

The Committee noted that the Audit Commission (Audit) had conducted a review to examine the recovery of legal costs by the Legal Aid Department (LAD). The review focused on the following areas:

- cost recovery of the legal aid schemes;
- planning and monitoring of the recovery of legal costs;
- enforcement proceedings against judgment debtors;
- administration of outstanding and irrecoverable legal costs; and
- Audit's access to legal aid case files.

2. As Hon Andrew CHENG Kar-foo has declared that he is a lawyer on the Legal Aid Panel, the Committee has agreed that he be relieved from taking part in the examination of this chapter.

3. The Committee did not hold any public hearing on this subject. Instead, the Committee asked for written responses to its enquiries.

4. The **Director of Legal Aid** and the **Director of Accounting Services** responded to the Committee's enquiries in their respective letters of 1 December 2005, in *Appendices 31 and 32*. Their responses are set out in the ensuing paragraphs.

A. Cost recovery of the legal aid schemes

5. The Committee noted from paragraphs 2.6 to 2.8, 2.12 and 2.18 of the Director of Audit's Report (the Audit Report) that the accrual-based accounting principle was adopted in compiling the financial statements of the Supplementary Legal Aid Scheme (SLAS). On the other hand, receipts and payments under the Ordinary Legal Aid Scheme (OLAS) were accounted for in the Government's General Revenue Account, which adopted the cash-based accounting principle. Audit considered that the financial statements of the SLAS reflected more clearly its financial performance, including the extent to which legal costs incurred in legal aid cases had been recovered, than the financial information published in the Estimates and the LAD's annual reports for the OLAS.

6. The Committee also noted Audit's other view that, in order to enhance transparency and public accountability, there were merits for the LAD to disclose to the public the extent to which legal costs of civil cases under the OLAS where the court had awarded an order for costs and damages to the aided person had been recovered. The Committee asked whether the LAD would:

- reconsider adopting the accrual-based accounting principle in compiling the financial statements under the OLAS in view of Audit's view; and
- prepare and disclose to the public relevant financial information, in the form of income and expenditure statements similar to those for the SLAS, for the above-mentioned OLAS cases.

7. In his letter of 1 December 2005, the **Director of Legal Aid** informed the Committee that:

- the issue related to the difference between cash-based accounting and accrual based accounting, a subject relevant to not just the legal aid schemes but also the government accounting arrangement as a whole. The Government's General Revenue Account adopted cash-based accounting;
- there was a fundamental difference in nature and in the mode of operation between the OLAS and the SLAS. The SLAS, operated on a contingency fund basis, had been set up as a self-financing scheme. The successful aided person would pay to the SLAS Fund a percentage of the damages recovered to support the administration cost and the costs of other cases under the SLAS, so as to maintain self-sufficiency of the Scheme;
- the OLAS, like many other government services, was a form of public service which incurred expenditure on the Government. Though it also received payments, its objective was not to make a profit or surplus. Indeed, it could never make a profit. The design of the OLAS was such that the LAD could at best recoup only the expenses it had paid out for the purpose of the legal aid proceedings. The LAD bore the entire cost for processing applications and their subsequent monitoring. Against this background, the expenditure of the OLAS should not, as a matter of principle, be used as a benchmark to measure the success or otherwise of the Scheme, bearing in mind that the policy objective for the OLAS was to ensure that no one with a reasonable case for pursuing or defending legal proceedings should be denied access to court because of lack of means;
- the current cash-based presentation of financial information on the OLAS in the Annual Estimates was in line with the format adopted by other departments in the Estimates in respect of services provided to the public. Under the cash-based accounting principle, legal aid costs incurred for the OLAS were recorded on a rolling basis and a position at a point in time or in a period of time was shown in the Annual Estimates with the primary aim of monitoring the expenditure of legal aid costs to ensure that the expenditure stayed within the approved estimates. Similarly, the costs recovered from legal aid cases for a financial year were also recorded on a rolling basis and a position at a point in time or in a period of time was also shown in the Annual

Revenue Estimates. It was, however, not necessary to match the actual income and expenditure in order to ascertain the surplus or deficit as the OLAS was not a self-financing scheme and would never make a profit;

