

ITEM FOR FINANCE COMMITTEE

**HEAD 156 – GOVERNMENT SECRETARIAT : EDUCATION BUREAU
Subhead 700 General non-recurrent
New Item “Funding Support to the Hong Kong Examinations and Assessment
Authority”**

Members are invited to approve a new commitment of \$360.8 million to support the effective operation of the Hong Kong Examinations and Assessment Authority for four years from 1 September 2018 to 31 August 2022.

PROBLEM

The Hong Kong Examinations and Assessment Authority (HKEAA) is running into financial difficulties in maintaining its effective operation and sustaining the administration of the Hong Kong Diploma of Secondary Education (HKDSE) Examination.

PROPOSAL

2. The Secretary for Education proposes to create a new commitment of \$360.8 million as a one-off funding support to enable HKEAA to sustain the administration of the HKDSE Examination for four cohorts from 2019 to 2022, and thereby enable its effective operation for four years from 2018/19 to 2021/22¹.

/JUSTIFICATION

¹ Unless otherwise specified, the “year” in this paper refers to the financial year of HKEAA, which runs from 1 September of a year to 31 August of the following year.

JUSTIFICATION

HKEAA's operation

3. According to the HKEAA Ordinance (Cap. 261), the HKEAA's main statutory responsibility is to conduct the "specified examinations", which currently refers to the HKDSE Examination. It is therefore the HKEAA's single most important duty to professionally administer the HKDSE Examination and to ensure fair and just assessment of all candidates. It also runs a number of fee-charging examination and assessment services commissioned by the Government or outside bodies, including the Territory-wide System Assessment (TSA), Language Proficiency Assessment for Teachers (LPAT), and a range of international and professional examinations (IPEs).

4. The HKEAA operates on a self-financing basis and does not receive any recurrent subvention from the Government though in the past, the Government provided the HKEAA with non-recurrent grants for specific initiatives/projects to assist towards the cost of conducting public examinations. The HKEAA's income is mainly derived from the HKDSE examination fees and service fees paid by organisations that engage its services, followed by the sale of publications and provision of assessment services for organisations and individuals. In 2017/18, the income related to the HKDSE Examination accounted for about 52% of HKEAA's income, while that related to IPEs and other local examinations (including TSA and LPAT) contributed to the remaining share of the income.

Continuous operating deficits of HKDSE examination

5. The HKDSE Examination was introduced in 2011/12. As shown in Table 1 below, except the first two cohorts, HKDSE Examination has been running at an increasing deficit, which has been aggravating the financial position of the HKEAA. For 2017/18, the HKDSE Examination recorded a deficit of about \$70 million, leading to an overall deficit of about \$10 million for HKEAA, partly offset by income from other examinations/activities.

/Table 1:

Table 1: Overall financial position of the HKEAA since implementation of the HKDSE Examination in 2011/12

Year		Income (\$ million)	Expenditure (\$ million)	Surplus/ (Deficit) (\$ million)	HKEAA's Overall Surplus/ (Deficit) (\$ million)
2011/12	HKDSE [#]	219.1	206.1	13.0	63.9
	Others [*]	381.5	330.6	50.9	
2012/13	HKDSE [#]	259.6	247.4	12.2	60.8
	Others [*]	284.1	235.5	48.6	
2013/14	HKDSE [#]	253.1	278.7	(25.6)	7.4
	Others [*]	215.7	182.7	33.0	
2014/15	HKDSE [#]	237.1	281.3	(44.2)	(6.1)
	Others [*]	210.4	172.3	38.1	
2015/16	HKDSE [#]	223.5	280.5	(57.0)	(19.7)
	Others [*]	185.2	147.9	37.3	
2016/17	HKDSE [#]	213.0	278.4	(65.4)	(16.5)
	Others [*]	197.4	148.5	48.9	
2017/18	HKDSE [#]	215.0	284.2	(69.2)	(10.1)
	Others [*]	199.7	140.6	59.1	

This covers HKDSE Examination fees and services/activities related to the HKDSE Examination (such as publications).

* Other examination services and other activities.

