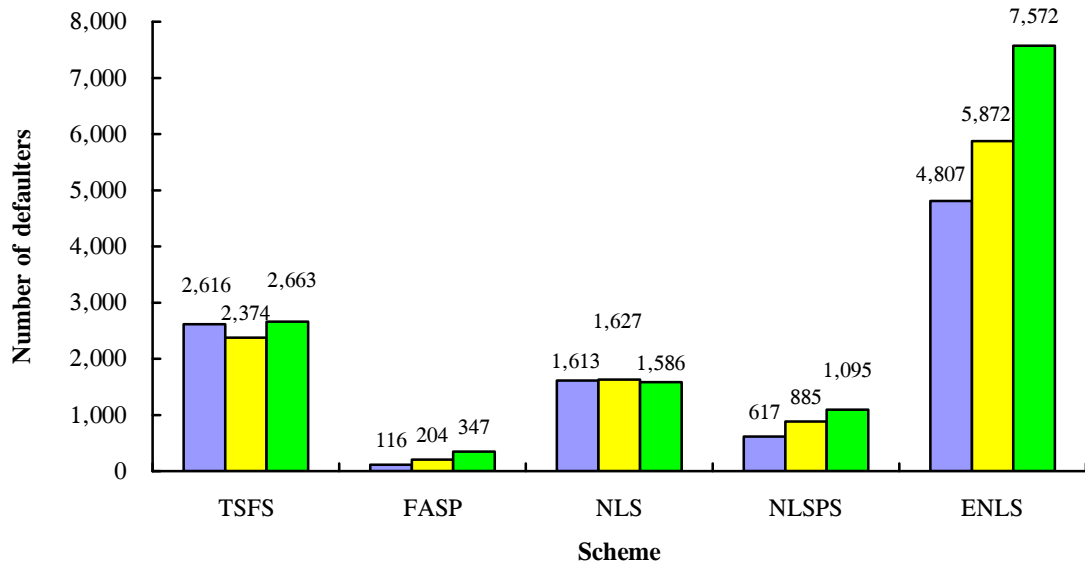
Source: SFAA records

3.11 Audit analysed the number of defaulters and amount of outstanding principal and arrears in defaulted accounts for each scheme. The results are shown in Figure 1.

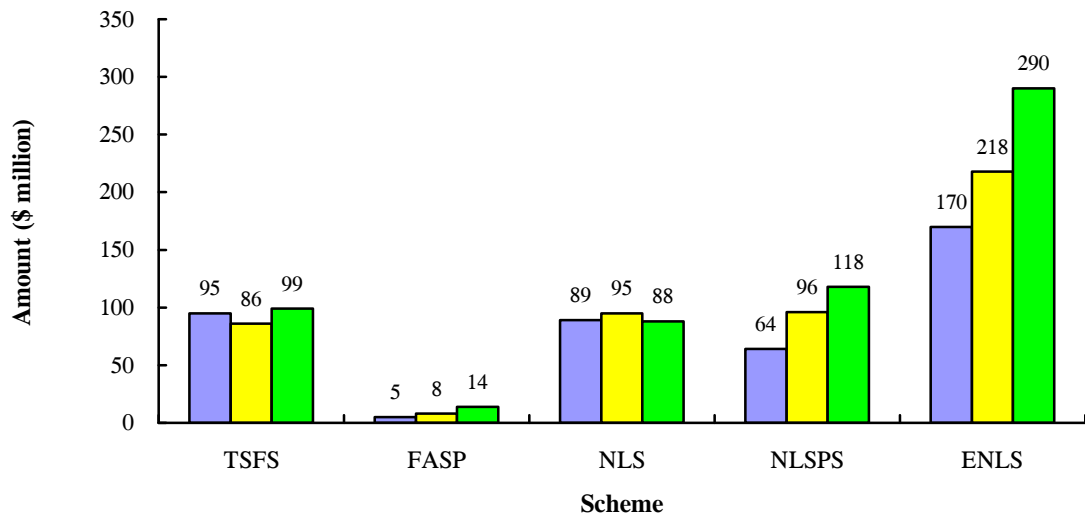
Figure 1

Defaulted loans by type of scheme  
(2007 to 2009)