- as for the SLAS, because of its self-financing nature, it was of the greatest importance to ensure the financial well-being of the fund at all times. To this end, the financial statements for the SLAS differed from the usual format for other government services, including the OLAS, and were prepared on an accrual basis. The statement of income and expenditure showed income and expenditure for a financial year on accrual basis, so as to identify surplus or deficit for that year. Some of the income or expenditure items were directly related to the finalised cases, e.g. payment from aided persons out of damages recovered from finalised cases, and legal costs and disbursements incurred in the finalised cases, but some did not, e.g. administration cost incurred in the processing of applications and monitoring of cases, and bank interest and charges. The balance sheet showed the accumulated balance of the fund as at the end of the financial year. Similar accounting arrangements were adopted for other government funds which were run on a self-financing basis, e.g. trading funds operated by trading fund departments;
- in the light of the above, it would not be cost-effective or appropriate to adopt the accrual-based accounting principle and to prepare financial statements for the OLAS cases on a par with the accounting arrangements in respect of the SLAS. The reasons were as follows:
 - (a) given the nature of the OLAS which was not a self-financing scheme, the costs incurred would invariably exceed the income. Preparing financial statements similar to those for the SLAS, the main purpose of which was to show the surplus or deficit position so that the LAD could monitor the viability of the fund, would not provide additional meaningful or useful information to both the LAD and the users;
 - (b) the current cash-based accounting principle adopted for the OLAS was in line with service wide arrangements. The LAD had consulted the Director of Accounting Services who had also advised that the present different formats of the financial statements for the OLAS and the SLAS were in line with the accounting policy of the Government for monitoring the financial aspects of the two legal aid schemes;
 - (c) the use of the accrual-based accounting involved an overhaul of the LAD's current system, e.g. the staff costs for processing and monitoring thousands of cases had to be apportioned, staff (officers and clerical alike) would need to clock their activities and input the time into the system even though the costs were not to be recovered, and the current Case Management and Case Accounting System had to be overhauled as well. The additional resources implications for enhancement of the

system would be significant and the time taken for staff to clock and input into the system the time spent on every piece of work that they had carried out would inevitably hamper the efficiency and effectiveness of the services provided to the public if there was no additional manpower provided; and

(d) as the Government still adopted cash-based accounting for its General Revenue Account, it meant that the LAD would have to run both systems in parallel. The existing accounting support resources, one Treasury Accountant and one Accounting Officer I, would have to be increased significantly to undertake the large volume of extra work generated; and

- against the above background, Audit had decided not to include in its recommendations its original proposal for the adoption of such accounting arrangements.

8. The Committee noted from paragraph 2.13 of the Audit Report that, in its 1995-96 Controlling Officer's Report, the LAD reported the "amount of damages, maintenance and costs recovered as % of total amount due to department and aided persons". The percentages were 31.4% in 1993, 53.9% in 1994 and 40% in 1995. Since then, the LAD had not provided similar statistics in its Controlling Officer's Reports. The Committee asked:

- why the LAD had not continued to provide the statistics in its subsequent Controlling Officer's Reports; and
- whether the LAD would disclose these statistics to the public in future.

9. The **Director of Legal Aid** responded in his letter that:

- since 1995-96, the LAD had discontinued the preparation of statistics on "amount of damages, maintenance and costs recovered as % of total amount due to department and aided persons". It had been accepted that there was no direct relationship between the LAD's performance and the damages/costs recovery ratio. A higher or lower ratio in a year could not serve as a relevant or reliable indicator of the LAD's performance in that year. The recovery ratio was indeed affected by many external factors beyond the control of the LAD. The most pertinent ones being the nature of the cases involved, the financial circumstances of opposite parties and the general economic situation in Hong Kong, as elaborated below:

Recovery of legal costs by the Legal Aid Department

- (a) *Case nature:* Experience showed that full recovery of damages and costs was more likely or achievable only in personal injuries claims because most, if not all, of the opposite parties were insured. In some cases, payment was underwritten by bodies such as the Employees Compensation Assistance Fund Board and the Motor Insurers' Bureau;
 - (b) *Financial circumstances of opposite parties:* About 92% of the legal costs written off in 2004-05 were attributable to two types of cases, namely, wages claims against insolvent employers (at \$38 million, or 61%) and matrimonial cases (at \$ 19.4 million, or 31%). For insolvency cases, by nature, the chance of recovery was very slim since the employers who were the judgment debtors were invariably financially insolvent, and were the subjects of either a bankruptcy or winding-up order. As for matrimonial cases, many of the judgment debtors faced similar financial difficulties as the aided persons. They were often unemployed or of low income, and their financial well-being was particularly susceptible to changes in the economic situation in Hong Kong; and
 - (c) *Economic situation in Hong Kong:* The impact of the economic situation in Hong Kong on costs recovery rate was best illustrated by the drastic drop in the write-off amount for the first six months of 2005-06 which was \$18.3 million, 45% less than that in the same period in 2004-05. This helped to show that judgment debtors in legally aided cases were particularly vulnerable to the economic downturn in the past few years, and also helped to explain the reason for their failure to pay costs due to aided persons;
- the LAD had explained the above to Audit during the course of the audit review, and took it that Audit had accepted the LAD's explanation as Audit had not included in its recommendations its original proposal for the LAD to reintroduce the compilation of the percentage recovery statistics. The replacement proposal for the LAD to identify additional indicators for evaluating the efficiency and effectiveness of legal aid services had been accepted by the LAD; and
 - in view of the concern expressed by the Committee, the LAD would make the information available to the public.