Declining candidature for HKDSE Examination

6. Between 2012/13 and 2017/18, the number of candidates taking HKDSE Examination has significantly dropped by about 28%. According to the population projection of the Census and Statistics Department², during 2018 to 2021, the population of the age group between 15 and 19 residing in Hong Kong will decrease continuously. It is expected that the number of HKDSE candidates during the same period will continue to drop along with the change in population size of the relevant age groups. The actual/projected number of HKDSE Examination candidates since it was introduced in 2011/12 is set out in Table 2 below.

/Table 2:

² Released in September 2017.

Table 2: Actual/projected number of HKDSE Examination candidates

School Year	Actual/Projected Number* of HKDSE Examination Candidates
2011/12	73 074
2012/13	82 283
2013/14	79 572
2014/15	74 131
2015/16	68 128
2016/17	61 624
2017/18	59 000
2018/19	55 100
2019/20	51 400
2020/21	48 700
2021/22	47 400

* Projected figures for 2018/19 to 2021/22 are rounded to the nearest hundred.

Cost structure and increasing cost for administering the HKDSE Examination

7. Owing to the wider choice of subjects and the fewer number of subjects that a candidate takes, the cost per candidate of the HKDSE Examination is higher than that of the previous Hong Kong Certificate of Education Examinations (HKCEE). To illustrate, the cost per candidate for the HKDSE Examination in 2013/14 with about 80 000 candidates was about \$3,500, while that for the last HKCEE for school candidates in 2009/10 with about 127 000 candidates was about \$1,200. In addition, the HKEAA considers that many of the expenditure items for administering the HKDSE Examination are fixed cost which cannot be reduced proportionately with the decrease in the number of candidates. These include costs of HKEAA staff and examination personnel (e.g. paper setters, moderators and proof-readers), operating cost for onscreen marking assessment centres, information technology systems and data processing, and venue cost, etc. The costs of renting examination centres and on-site examination personnel may only decrease slightly because of the need to maintain a reasonable geographical spread of examination centres over the whole of Hong Kong. Such fixed/invariable costs take up about 75% of the overall cost.

8. Another significant increase in the operating cost for administering the HKDSE Examination is the special examination arrangements (SEAs) for candidates with special educational needs (SEN). Between 2011/12 and 2017/18, the number of candidates with SEN has increased by about 152%, with a corresponding increase in expenses on SEAs, including special centres, braille question papers, speech-to-text software, ancillary aids for candidates with visual and aural disabilities, etc. Currently, the SEA costs are fully borne by the HKEAA without any special charge to SEN candidates. Having regard to the past trend, it is estimated that the SEA-related cost will further increase from the present level of about \$14.7 million to more than \$20 million in a few years' time. The number of candidates with SEN and SEA-related cost from 2011/12 to 2021/22 are set out in Table 3 below –

Table 3: Number of candidates with SEN and SEA-related costs^{*}

School Year	Number of Candidates with SEN	SEA-related Cost (\$ million)
2011/12	1 056	3.1
2012/13	1 208	3.6
2013/14	1 595	7.2
2014/15	1 746	10.7
2015/16	2 047	12.1
2016/17	2 442	14.6
2017/18	2 666	14.7
2018/19	3 600	18.4
2019/20	3 700	19.4
2020/21	3 700	20.5
2021/22	3 900	23.1

* The number of applications from candidates with SEN in 2018/19 to 2021/22 are projected figures rounded to the nearest hundred.

No significant increase in profit from IPEs

9. In recent years, the HKEAA has been able to derive profit by undertaking entrusted IPEs in Hong Kong (such as the Associated Board of the Royal Schools of Music examinations, Scholastic Aptitude Test, General Certificate of Secondary Education examinations and Australian Teachers of Dancing Exams), to partially offset the aggravating deficit attributed to the HKDSE Examination. The number of candidates taking IPEs in Hong Kong has been

/relatively

relatively stable from 2012/13 onwards, ranging from the peak level of 309 000 in 2012/13 to the lowest level of 277 000 in 2016/17. It is expected that the number of IPE candidates will not change significantly in the coming few years and thus the contribution to the income of the HKEAA will be relatively stable.