(A) Number of defaulters



(B) Amount of outstanding principal and arrears in defaulted accounts



Legend:   
■ As at 31 March 2007  
■ As at 31 March 2008  
■ As at 31 March 2009

Source: SFAA records



3.12 It can be observed from Figure 1 that except the NLS, all the other four loan schemes recorded an increase in defaulters and defaulted loan amounts during the period 2007 to 2009. **Of these four schemes, the ENLS had the most serious loan default problem in terms of number of defaulters, loan amount and default rate (see Table 10 in para. 3.9).**

*Need to expedite referral of default cases to DoJ*

3.13 The SFAA refers default cases to the DoJ for legal action if its attempts to recover the loans from the borrowers/indemnifiers are in vain. For the purpose of clearing the backlog of default cases pending referral to the DoJ, the SFAA created a Deputy Controller post to head the Default Unit (see para. 2.18) and increased the Unit's staff establishment from 24 to 66 posts with effect from March 2008 (most of the additional staff were in post in late 2008). The number of cases referred to the DoJ increased nearly threefold, from 310 in 2007-08 financial year to 823 in 2008-09 financial year (see Table 12).

**Table 12**

**Loan default cases referred to DoJ  
(2006-07 to 2008-09 financial years)**

<b>Scheme</b>	<b>2006-07</b>	<b>2007-08</b>	<b>2008-09</b>
TSFS	158	113	322
FASP	11	22	53
NLS	51	48	74
NLSPS	14	18	42
ENLS	48	109	332
<b>Total</b>	<b>282</b>	<b>310</b>	<b>823</b>

*Source: SFAA records*

*Remarks: The default cases under the FASP were referred to the DoJ by the DDR Unit of the Post-secondary Students Section. The other cases were referred to the DoJ by the Default Unit.*

3.14 The Government's right to recover the outstanding loans through legal action is subject to the provisions of the Limitation Ordinance (Cap. 347). According to the advice given by the DoJ in April 2009, the limitation expiry date of legal action against the borrower would be six years (counting from seven days beyond the due date of the first overdue instalment). For legal action against the indemnifier, the limitation expiry date is 12 years counting from the date of the SFAA's formal demand letter to the indemnifier (Note 13). These limitation expiry dates are only applicable to cases under which no repayment was made by the borrower or the indemnifier. In case there is part-payment, limitation action will be counted for six years from the date of last repayment made by the borrower and 12 years from the date of last repayment made by the indemnifier.

3.15 Since September 2008, the Default Unit has compiled ageing analyses to analyse the time-bar limit of taking legal action against the borrowers. The ageing analysis of the default cases under the TSFS, NLS, NLSPS and ENLS (excluding cases referred to the DoJ and cases the borrowers of which had declared bankrupt) as at 31 March 2009 is at Appendix C. **The analysis indicated that 127 cases exceeded the time-bar limit of six years, and the SFAA was debarred from taking legal action against the borrowers of these cases. Of these 127 cases, 118 cases were within the time-bar limit of 12 years. Therefore, legal action could be taken against the indemnifiers. However, the SFAA was debarred from taking legal action against the indemnifiers of the remaining 9 cases.**

3.16 As at 31 March 2009, there were 114 cases (with a total loan amount of \$5.7 million) that would soon exceed the time-bar limit of six years by 31 March 2010 (see Appendix C). The SFAA needs to expedite the referral of these cases, and other cases that are approaching the time-bar limit (see Appendix C) to the DoJ for legal action. In this connection, Audit noted that the DoJ had also advised the SFAA to expedite action as the DoJ might not be able to take prompt legal action if the default cases were not referred to it in time.

#### *Need to compile ageing analysis for FASP loans*

3.17 The SFAA had not compiled an ageing analysis of default cases under the FASP to monitor the time-bar limit of taking legal action against the borrowers/indemnifiers. Audit considers that the SFAA needs to compile such an analysis, similar to that compiled by the Default Unit for the other four loan schemes.