10. According to paragraph 2.15 of the Audit Report, the LAD had paid \$16.9 million in 2003-04 and \$22.2 million in 2004-05 by way of legal costs to the opposite party in respect of cases where judgment was in the latter's favour. The Committee asked, for transparency and public accountability purposes, whether the LAD would disclose such information in its annual reports and website in future.

11. The **Director of Legal Aid** advised that:

- the amount of legal costs paid to opposite parties bore no direct relationship with and provided little information on the performance of the LAD. By law, legal aid should be granted where there was a reasonable case for court proceedings. It was not the policy objective that legal aid should only be granted to a cast-iron case. Neither would it be appropriate to use the outcome of court cases or the amount of legal costs paid to opposite parties as the LAD's performance indicator;
- the LAD took it that Audit had accepted its explanation as the latter had not included in its recommendations its original proposal on the requirement for statistics of payment of legal costs to the opposite party; and
- in view of the concern raised by the Committee, the LAD would provide the information to the public. Indeed, the LAD had been actively exploring various alternatives and drawing reference from experience of overseas legal aid authorities. It would keep the Committee informed of the developments.

12. In response to the Committee's enquiry on the adoption of a computerised staff time-charging system by the LAD, the **Director of Legal Aid** informed the Committee that:

- the computerised staff time-charging system commonly adopted by professional firms was to record the staff time expended in each case and the staff cost incurred, for the purpose of cost management and billing arrangements; and
- the LAD had in place a similar computerised system, namely, the time-costing programme in respect of areas of work for which costs were chargeable for in-house litigation cases. The objective of this system was to support costs assessment and generate bills of costs similar to the arrangements in professional firms in private practice.

B. Enforcement proceedings against judgment debtors

13. The Committee noted Audit's view in paragraph 4.12 of the Audit Report that, in conducting searches for judgment debtors' addresses, the LAD should coordinate the requests and send them, in computer-readable form, periodically to all relevant government departments and the Hospital Authority which might have such information. In response to the Committee's enquiry as to whether the LAD would adopt this arrangement, the **Director of Legal Aid** stated that:

- in taking enforcement proceedings, the LAD was acting as solicitors of aided persons in civil proceedings. That being the case, the LAD owed a duty to act professionally not only to the aided person but also to the court. Costs and disbursements incurred in the enforcement proceedings might only be recovered from the opposite party if the LAD could demonstrate to the court that it was proper and necessary to incur them and that the amounts incurred were fair and reasonable. The need for and the frequency of conducting searches for addresses as well as assets and income of judgment debtors must therefore be determined by the facts of the cases in question. Since each case was different, action should be taken only where the circumstances of a particular case warranted it. It was also noteworthy that, for costs that could not be recovered from the opposite party, they would be borne by the aided person where property had been recovered or by the public fund in other cases. Hence, there was a need to be prudent in conducting enforcement proceedings;
- the LAD had indeed been sending requests to all relevant government departments and the Hospital Authority if, based on the facts of the cases in question, there were reasons to believe that these departments/agencies might have the required information. The LAD assured the Committee that it would continue to exercise its professional judgment with due care and would make its best endeavours in this regard;
- regarding the form of delivery, the LAD had already been sending requests in electronic forms and templates wherever possible. It would continue to do so; and
- in making the relevant searches, the LAD should exercise prudence in deciding what was the “relevant” organisation that might have the information required for the specific case in question, bearing in mind that:
 - (a) the costs of the searches might need to be borne by the aided person where property had been recovered or by the public fund, and the LAD should hence minimise unnecessary searches and reduce related costs. If the LAD was to conduct all the searches with the departments/agencies set out in paragraph 4.9 of the Audit report, the costs of the searches would come to about \$3,500 for each case; and
 - (b) the work involved, not only in respect of the LAD, but also of the receiving departments, could be substantial if such searches were conducted indiscriminately or, as a matter of course, bearing in mind that there were a large number of such searches ongoing at any one time. For example, there were currently about 370 address searches being conducted each month. The cumulative effect and hence the workload for the departments/agencies on the receiving end would be significant. It was imperative that the LAD should be prudent and should ensure

