

**Procedures for Approval of Loan Applications and Recovery of Debts
under the Non-means-tested Loan Scheme
Executive Summary of Direct Investigation Report**

Background

The Non-means-tested Loan Scheme (“the Loan Scheme”) of the Working Family and Student Financial Assistance Agency (“WFSFAA”) aims at providing financial assistance to those students who are unwilling to undergo or fail to pass the income and assets assessment of WFSFAA’s Tertiary Student Finance Scheme – Publicly-funded Programmes (“the Finance Scheme”).

2. There are three schemes under the Loan Scheme to cater for the needs of different categories of students, namely:

- (1) Non-means-tested Loan Scheme for Full-time Tertiary Students (“the Full-time Tertiary Students Scheme”) for full-time students pursuing publicly-funded tertiary programmes;
- (2) Non-means-tested Loan Scheme for Post-secondary Students (“the Post-secondary Students Scheme”) for students pursuing full-time accredited self-financing post-secondary programmes offered by various institutions; and
- (3) Extended Non-means-tested Loan Scheme (“the Extended Scheme”) for students pursuing specified part-time or full-time post-secondary/continuing and professional education courses.

3. The Loan Scheme involves huge amounts of money. Taking the 2013/14 academic year as an example, the total amount of loans granted under the scheme was as much as \$1.3 billion, while the total amount in default now reached an accumulative total of \$170 million. The situation attracts concern. Some members of the public had complained to this Office, alleging that WFSFAA was lax in its debt recovery action against loan borrowers such that the indemnifiers, as guarantors for the borrowers, were inflicted with the burden of paying the accumulated interest and the associated legal fees. In addition, media reports had revealed the following two problems:

- (1) some people allegedly had their identity stolen and used to play indemnifier in loan applications; and
- (2) the staff/agents of some education institutions conspired with loan applicants/indemnifiers/witnesses to obtain loans by fraud using false information and documents.

4. In view of the above, The Ombudsman conducted a direct investigation to examine the procedures for approval of loan applications and recovery of debts under the Loan Scheme, with a view to identifying inadequacies.

Our Findings

Failure to Properly Manage the Scheme More Prone to Loan Default

5. Among the three schemes under the Loan Scheme, the Extended Scheme involves higher management risks and has the most serious problem of default on loan repayment. That is partly due to the fact that the scheme covers an extensive range of education institutions and courses.

6. Statistics of the 2011/12 to 2013/2014 academic years show the following:

- (1) Of all the default cases under the Loan Scheme, about 70% were under the Extended Scheme. Also, the amount in default under the Extended Scheme persistently accounted for more than half of the total overdue amount, standing at about \$100 million per year throughout the period.
- (2) During the 2013/14 academic year, 5,115 (68.81%) of the 7,434 cases with the longest default period (over 12 months) were under the Extended Scheme.
- (3) During the same academic year, 870 (40.88%) of the 2,128 cases involving the largest overdue amounts (over \$100,000) were under the Extended Scheme.

7. Quite a few of the loan borrowers under the Extended Scheme are in fact in employment and hence able to repay their loans. And yet the scheme has recorded such a serious default problem. WFSFAA should face this problem squarely by devising measures to reduce the credit risk of the Extended Scheme. We understand that such measures will to some extent impose extra restrictions on loan applicants' continuing learning. However, WFSFAA indeed has the duty to strike a balance between encouragement of continuing learning and protection of public funds from abuse.

Lack of Effective Deterrent Measures

8. Under the current system, loan defaulters are only asked to repay their debt with interest (their obligation anyway) together with an administrative charge. The deterrent effect is very weak.

9. We note that WFSFAA has once considered forwarding the negative credit data of the more serious defaulters to credit reference agencies for greater deterrent

effect. If such a measure is to be implemented, WFSFAA will give loan applicants clear prior notice of the measure and ask them to sign for consent.