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**Note 13:** *The SFAA issues a formal demand letter to the indemnifier if no repayment/response is received from the borrower after sending two reminders.*

*Need to step up recovery actions and improve case management procedures*

3.18 Audit reviewed a sample of 42 default cases to ascertain the adequacy of recovery actions taken by the SFAA. Audit found that in some cases:

- (a) follow-up actions to recover the loans from the borrowers/indemnifiers were inadequate and not timely (see examples at Appendix D); and
- (b) the SFAA did not follow up regularly the progress of the recovery actions taken by the DoJ.

3.19 Audit noted that the SFAA had strengthened its loan recovery process after the creation of the Deputy Controller post in March 2008 (see para. 3.13). However, the audit findings on loan recovery actions taken by the SFAA indicate that **there is a need for the SFAA to further improve its case management procedures with an effective bringing-up system to ensure that its staff take adequate and timely actions on the recovery of loans.**

*Need to explore other measures to tackle default problem*

3.20 Apart from speeding up the loan recovery actions, there is a need to explore more effective measures to tackle the default problem. Audit noted that the SFAA had been seeking the advice of the JCSF in this respect. At the meeting held in January 2008, the JCSF suggested that the SFAA should consider supplying the credit information of student loan borrowers to a credit reference agency so as to deter loan borrowers from defaulting loan repayment. Up to July 2009, the SFAA was still exploring the feasibility of the suggestion having regard to the advice of the Privacy Commissioner for Personal Data and the DoJ.

*Audit recommendations*

3.21 **Audit has recommended that the Controller, Student Financial Assistance Agency should:**

- (a) **ascertain the reasons for the increase in defaulted loans and take prompt actions to tackle the problem, especially for loans under the ENLS;**
- (b) **expedite the referral of default cases to the DoJ for taking legal action to recover the outstanding loans;**
- (c) **compile ageing analysis of default cases under the FASP to monitor the time-bar limit of taking legal action against the borrowers/indemnifiers;**

- (d) **improve the case management procedures with an effective bringing-up system to ensure that SFAA staff take adequate and timely actions to recover the loans from the borrowers/indemnifiers;**
- (e) **follow up regularly the progress of the recovery actions taken by the DoJ; and**
- (f) **continue to explore measures to tackle the loan default problem.**

### **Response from the Administration**

3.22 The **Controller, Student Financial Assistance Agency** agrees with the audit recommendations. She has said that:

- (a) with the exception of loan borrowers who have approached the SFAA to apply for deferment of loan repayment, most of the defaulters have disregarded notices of loan repayment and reminders issued by the SFAA. Neither have they approached the SFAA to resolve their problems in repayment or disclose their reasons for default. The SFAA is therefore unable to ascertain the reasons behind these non-responding loan defaulters for the purpose of accounting for the increase in defaulted loans;
- (b) the SFAA has strengthened its staff resources and implemented streamlined procedures to expedite the referral of default cases to the DoJ since late 2008. The number of cases referred to the DoJ has increased from around 300 in 2007-08 financial year to over 800 in 2008-09 financial year. The 114 default cases that would exceed the time-bar limit of six years by 31 March 2010 (see para. 3.16) have all been dealt with;
- (c) the SFAA is compiling a similar ageing analysis for default cases under the FASP to ensure timely referral of cases for legal action;
- (d) the SFAA has put in place a monitoring and control mechanism since December 2008 to improve the management of default cases. To further improve the case management process and ensure that recovery actions are adequate and timely, the SFAA is developing a computer system with a tentative completion date in mid-2010. The system will automate the manual process in issuing reminders, calculating the debt and preparing various documents for recovery action. It will provide management reports to monitor the progress of the cases to facilitate timely recovery actions;
- (e) the SFAA has been regularly following up the progress of the recovery actions taken by the DoJ since late 2008; and

- (f) the SFAA will continue to explore other possible and effective ways to tackle the loan default problem.

3.23 The **Director of Administration and Development, Department of Justice** has said that:

- (a) the DoJ supports the audit recommendation in paragraph 3.21(b) that the SFAA should expedite the referral of default cases to the DoJ for taking legal action to recover the outstanding loans; and
- (b) the DoJ has no problem with the audit recommendation in paragraph 3.21(e). In handling the student loan recovery cases, the DoJ will seek instructions from the SFAA where appropriate and will keep it informed of material developments of the recovery process of the cases concerned. The DoJ has internal measures in place to monitor the overall progress of the recovery cases. Whilst the SFAA could at any time follow up with the DoJ regarding the progress of the recovery actions, the DoJ will take the necessary steps to recover the loans as a matter of course.

