

For discussion on 7 December 2018

## **Legislative Council Panel on Education**

### **Proposed Funding Support to the Hong Kong Examinations and Assessment Authority**

#### **Purpose**

This paper seeks Members' support for the proposed creation of a non-recurrent commitment of \$360.8 million to support the effective operation of the Hong Kong Examinations and Assessment Authority (HKEAA) for the four financial years from 1 September 2018 to 31 August 2022<sup>1</sup>.

#### **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 Hong Kong Diploma of Secondary Education (HKDSE) Examination for four cohorts from 2019 to 2022. At the same time, the HKEAA and the Government will work out a proposal to ensure its long-term financial sustainability.

#### **Justification**

3. The HKEAA is a statutory body established in 1977 under the Hong Kong Examinations and Assessment Authority Ordinance (Cap. 261) (HKEAA Ordinance)<sup>2</sup>. Its main statutory responsibility is to

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<sup>1</sup> The financial year of the HKEAA runs from 1 September of a year to 31 August of the following year.

<sup>2</sup> 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.

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 provide a fair and just assessment of all candidates. It also runs a number of fee-charging examination and assessment services, including those for the Territory-wide System Assessment (TSA)<sup>3</sup>, Language Proficiency Assessment for Teachers (LPAT)<sup>3</sup>, and a range of international and professional examinations (IPEs)<sup>4</sup>. The HKEAA operates on a self-financing basis and does not receive any recurrent subvention from the Government, though in the past the Government had also 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 made up about 52% of HKEAA’s income, while that related to IPEs and other local examinations (including TSA and LPAT) took up the bulk of the remaining share of the income.

#### Continuous Operating Deficits of HKDSE Examination

4. Except the first two cohorts, HKDSE Examination has been running at a deficit and the operating deficit has been aggravating the financial position of the HKEAA. As shown in **Table 1**, the HKEAA recorded a surplus in each of the initial years of the implementation of the HKDSE Examination from 2011/12 to 2013/14. In the succeeding years, it continuously recorded deficits. For 2017/18, it is projected that a further deficit of over \$10 million will be recorded.

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<sup>3</sup> The TSA and LPAT are commissioned by the Government.

<sup>4</sup> These IPEs are commissioned by the Government and outside bodies.

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

School Year/HKEAA's Financial 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 (Unaudited)	#HKDSE	215.0	284.2	(69.2)	(10.1)
	*Others	199.7	140.6	59.1	

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

\*Others: Other examination services and other activities

Note: The financial year of the HKEAA runs from 1 September to 31 August of the subsequent year. The provisional figures for 2017/18 are subject to auditing.

### Declining Candidature for HKDSE Examination

5. The HKDSE Examination was introduced in 2011/12. Because of the wide choice of subjects, and the fewer number of subjects that a candidate will take, the cost per candidate is relatively high when compared with previous Hong Kong Certificate of Education Examinations. This can be reflected in the operating report for 2013/14, when there were nearly 80 000 candidates. Coupled with the significant drop in the number of candidates by about 28% between 2012/13 and 2017/18, and the declining trend expected in the coming years, it is

unlikely that the cost of HKDSE Examination could be balanced by the fee collected, unless there is a significant increase in the fee against public expectation. The actual and projected number of HKDSE Examination candidates from 2011/12 to 2021/22 is shown in **Table 2** below. It is estimated that if the cost of the HKDSE Examination is to be fully recovered, even after taking into account the projected profit from IPEs etc., the fee increase would have to be around 50% for the 2019/20 HKDSE Examination, followed by a double-digit increment in the subsequent year to support the conduct of the HKDSE Examination. The actual/projected number of HKDSE Examination candidates and operating deficit from the examination are shown in **Table 2** below.

**Table 2:** Actual/projected number of HKDSE Examination candidates and operating deficit from the examination

<b>School Year</b>	<b>Actual / Projected Number of HKDSE Examination Candidates<sup>5</sup></b>	<b>Actual / Projected Operating deficit from HKDSE Examination (\$million)</b>
2011/12	73 074	13.0
2012/13	82 283	12.2
2013/14	79 572	(25.6)
2014/15	74 131	(44.2)
2015/16	68 128	(57.0)
2016/17	61 624	(65.4)
2017/18	59 000	(69.2)
2018/19	*55 100	^(105.2)
2019/20	*51 400	^(120.5)
2020/21	*48 700	^(128.9)
2021/22	*47 400	^(141.7)

\*The figures are rounded to the nearest hundred

^These are projected figures

<sup>5</sup> According to the population projection released by the Census and Statistics Department in September 2017, during 2018-2021, the population of the age group between 15 and 19 residing in Hong Kong is projected to decrease continuously from 2018, with a slight rebound in 2022. It is expected that generally speaking the number of HKDSE candidates in the future will be aligned with the change in population size of the relevant age groups.