that the searches were relevant and likely to be useful before requiring the departments/agencies to devote resources to facilitate the searches. For instance, the LAD should not insist on a particular area of search if the instructions given by the aided person and the information to the LAD already showed that a department/agency did not possess or could not provide the information required.

14. The Committee also noted Audit's view in paragraph 4.17(b) of the Audit Report that, for cases other than those with sufficient and clear reasons for write-off, the LAD should consider conducting searches for assets and income of judgment debtors at the Land Registry, Companies Registry, Business Registration Office and Transport Department. The Committee asked whether the LAD would adopt Audit's proposal and conduct such searches.

15. The **Director of Legal Aid** pointed out that the LAD would only write off outstanding costs when there were sufficient reasons for doing so. As the costs of the searches might need to be borne by the aided persons or by the public fund eventually, the LAD had reservations about indiscriminate searches on an across-the-board basis, without paying due regard to the facts of the case. Nevertheless, the LAD assured the Committee that it would endeavour to conduct relevant and appropriate searches among identified departments, with due consideration given to the circumstances of each case.

16. According to paragraph 4.19 of the Audit Report, the LAD has laid down seven types of legal proceedings for taking enforcement actions against judgment debtors. The Committee noted Audit's view in paragraph 4.22 that the LAD should prepare a checklist of enforcement actions to help its staff document the actions taken, together with the results, and the reasons for not pursuing certain courses of action. In this connection, the Committee asked whether the LAD would adopt the proposed checklist arrangement.

17. In his letter, the **Director of Legal Aid** replied that:

- in determining the mode of recovery action for a particular case, the professional officer had to assess, subject to the circumstances of the case, the prospect of success of such action and which mode of action was the most cost-effective. Indeed, Audit had not included in its recommendations its original proposal on the requirement for the above checklist arrangement; and
- in view of the Committee's concern, the LAD would consider the format of the proposed checklist and see how it could be put to effective use before writing off outstanding costs.

C. Administration of outstanding and irrecoverable legal costs

18. The Committee noted from paragraph 5.10 of the Audit Report that the Director of Accounting Services agreed with Audit that outstanding legal costs awarded to the aided person were, in substance, government revenue and therefore should be included in the annual returns of arrears of revenue as laid down in Standing Accounting Instruction (SAI) 1020. However, as revealed in paragraph 5.16(a), the LAD considered that as costs owed by the opposite party in legally-aided proceedings pursuant to a court order were debts due to the aided person and not to the Government, such costs did not fall within the ambit of SAI 1020 and should not be included in the annual returns of arrears of revenue. As the Director of Accounting Services was the official who had been authorised to interpret the SAIs, the Committee asked the Director if she maintained her view that the LAD should include in its annual returns of arrears of revenue outstanding legal costs awarded to the aided person.

19. In her letter of 1 December 2005, the **Director of Accounting Services** reaffirmed her view that, to facilitate monitoring, the Director of Legal Aid should provide her with an annual return on the outstanding legal costs awarded to aided persons. She added that, taking into account the special circumstances of the LAD, the Treasury would work with the Director of Legal Aid to design a specific form for use by the LAD in future reports to the Treasury on outstanding legal costs awarded to aided persons.

20. In response to the Committee's question as to whether the LAD would include in its annual returns of arrears of revenue outstanding legal costs awarded to the aided person, the **Director of Legal Aid** stated in his letter that:

- to enhance public accountability and facilitate monitoring, the LAD agreed with the Director of Accounting Services on the need for the LAD to compile annual returns on the outstanding legal costs awarded to aided persons;
- taking into account the legal position that costs due from an opposite party were costs due to the aided person and not to the Government, as confirmed by legal advice of the Department of Justice, it would not be appropriate to report such amounts in the specific annual returns of arrears of revenue, under SAI 1020, due to the Government;
- an alternative and pragmatic way forward could be for the LAD to devise appropriate reports to the Director of Accounting Services to achieve the same objectives underlined by Audit. In this regard, the LAD noted the Secretary for Financial Services and the Treasury's advice in paragraph 5.17 of the Audit Report that the LAD might consider including the amounts in other suitably formatted reports. Hence the proposed alternative report to the Director of Accounting Services; and

- the LAD would work closely with the Director of Accounting Services to design a specific form to cater for the special circumstances of the LAD. It was confident that the two departments would be able to develop a mutually agreeable format for the LAD to report on outstanding legal costs awarded to aided persons in future. The LAD would keep the Committee informed of the progress.