## **PART 4: FINANCIAL ASSISTANCE OF MEANS-TESTED SCHEMES**

4.1 This PART examines the level of financial assistance under the means-tested schemes and suggests measures for improvement.

### **Level of financial assistance**

4.2 A successful applicant under the TSFS or FASP may receive assistance up to the maximum amounts of grant and loan depending on the financial circumstances of the applicant's family.

4.3 The maximum amounts of grant and loan under the TSFS comprise:

#### ***Grant***

- the actual amount of tuition fees and compulsory student union fees. For 2008/09, the largest amount of tuition fees payable was \$42,100;
- an amount of academic expenses depending on the course of study pursued. For 2008/09, the maximum amount ranged from \$4,550 to \$25,890. It is adjusted annually according to the movements of the Student Price Index (SPI — Note 14); and

#### ***Loan***

- an amount of living expenses. For 2008/09, the maximum amount was \$35,670. It is also adjusted annually according to the movements of the SPI.

4.4 The maximum amounts of grant and loan under the FASP comprise:

#### ***Grant***

- an amount of tuition fees subject to a ceiling. For 2008/09, the ceiling was \$58,270;

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**Note 14:** *The SPI is compiled by the Census and Statistics Department. It is similar to the Consumer Price Index but measures more accurately the effect of price changes on expenses normally incurred by tertiary students.*

- an amount of academic expenses. For 2008/09, the maximum amount was \$3,090; and

(The maximum amounts of the tuition fees and academic expenses are adjusted annually according to the movements of the Consumer Price Index (A).)

#### *Loan*

- an amount of living expenses. It is the same as that under the TSFS.

### **Student expenditure survey**

4.5 Student expenditure surveys (SESs) were carried out periodically by the SFAA to ascertain the academic and living expenses of an average full-time student enrolled in the publicly-funded programme. The results of the SES formed the basis for determining the maximum levels of grant (for academic expenses) under the TSFS, and loan (for living expenses) under the TSFS and FASP. These maximum levels are adjusted annually according to the movements of the SPI.

### **Audit observations and recommendations**

4.6 The maximum levels of grant and loan for 2008/09 were based on the SES conducted in 1988. Although an SES was conducted in 1999 to update the expenditure patterns of students, the results of the SES were not adopted due to reservations about the findings and methodology of the survey. At the meeting held in September 2005 to consider the way forward, the JCSF agreed that a consultancy study should be conducted with a view to establishing a sustainable, viable and simpler mechanism for setting and adjusting the grant and loan levels in place of the SES.

4.7 In January 2006, the JCSF formed a working group to steer the proposed consultancy study. The working group originally planned to complete the consultancy study in early 2007. However, due to the long time taken in selecting the consultant, the study only commenced in September 2007 and was expected to be completed in 13 months' time by October 2008.

4.8 Audit noted that up to September 2009, the consultancy study was still in progress and the consultant was working on the interim report. The review of the level of assistance had dragged on for a long time since the last SES was conducted in 1999. **The present levels of grant for academic expenses and loan for living expenses are still based on the findings of the 1988 SES which was conducted more than 20 years ago.**

*Audit recommendations*

4.9 **Audit has recommended that the Controller, Student Financial Assistance Agency should:**

- (a) **take action to expedite the completion of the consultancy study on the mechanism for setting and adjusting the level of financial assistance; and**
- (b) **consult the stakeholders as soon as possible for implementing the new mechanism.**

**Response from the Administration**

4.10 The **Controller, Student Financial Assistance Agency** agrees with the audit recommendations. She has said that:

- (a) the progress of the consultancy was slower than expected owing to unforeseen difficulties, in particular relating to the conduct of a student survey. The SFAA will make efforts to expedite the completion of the consultancy study with a view to working out a sustainable, viable and simpler mechanism for setting and adjusting the level of assistance for the TSFS; and
- (b) the SFAA will consult the JCSF on the findings and recommendations of the consultancy study in due course.