10. For the following reasons, we strongly support in principle WFSFAA's implementation of the above measure for greater deterrence:

- (1) It is a long established and lawful practice that private financial institutions would forward the negative credit data of their loan defaulters to credit reference agencies. WFSFAA's function of granting loans to students is no different in nature from the business of private financial institutions in advancing credit to borrowers. The deterrent measure proposed by WFSFAA would only be in line with the practice of private financial institutions and would not be unfair to student defaulters.
- (2) We understand that once a negative credit record of default on loan repayment is registered in a credit database, it will to some extent affect the future credit applications by the person concerned to banks or other financial institutions. When loan borrowers under the Loan Scheme of WFSFAA are aware of such a possible consequence, they will think twice before defaulting on repayment.
- (3) The granting of non-means-tested loans to students under the WFSFAA Loan Scheme is indeed very generous. We do not consider it harsh at all for WFSFAA to require loan applicants to give consent to WFSFAA to forward their negative credit data to credit reference agencies in the event of their default on repayment.

11. We hope that WFSFAA could secure the agreement of the Privacy Commissioner for Personal Data ("PCPD"), so that the proposed deterrent measure can be put into effect.

Failure to Fully Verify Indemnifiers' Intention

12. Applicants under the Loan Scheme are not subject to any income and assets assessment, nor are they required to provide any assets as collateral. The credit risk is rather high. If the borrowers intentionally default on repayment of the loans or become insolvent, Government can only resort to recovering the debts from their indemnifiers.

13. WFSFAA could approach indemnifiers by **telephone** or **interview** to verify their intention to act as indemnifiers as well as the loan amounts against which they agree to indemnify. However, in practice, WFSFAA contacts just a small percentage of the indemnifiers by telephone or interview:

- (1) **Telephone:** For the loan applications under the Full-time-Tertiary

Students Scheme and the Post-secondary Students Scheme, WFSFAA randomly selects only 10% and 5% respectively of the indemnifiers and contacts them by telephone.

- (2) **Interview:** WFSFAA telephones nearly all indemnifiers under the Extended Scheme. But because of staff constraint, WFSFAA interviews only a small percentage of those indemnifiers. In the 2012/13 academic year, only 16 indemnifiers were invited to interview; after we had expressed concern, the number of indemnifiers interviewed in the 2013/14 academic year rose to 391, which was still a small number. The numbers of indemnifiers interviewed, represented a scanty 0.21% and 5.42% of the numbers of applications received in those two years.

14. WFSFAA's efforts in verification with indemnifiers are clearly inadequate.

Need to Ensure Careful Vetting

15. The database in WFSFAA's computer system contains the data of each Loan Scheme/Finance Scheme account. Staff can extract information from such data and then check whether a loan applicant/indemnifier is the loan applicant/indemnifier of other Loan Scheme/Finance Scheme accounts and whether he/she has ever been a defaulter or a defaulter's indemnifier, thereby identifying cases of higher management risks. It can be seen that the checking process is not fully computerised and part of the process is performed manually. As a result, human errors are possible. We consider that WFSFAA should fully computerise the checking process and in the interim closely supervise staff to ensure that they carry out the checking conscientiously.

Recommendations

16. In the light of the above findings, The Ombudsman urges WFSFAA to:
 - (1) devise measures to reduce the credit risk of the Extended Scheme, such as suitably limiting the number of courses that a loan borrower may take and the number of loan applications that he/she may make in any academic year;
 - (2) further deliberate with PCPD, with a view to implementing as soon as possible the measure of forwarding the negative credit data of the more serious defaulters to credit reference agencies in order to increase deterrence against loan default;
 - (3) deploy or increase staff to raise the percentage of indemnifiers contacted by telephone and interview, so as to reduce credit risks;
 - (4) consider fully computerising its process of checking loan

applicants/indemnifiers in order to ensure effective vetting of loan applications; and

- (5) before full computerisation of the process, supervise staff closely to ensure that they conscientiously check whether loan applicants/indemnifiers are playing multiple roles and whether they have ever been defaulters or defaulters' indemnifiers.

**Office of The Ombudsman
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