21. The Committee noted from paragraph 5.11 of the Audit Report that, following Audit's request in May 2005 for the LAD to provide it with a list of legal aid cases with outstanding legal costs to be recovered, the LAD had only provided a list of cases where there had been outstanding instalment payments due to the LAD. In response to the Committee's request for the provision of a list of legal aid cases with outstanding legal costs to be recovered as at 31 March 2005, the **Director of Legal Aid** said in his letter that:

- the LAD and Audit had had detailed discussions on the specific cut-off or point in time that legal costs due to an aided person should be regarded as outstanding legal costs to be recovered. This was because there were many external but complex issues that would affect the progress and outcome of a particular case. For instance, an opposite party might appeal against the costs order or the court order as a whole, the amount of costs had to be agreed or assessed by the court, or the opposite party might seek a review even after the court had determined the costs after taxation; and
- in the light of the above, the LAD had explained to Audit that it might arrive at the outstanding costs to be recovered only when an opposite party had agreed to pay the costs by signing an undertaking or had been ordered by the court to pay the costs by instalments. It was on this basis that Table 6 in paragraph 5.11 of the Audit Report had been prepared to capture the amount of outstanding legal costs to be recovered as of 31 March 2005.

D. Audit's access to legal aid case files

22. The Committee noted from paragraphs 6.9 and 6.10 of the Audit Report that, regarding those aided persons who had not given consent to Audit's access to their case files, the LAD had discussed with Audit in February 2005 the possibility of providing Audit with photocopies of the case files selected by Audit with the personal data concealed. The LAD had informed Audit in May 2005 that the production of such photocopied case files involved photocopying of voluminous files and efforts of the LAD's staff, including professional officers who needed to go through the files to ensure that there was no inadvertent disclosure of personal data. As a result, Audit could only examine 173 case files, i.e. 26% of the 661 case files selected by Audit.

23. In response to the Committee's question as to whether the LAD would, in future, use the same reasons given in May 2005 to refuse making photocopies of the case files selected by Audit, the **Director of Legal Aid** clarified in his letter that:

- the LAD had undertaken to continue to facilitate Audit's access to its case files even for cases to which the legally aided persons had not granted their consent for such disclosure. In these cases, the LAD would stand ready to make photocopies of the case files with all personal data obliterated. This would serve to balance the need for Audit to have access to case files to conduct value for money audits, whilst observing the need to respect the fundamental right of privacy of the aided persons;
- as to the incident above, the LAD had on no occasion refused to photocopy the case files. While the discussion of the possibility of making photocopies of case files had taken place in February 2005, Audit had requested on 26 April 2005 to have the files of 513 cases for inspection, with a request that the files be provided within a month's time. The LAD had immediately begun to seek consent from the 500-odd aided persons to disclose their case files to Audit. As Audit might require photocopies of those files where the aided persons had refused to give consent, the LAD had invited Audit to consider, before it made a decision, the resource constraints for the LAD to provide the large volume of case files with all the personal data removed manually. The LAD had also appealed to Audit that, should it decide to have photocopies of case files, the number of such files be kept to a manageable size; and
- the LAD, though facing the problem of limited resources, would always stand ready to cooperate with Audit to facilitate its value for money audits. Nevertheless, the LAD would make its best endeavours to render assistance within a reasonable remit.

24. Paragraph 6.12 of the Audit Report revealed that the LAD would consider setting up an independent team of its staff to conduct examination of case files selected by Audit where consent of the aided persons had not been given. In response to the Committee's enquiry about the progress made in this regard, the **Director of Legal Aid** advised, in his letter, that the LAD had engaged its internal audit team to examine the case files in question with a view to identifying non-compliance with the LAD's relevant guidelines as well as areas for improvement. The LAD would keep the Committee informed of the progress in due course.

E. Follow-up action

25. The Committee notes the replies of the Director of Legal Aid and the Director of Accounting Services and wishes to be kept informed of the progress of the various courses of action taken by the LAD.