## **PART 5: INTEREST RATES ON LOANS**

5.1 This PART examines the interest rates on loans and suggests measures for improvement.

### **Interest rate for means-tested loans**

5.2 In 1987/88, the Government introduced a fixed interest rate of 2.5% per annum on TSFS loans. The charging of interest was made on the recommendation of the Public Accounts Committee in 1986 to consider imposing a concessionary rate of interest on outstanding loans, partly to defray the cost of running the scheme and partly to ensure that students apply only for what they genuinely need. **This interest rate was set based on the borrowers' affordability to repay, without making reference to the market interest rate.** When the FASP was introduced in 2001/02, the same interest rate was charged for FASP loans. The interest rate of 2.5% has remained unchanged since 1987/88.

### *Review of the interest rate*

5.3 At the Legislative Council (LegCo) meeting held on 28 November 2001, the Government was urged to review the adjustment mechanism of the interest rate of loans provided under various student financial assistance schemes with a view to lowering the interest rates to alleviate the burden of borrowers. In November 2002, the Government informed the LegCo Panel on Education that there should be no change to the fixed interest rate of 2.5% because:

- (a) interest was a small element in the monthly repayment amount. For example, a 1% reduction of the rate to 1.5% would bring down the monthly repayment amount for an average borrower taking a loan of \$63,000 by \$28, from \$1,120 to \$1,092;
- (b) a general reduction of the rate would have little impact for borrowers suffering from financial hardship. However, the financial implication for the Government was substantial taking into account the total amount of loans; and
- (c) deferment/rescheduling of repayment was a more effective measure to assist borrowers suffering from financial hardship.

### **Audit observations and recommendation**

5.4 When the interest rate of 2.5% for means-tested loans was determined in 1987, it was based on the borrowers' affordability to repay at that time. In Audit's view, the repayment affordability is dependent on a number of factors, such as the amount of the loan, whether the borrower is in employment after graduation, and his salary level. These

factors may have changed over the years since 1987 (e.g. the maximum level of the loan had increased from \$11,350 in 1987/88 to \$35,670 in 2008/09).

### *Audit recommendation*

5.5 **Audit has recommended that the Controller, Student Financial Assistance Agency should revisit the issue of the borrowers' affordability to repay (e.g. by obtaining from the tertiary institutions up-to-date information on their graduates' employment and salary levels) in order to ascertain whether the interest rate of 2.5% needs to be adjusted.**

### **Response from the Administration**

5.6 **The Controller, Student Financial Assistance Agency** agrees with the audit recommendation. She has said that:

- (a) the interest rate was set at 2.5% having regard to the fact that the interest only accrued from the date after graduation and the actual increase in repayment amounts for individual students was small. Hence, the repayment was affordable to the graduates;
- (b) as of now, the interest rate of 2.5% is far below the interest rate on unsecured loans in the market and forms only a small part of the overall repayment amounts for individual students. The SFAA has in place effective measures to help borrowers with repayment difficulties;
- (c) it is practically very difficult to establish the borrowers' affordability to repay for the purpose of determining an interest rate, given the vast diversity in the graduates' employment, income levels and expenditure patterns; and
- (d) the SFAA will nevertheless review this interest rate given that it has been in place for more than 20 years.

5.7 **The Secretary for Financial Services and the Treasury** has said that:

- (a) he acknowledges the audit recommendation that the SFAA should revisit the issue of the borrowers' affordability to repay under the means-tested loans to ascertain whether the interest rate of 2.5% needs to be adjusted; and
- (b) the audit recommendation would entail a review that takes into account the borrowers' affordability to repay and the financial implications to the Government.

## **Interest rate for non-means-tested loans**

5.8 Interest on non-means-tested loans is charged at the Government's no-gain-no-loss rate, plus a RAF of 1.5% (see para. 1.13(a)). The rate of RAF has remained at 1.5% since the NLS was introduced in 1998/99.

### ***Review of the RAF***

5.9 When the Finance Committee of LegCo discussed the proposed NLS in December 1997, the Government undertook to review the RAF when the first group of NLS borrowers had commenced loan repayment for one year, i.e. towards the end of 2000. In November 2001, the Government informed LegCo that in the light of the rapid expansion of the non-means-tested loan schemes to cover additional categories of applicants (i.e. students under the NLSPS and ENLS), it had to examine more statistical data to conduct a more comprehensive review of the RAF.

