

香港特別行政區政府
工商及科技局
工商科



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19 December 2002

Clerk to Public Accounts Committee
(Attn : Miss Sandy CHU)
Legislative Council Building
8 Jackson Road,
Central, Hong Kong


Dear Ms CHU,

**The Director of Audit's Report on the
results of value for money audits (Report No. 39)**

**Chapter 5 : Special Finance Scheme for
small and medium enterprises**

Thank you for your letter dated 8 December 2002. The information requested is attached for the Committee's perusal please. We shall separately let you have the reply to item (c) as soon as practicable.

Yours sincerely,


(Anita Chan)

for Secretary for Commerce, Industry and Technology

c.c.

Secretary for Financial Services and the Treasury	(Fax no. 2537 1736)
Director-General of Trade and Industry	(Fax no. 2789 2491)
Director of Accounting Services	(Fax no. 2598 9273)
Director of Audit	(Fax no. 2583 9063)

**The Director of Audit's Report on the
Results of the Value for Money Audits (Report No. 39)
Additional Information to the Public Accounts Committee regarding the
Special Finance Scheme for Small and Medium Enterprises**

- (a) *The monthly amount of guarantees offered by the Government in the period leading to the review of the operation of the Special Finance Scheme for Small and Medium enterprises (the Scheme) in December 1998.*

The Special Finance Scheme for SMEs (the Scheme) was launched in August 1998. The Administration conducted a review of the Scheme in December 1998. The review recommended, among other things, that :

- (a) the risk sharing ratio between the Government and participating lending institutions (PLIs) should be revised from 50:50 to 70:30;
- (b) the maximum guarantee period should be extended from one year to two years; and
- (c) the “no overdue loan” declaration should be removed.

Revisions to the Scheme were endorsed by the Finance Committee of the Legislative Council and put in place in late April 1999.

For the eight months from August 1998 to April 1999, the amount of guarantee approved was about \$856 million (The entire amount of the initial commitment of \$2.5 billion was used up by end of August 1999, i.e. four months after the implementation of the aforementioned revisions.)

Monthly breakdown of the number of approved cases and the amount of guarantee approved during the period from August 1998 to April 1999 is as follows :

	<u>Number of approved cases</u>	<u>Amount of guarantee approved</u>
Aug. 1998	0	0
Sep. 1998	93	about \$88 million
Oct. 1998	201	about \$138 million
Nov. 1998	240	about \$161 million
Dec. 1998 (The review was conducted)	196	about \$116 million
Jan. 1999	186	about \$106 million
Feb. 1999	127	about \$57 million
Mar. 1999	228	about \$91 million
Apr. 1999	245	about \$99 million
Total	1 516	about \$856 million

(b) In view of the consequences of the absence of a clear provision in the Deed on the prohibition of offloading bad loans onto the Scheme (with reference to paragraphs 2.21(b) and 2.24(a)), whether the Deed should have been revised to introduce additional safeguards against the possible abuse of the scheme in this regard by participating lending institutions (PLIs); if so, the direction of the revision;

At the time when the Scheme was devised, SMEs in Hong Kong were facing severe cashflow problems and were unable to secure finance due to the liquidity crunch. Indeed, many were no longer able to make repayments to existing loans as scheduled. Had we stated in the Deed that loan restructuring was disallowed, lending institutions would simply recall the loans, and a lot of SMEs would have been forced to wind up their businesses as a result. This would have been against the objective of setting up the Scheme which aimed at relieving the financial hardship of SMEs when Hong Kong was undergoing a particularly difficult time after the Asian Financial crisis.

In view of the unique liquidity crunch at the time and judging from the encouraging outcomes that more than 92% of the loans guaranteed under the Scheme are performing or are fully repaid, we consider that we had made the right decision not to prohibit loan restructuring under the Scheme in the Deed. But this does not mean that we do not consider it necessary to provide additional safeguards for similar funding schemes when the circumstances are different. Indeed when we launched the SME Business Installations and Equipment Loan Guarantee Scheme in 2001, we had included in the Deed provisions expressly disallowing borrowers and lenders to use the scheme for loan restructuring, partly because of the improved financing environment for

SMEs as compared with 1998. We shall continue to devise our SME funding schemes with the aim of striking the right balance between upholding fiscal prudence and providing necessary support to SMEs.

(d) Before the Scheme was launched, whether the then Trade and Industry Bureau (TIB) had given instructions to the Department of Justice on the drafting of the Deed regulating the prohibition of offloading bad loans onto the Scheme;

(e) If the answer to (d) is in the affirmative, please provide the following information:

- (i) a copy of the comments of the Department of Justice on this point;*
- (ii) if the Department of Justice had considered that there should be a clause in the Deed prohibiting the offloading of bad loans, the officer(s) in the TIB made the decision for not including such a clause in the Deed; and when and why the decision was made;*

We can find no written record of the then Trade and Industry Bureau (TIB) giving instructions to the Department of Justice (DOJ) on the drafting of the Deed regarding the prohibition of offloading bad loans onto the Scheme. As described in the Audit Department's Report, TIB has however explained to the relevant parties, including the Hong Kong Monetary Authority and the Treasury, that it considered the Deed need not be amended to include provisions disallowing the restructuring of loans.

- (f) *The respective amounts of the funds available for the Scheme eventually used for helping SMEs and for settling claims for compensation from PLIs*

The relevant statistics are as follows-

- initial capital amount (i.e. expected total expenditure): \$2.5 billion
- expected total commitment : \$5 billion
- actual amount of guarantee approved : \$5.8 billion ^(Note)
- net amount of compensation claimed as at 12.12.2002 (including cases being processed): \$439 million

Note : The actual amount of guarantee provided by the Government is greater than \$5 billion, because funds released from matured loans were ploughed back for providing guarantee as well..

- (g) *When launching similar schemes in future, how the Government could strike a balance between competing objectives or principles of the schemes.*

When launching similar schemes in future, we would aim to strike the right balance between achieving the objectives of the schemes (including the market-driven principle), and putting in the necessary safeguards to avoid abuse of the schemes. We would also consult widely before deciding on the means that will maximize the usefulness of the schemes while ensuring that public money will be used properly.

A case in point is the SME Business Installations and Equipment Loan Guarantee Scheme (BIG) launched in December 2001 which aims at helping

SMEs get loans to acquire business installations and equipment for enhancing their competitiveness. To achieve this objective as well as to ensure that public money is properly spent, we have made it clear that SMEs are not allowed to use the scheme to refinance business installations and equipment already in their possession or in the possession of their associates. The Deed signed with PLIs also expressly disallows borrowers and lenders to use the scheme to repay, restructure or repackage other loan facilities, including doubtful or bad loans.

We will continue to maintain the right balance in implementing the latest recommendations of the Small and Medium Enterprises Committee on enhancing the effectiveness of BIG.

In addition, after the launch of any loan guarantee scheme, we would continue to monitor closely the performance and effectiveness of the scheme and, if necessary, make adjustments to ensure that we are indeed striking the right balance between competing considerations.