Long-term viability of the HKEAA

10. At present, the HKDSE Examination fees only recover about 65% of the cost. Given the declining candidature and structure of cost items of HKDSE, it is unlikely that the cost of HKDSE Examination could be fully recovered by the examination fees without the latter being increased substantially. Table 4 below shows the number of HKDSE Examination candidates, fee increment rates and operating surplus/deficit from the examination.

Table 4: Actual/projected number of HKDSE Examination candidates, rates of fee increment and operating surplus/deficit from the examination

School Year	Number of HKDSE Examination Candidates ^{Note 1}	HKDSE Examination Fee Increment ^{Note 2} (%)	Operating Surplus/(Deficit) from HKDSE Examination ^{Note 1} (\$ million)
2011/12	73 074	Not Applicable	13.0
2012/13	82 283	5	12.2
2013/14	79 572	0	(25.6)
2014/15	74 131	0	(44.2)
2015/16	68 128	2	(57.0)
2016/17	61 624	3	(65.4)
2017/18	59 000	4	(69.2)
2018/19	55 100	4	(105.2)
2019/20	51 400	2.5	(120.5)
2020/21	48 700	2.5	(128.9)
2021/22	47 400	2.5	(141.7)

^{Note 1} Projected figures for 2018/19 to 2021/22. The projected number of candidates is rounded to the nearest hundred.

^{Note 2} The annual rate of fee increment for 2019/20 to 2021/22 is assumed to be 2.5%, which is in line with the inflation rate in Government's medium range forecast.

11. The rates of HKDSE Examination fee increase since 2012/13 ranged from 2% to 5%, which were determined taking into account factors such as the HKEAA's overall financial position, the costs and resources required, the inflation rate, local economic situation and affordability of families in general. It is estimated that to fully recover the cost of the HKDSE Examination, after taking into account the projected profit from IPEs etc., the rate of fee increase would have to set at around 50% for the 2019/20 HKDSE Examination and followed by a double-digit increment in the subsequent year. This will certainly go against public expectation.

Need for one-off grant

12. The current mode of operation and cost structure of the HKEAA obviously could not support the long-term operation of HKDSE Examination. As at end 2017/18 (i.e. 31 August 2018), the cash balance of the HKEAA was about \$189 million. The HKEAA estimates that it would run out of sufficient cash to maintain effective operation in the second half of 2019, and the liquidity problem is expected to aggravate in subsequent years. To allow time for the HKEAA, in consultation with the Government, to study in detail how to alleviate the serious deficit problem and to work out a long-term solution, the Chief Executive announced in the 2018 Policy Address that the Government would provide the HKEAA with a non-recurrent funding of \$360 million in four years to support the effective operation of the HKEAA during the period.

FINANCIAL IMPLICATIONS

13. Taking into account HKEAA's funding requirements for maintaining its operation, financial commitment and development needs (such as development or upgrading of information technology systems for administration of examination and for general organisational administration and maintenance of HKEAA premises, etc), its current financial position as well as projected profit from IPEs, HKEAA estimates that it will require funding support of \$328 million from the Government in the coming four years. It is also proposed that a contingency of \$32.8 million, equivalent to 10% of the above sum of \$328 million, be provided to cater for unforeseen or unexpected expenditure items required for conducting public examinations. The total requirement is therefore \$360.8 million for four years. The major assumptions of HKEAA's estimates are set out at the Enclosure.

Encl.

14. The estimated cash flow requirement in government financial year is as follows. The actual cash flow requirement may be adjusted to meet possible committed/contingency payment arising from 2018/19 to 2021/22 to be made by the HKEAA.

/Item

Item	2019-20 (\$ million)	2020-21 (\$ million)	2021-22 (\$ million)	Total (\$ million)
(a) Estimated requirement	82.4	124.1	121.5	328.0
(b) Contingencies	8.3	12.4	12.1	32.8
Total	90.7	136.5	133.6	360.8

CONTROL AND MONITORING MECHANISM

15. The proposed commitment of \$360.8 million represents the estimated maximum amount of government funding required by the HKEAA from 2018/19 to 2021/22. Notwithstanding HKEAA's current estimates of its future funding needs, the Government will carefully scrutinise the HKEAA's annual estimates, including its proposed funding requirement to maintain the minimum cash flow each year, to ensure its funding request is necessary and reasonable, and disburse the proposed one-off grant to the HKEAA by instalment. During the period, the HKEAA will continue with its endeavour to reduce cost while maintaining a high standard of examination and assessment services.