5.10 In early 2005, the review of the RAF was put on hold when the Government was exploring the feasibility of the disposal and outsourcing of the non-means-tested loan schemes. The review of the RAF was subsequently resumed after the LegCo Panel on Education disagreed with the Government's proposal of the disposal and outsourcing of the non-means-tested loan schemes in January 2006.

5.11 At a meeting of the LegCo Panel on Education held in February 2009, in response to proposals on economic relief measures relating to the non-means-tested loan schemes, the Administration stated that the income from the RAF had yet been able to fully cover the Government's risk of loss due to default in repayment of the loans. This was especially so in view of the increasing rate of default. To remove the RAF would go against the full-cost-recovery principle of the non-means-tested loan schemes. The Administration would need to observe for a longer time the loan repayment and default situation before considering any changes to the RAF.

### **Audit observations and recommendation**

5.12 The same rate of RAF is used for loans under the three non-means-tested loan schemes, notwithstanding the fact that they cover different categories of students. The use of the same RAF rate may not be able to adequately cover the different levels of credit risk of the schemes.

5.13 At the meeting held in June 2009, the SFAA informed the JCSF that the interest collected from the RAF for the NLSPS and ENLS was not sufficient to cover the possible loss due to defaulted loans. As at 31 March 2009, the total cumulative shortfall for the three loan schemes was \$255 million. Details are shown in Table 13.

Table 13

**Cumulative shortfall under the non-means-tested loan schemes  
(31 March 2009)**

Scheme	Cumulative surplus/(shortfall) (\$ million)
NLS	16
NLSPS	(85)
ENLS	(186)
<b>Total</b>	<b>(255)</b>

*Source: SFAA records*

5.14 It can be observed from Table 13 that the cumulative shortfall was mainly attributed to the ENLS. As noted in Table 10 in paragraph 3.9, the ENLS had the highest default rate of 17.2% as compared to 9.4% of the NLS and 13% of the NLSPS. **This indicated that there were different levels of credit risk of the schemes.**