6. At present, the HKDSE Examination fees only cover about 65% of the cost. The rates of HKDSE Examination fee increase from 2012/13 to 2018/19 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. They are set out in **Table 3** –

**Table 3:** The rates of HKDSE Examination fee increase from 2012/13 to 2018/19

School Year	HKDSE Examination Fee Increment
2012/13	5%
2013/14	0%
2014/15	0%
2015/16	2%
2016/17	3%
2017/18	4%
2018/19	4%

#### Long-term Viability of the HKEAA

7. The HKEAA considers that many of the expenditure items for administering the HKDSE Examination are relatively fixed and the related cost cannot be reduced proportionately with the decrease in the number of candidates. These include costs of HKEAA staff and examination personnel (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 involved in renting examination centres and on-site examination personnel may only slightly decrease because of the need to maintain a reasonable geographical spread of examination centres over the whole of Hong Kong. Such fixed/invariable items 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). During 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 a 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 2017/18 can be found in **Table 4** below -

**Table 4:** Number of candidates with SEN and SEA-related costs

<b>School Year</b>	<b>Number of Candidates with SEN</b>	<b>SEA-related Cost (\$million)</b>
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

\* These are projected figures. The number of applications from candidates with SEN is rounded to the nearest hundred.

#### No significant increase in profits 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 related to the HKDSE Examination. The number of candidates taking IPEs in Hong Kong has been 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 financial contribution to the HKEAA will be relatively stable.

10. It is thus quite obvious that the current mode of operation and cost structure of the HKEAA could not support the long-term operation of HKDSE Examination. The HKEAA will work out a proposal to ensure its long-term financial sustainability in consultation with the Government. It is envisaged that more time is required to study this important and complicated matter in detail. As a tide-over measure pending the comprehensive review, 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. The funding required is based on HKEAA's latest estimates on its cash requirement in the coming four years to ensure liquidity, meet various planned/committed expenses and maintain its day-to-day operation, including the administration of the HKDSE Examination, on the basis of its current operation mode and cost structure.

### **Financial Implications**

11. The HKEAA needs to maintain sufficient cash flow to ensure its smooth operation. As at end 2017/18 (i.e. 31 August 2018), subject to auditing, the estimated cash balance 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. A tentative breakdown of the estimated Government funding requirement by the HKEAA from 2018/19 to 2021/22 is as follows. The related major assumptions are set out at the **Annex**.

	<b>HKEAA's Financial Year</b>	<b>Projected Cash Balance as at 31 August (\$ million)</b>	<b>Cash Balance Required (\$million)</b>	<b>Estimated Fund Required (\$million)</b>
(a)	2018/19	106.5	115.2	8.7
(b)	2019/20	36.6	119.0	73.7
(c)	2020/21	(66.7)	139.8	124.1
(d)	2021/22	(195.6)	132.4	121.5
			<b><i>Sub-total:</i></b>	<b>328.0</b>
			<b><i>10% Contingency:</i></b>	<b>32.8</b>
			<b>Total:</b>	<b>360.8</b>

12. The estimated fund required by the HKEAA over its coming four financial years is \$328 million. A contingency of \$32.8 million, equivalent to 10% of the above sum of \$328 million, is proposed to cater for unforeseen or unexpected expenditure items to assist towards the cost of conducting public examinations. The proposed overall non-recurrent commitment is \$360.8 million.

13. The above yearly Government funding requirement is based on HKEAA's estimates, having regard to its financial position and practical needs. This covers the funding requirement to ensure HKEAA's liquidity 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. The projected profit from IPEs during 2018/19 and 2021/22 has been taken into account in estimating the above yearly Government funding requirement, and the HKEAA will continue to conduct the IPEs for profit.



## **Implementation**

14. The proposed new commitment of \$360.8 million represents the estimated maximum amount of Government funding required by the HKEAA in the four years from 2018/19 to 2021/22. In the period, the HKEAA will continue with its endeavour to reduce cost and increase income, while maintaining a high standard of examination and assessment services.

15. The Government will make use of the existing monitoring and control mechanism to ensure that the related funding allocation, reporting and auditing matters are handled properly. In accordance with the HKEAA Ordinance, 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 to the Government for approval. Notwithstanding HKEAA's current estimates of its future funding needs based on which the funding requirement is worked out, the Government will carefully scrutinise HKEAA's annual estimates, including its proposed funding requirement to maintain the minimum cash flow each year, to ensure that the funding request for each of its financial year is necessary and reasonable. The Government will disburse the approved funding to the HKEAA by batches and in light of the prevailing circumstances.

16. In accordance with the HKEAA Ordinance, the HKEAA is also required to submit its statement of accounts duly signed by the Chairman of the HKEAA to an independent auditor<sup>6</sup>. The accounts of the HKEAA and signed statement of accounts shall be audited by the appointed auditor. These arrangements will help ensure proper auditing of the HKEAA's accounts to facilitate the disbursement and the proper use of the allocated government funding. Financial Statements of each year is published in the HKEAA's Annual Report for public information.

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<sup>6</sup> The independent auditor shall be appointed by the HKEAA with the prior approval of the Government.

## **Advice Sought**

17. Members are invited to comment on the proposal. Subject to Members' views, we will seek the Finance Committee's approval for the creation of the non-recurrent commitment as soon as possible, such that the government funding could be made available to the HKEAA to ensure its liquidity.

**Education Bureau**  
**December 2018**

**Major assumptions adopted  
in projecting 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, IT systems, etc., would be created.
3. At least \$10 million or one-third of the surplus from the IPEs 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 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%.