16. The existing monitoring and control mechanism as stipulated in the HKEAA Ordinance will continue to apply to ensure proper auditing of the HKEAA's accounts and proper use of government funding. In particular, the HKEAA shall submit to the Government its annual estimates of income and expenditure and programme of its proposed activities including the proposed public examination fees for approval, and table its annual audited accounts and report of its activities at the Legislative Council every year. Financial statements of each year are also published in the HKEAA's Annual Report for public information.

PUBLIC CONSULTATION

17. On 7 December 2018, the Education Bureau (EDB) consulted the Legislative Council Panel on Education (the Panel) on the proposal. Members supported the submission of the proposal to the Finance Committee for consideration. The Panel passed two motions urging the Government to provide recurrent financial funding to the HKEAA by paying the HKDSE Examination fees for school candidates on a cost-recovery basis, and to subsume the payment under the Government's 15-year free education policy. EDB explained at the meeting that the HKEAA, in consultation with the Government, will work out a proposal to ensure the long-term financial sustainability of the HKEAA. We will separately respond to the two motions passed by the Panel.

/BACKGROUND

BACKGROUND

18. The HKEAA is a statutory body established in 1977 under the HKEAA Ordinance³. It is governed by a Council with members drawn from various sectors, including tertiary institutions, schools, business and the Government. Before the HKDSE Examination was launched in 2011/12, it was responsible for the administration of the HKCEE and the Hong Kong Advanced Level Examination.

19. The Chief Executive announced in the 2018 Policy Address that the Government would provide the HKEAA with a non-recurrent funding of \$360 million in four years to support the effective operation of the HKEAA during the period. At the same time, the HKEAA, in consultation with the Government, will work out a proposal to ensure its long-term financial sustainability.

Education Bureau
January 2019

³ The HKEAA was formerly known as the Hong Kong Examinations Authority (HKEA). In July 2002, when the function of HKEA was widened to cover the administration of assessment, its name was changed to the HKEAA. The name of the previous “Hong Kong Examinations Authority Ordinance” was amended as “Hong Kong Examinations and Assessment Authority Ordinance” in the same year.

**Major assumptions adopted in projecting
Hong Kong Examinations and Assessment Authority (HKEAA)'s
financial requirements**

1. A minimum amount of cash in hand equivalent to two months' expenses should be maintained to ensure liquidity and meet the day-to-day operational needs.
2. A financial commitment to roll over different financial years for capital projects carried out by the HKEAA, e.g. building repairs, information technology systems, etc., would be created.
3. At least \$10 million or one-third of the surplus from the international and professional examinations would be kept for capacity building/development of the HKEAA, such as conducting assessment research, implementing initiatives to promote "Assessment for Learning", etc.
4. The inflation rate is assumed to be 2.5%, which is in line with the Government's medium range forecast.
5. It is assumed that in the material time, the Hong Kong Diploma of Secondary Education (HKDSE) Examination fee will continue to be charged less than its full cost, taking into consideration relevant factors including the operating costs and resources required, prevailing inflation rate, local economic situation, and affordability of the candidates and parents. For this exercise, the HKDSE Examination fee increase is assumed to be 2.5%, but the actual proposed examination fee increase submitted by the HKEAA to the Government each year will be examined in the light of the prevailing situation every year.
6. Under the existing mechanism, the actual rate of salary increase will be determined by the HKEAA Council, taking into account a host of relevant factors, including the HKEAA's overall financial position, performance of the HKEAA and staff concerned, the market pay trend (general market and civil service), economic indicators, latest trends of unemployment rates and other relevant factors, such as market competitiveness of the remuneration package for retention of staff. The Government will also examine the HKEAA's annual estimates of income and expenditure before giving approval. For this exercise, it is assumed to be 5%.