***Audit recommendation***

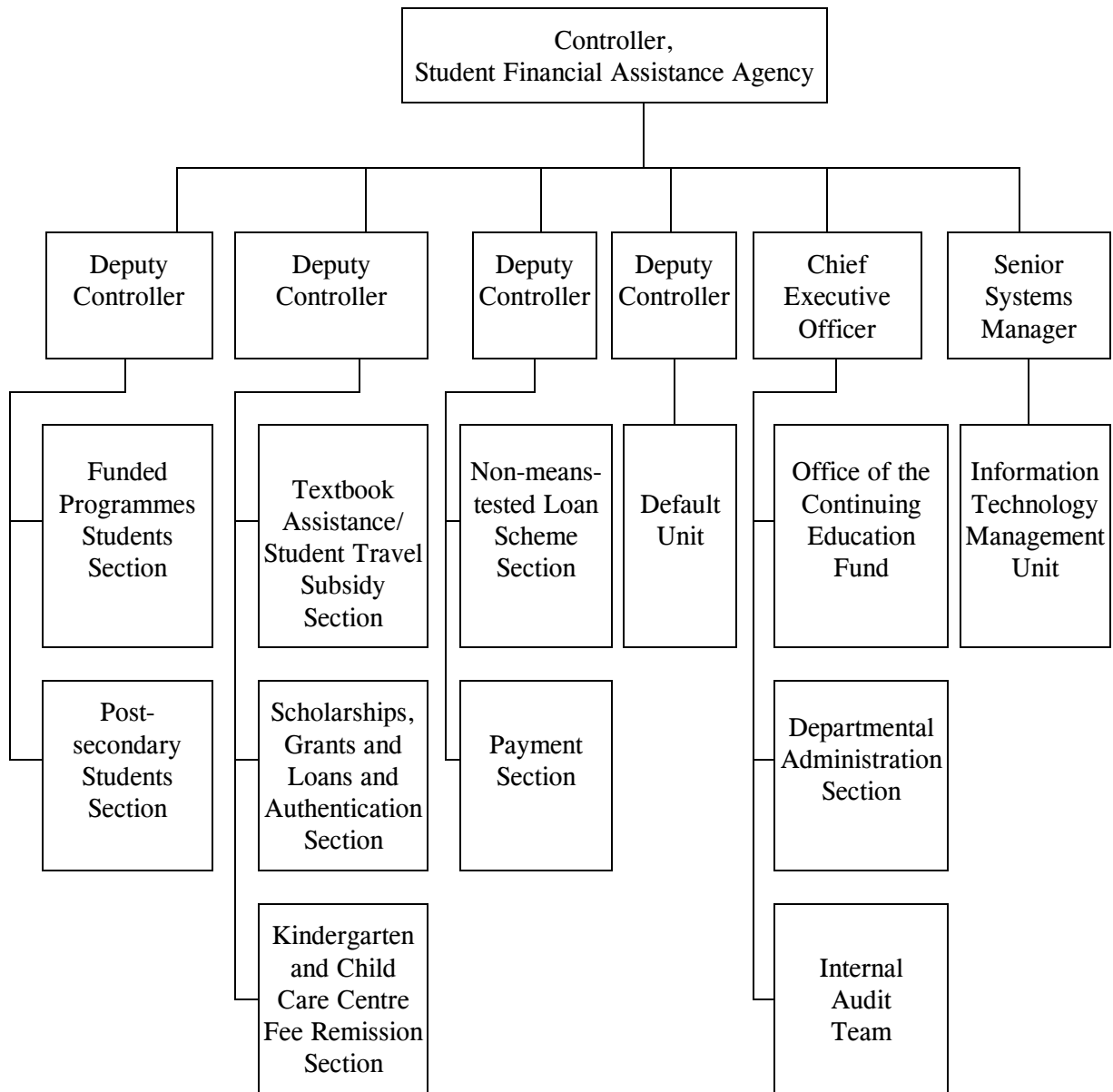
5.15 **Audit has recommended that the Controller, Student Financial Assistance Agency should consider adopting different rates of RAF to address the different levels of credit risk of the schemes.**

**Response from the Administration**

5.16 The **Controller, Student Financial Assistance Agency** agrees with the audit recommendation. She has said that the SFAA will review the rates of RAF under the various non-means-tested loan schemes with reference to their respective default rates, in the context of an overall review on the major operational aspects of the schemes.

5.17 The **Secretary for Financial Services and the Treasury** agrees with the audit recommendation that the RAF should reflect the credit risk of the different schemes and a review should be conducted.

**Student Financial Assistance Agency  
Organisation chart  
(30 June 2009)**



Source: SFAA records

**Repayment of loans**

<b>Scheme</b>	<b>Commencement of repayment</b>	<b>Repayment terms</b>
TSFS	Upon the student's graduation or termination of study	20 quarterly instalments over 5 years
FASP	Upon the student's graduation or termination of study, or the lapse of 6 years from the first disbursement of the loan, whichever is earlier	<ul style="list-style-type: none"> <li>• 40 quarterly instalments over 10 years for loans disbursed in 2005/06 or before</li> <li>• 20 quarterly instalments over 5 years for loans disbursed in or after 2008/09 (Note)</li> </ul>
NLS	Upon the student's graduation or termination of study	} 40 quarterly instalments within 10 years
NLSPS	Upon the student's graduation or termination of study, or the lapse of 6 years from the first disbursement of the loan, whichever is earlier	
ENLS	Upon the student's graduation, termination of study, achievement of the requisite number of credits/modules for the programme of study, or the lapse of 6 years from the first disbursement of the loan, whichever is the earliest	

*Source: SFAA records*

*Note: For 2006/07 and 2007/08, the SFAA did not provide any loans to students under the FASP.*

**Ageing analysis of default cases  
(31 March 2009)**

Ageing (Note)	TSFS		NLS		NLSPS		ENLS		Total	
	No. of cases	Amount (\$ million)	No. of cases	Amount (\$ million)	No. of cases	Amount (\$ million)	No. of cases	Amount (\$ million)	No. of cases	Amount (\$ million)
1 year or less	841	28.3	574	29.9	373	37.9	2,701	99.4	<b>4,489</b>	<b>195.5</b>
Over 1 year to 2 years	401	13.9	270	14.2	261	26.8	1,854	55.7	<b>2,786</b>	<b>110.6</b>
Over 2 years to 3 years	377	13	214	11.6	210	22.6	1,401	46.6	<b>2,202</b>	<b>93.8</b>
Over 3 years to 4 years	324	9.4	213	11.7	123	15.1	1,184	38.9	<b>1,844</b>	<b>75.1</b>
Over 4 years to 5 years	242	7	139	8.2	52	6.1	641	19.6	<b>1,074</b>	<b>40.9</b>
Over 5 years to 6 years	39	1.1	27	1.7	12	1.3	36	1.6	<b>114</b>	<b>5.7</b>
Over 6 years	110	2.1	12	0.9	1	0.2	4	0.2	<b>127</b>	<b>3.4</b>
<b>Total</b>	<b>2,334</b>	<b>74.8</b>	<b>1,449</b>	<b>78.2</b>	<b>1,032</b>	<b>110</b>	<b>7,821</b>	<b>262</b>	<b>12,636</b>	<b>525</b>

Source: SFAA records

Note: The analysis did not include cases referred to the DoJ and those in which the borrowers had declared bankrupt. The age of a case was counted from the start of the 6-year limitation period for taking legal action against the borrower.

**Examples of inadequate recovery action in default cases**

Case No.	Audit findings
1	<ul style="list-style-type: none"> <li>• A first reminder was issued to the borrower on 21 October 2004. It was returned undelivered.</li> <li>• A second reminder was issued to the borrower and copied to the indemnifier on 12 January 2009.</li> <li>• A final reminder was issued to the indemnifier on 11 February 2009.</li> <li>• The case was referred to the DoJ on 1 April 2009.</li> </ul>
2	<ul style="list-style-type: none"> <li>• A first reminder was issued to the borrower on 21 July 2004. It was returned undelivered.</li> <li>• A second reminder was prepared but not sent to the borrower. The copy issued to the indemnifier on 27 November 2008 was returned undelivered.</li> <li>• A final reminder was issued to the indemnifier on 17 December 2008. It was returned undelivered.</li> <li>• The case was referred to the DoJ on 16 January 2009.</li> </ul>
3	<ul style="list-style-type: none"> <li>• A first reminder was issued to the borrower on 21 July 2004.</li> <li>• A second reminder was issued to the borrower and copied to the indemnifier on 19 August 2004.</li> <li>• A final reminder was issued to the indemnifier on 16 September 2004.</li> <li>• The case was referred to the DoJ on 18 February 2009.</li> </ul>
4	<ul style="list-style-type: none"> <li>• A first reminder was issued to the borrower on 22 April 2004.</li> <li>• A second reminder was issued to the borrower and copied to the indemnifier on 19 August 2004.</li> <li>• A final reminder was issued to the indemnifier on 16 September 2004.</li> <li>• The case was referred to the DoJ on 12 November 2008.</li> </ul>
5	<ul style="list-style-type: none"> <li>• A first reminder was issued to the borrower on 22 April 2004.</li> <li>• A second reminder was issued to the borrower and copied to the indemnifier on 19 August 2004.</li> <li>• A final reminder was issued to the indemnifier on 16 September 2004. It was returned undelivered.</li> <li>• The case was referred to the DoJ on 20 November 2008.</li> </ul>

Source: *Audit analysis of SFAA records*



**Acronyms and abbreviations**

Audit	Audit Commission
DDR Unit	Default/Deferment/Recovery Unit
DoJ	Department of Justice
ENLS	Extended Non-means-tested Loan Scheme
FASP	Financial Assistance Scheme for Post-secondary Students
JCSF	Joint Committee on Student Finance
LegCo	Legislative Council
NLS	Non-means-tested Loan Scheme
NLSPS	Non-means-tested Loan Scheme for Post-secondary Students
RAF	Risk-adjusted factor
SES	Student expenditure survey
SFAA	Student Financial Assistance Agency
SPI	Student Price Index
TSFS	Tertiary Student Finance Scheme — Publicly-funded Programmes