

Summaries of Direct Investigations Completed

Housing Department (“HD”)

Case No. OMB/DI/274

Recovery of Mortgage Default Debts

(Investigation declared on 26 March 2012 and completed on 20 March 2013)

Introduction

It is the policy of the Hong Kong Housing Authority (“HKHA”) to issue mortgage default (“MD”) guarantees for properties sold under the Home Ownership Assistance (“HOA”) schemes¹ in order to secure favourable borrowing terms from the banks for the buyers. Where a property owner defaults on the mortgage, the bank may foreclose the property, and where the proceeds of sale is insufficient to cover the outstanding loan, the bank may make a claim to the Housing Department (“HD”), the executive arm of HKHA, for the shortfall. After settling the MD claim, HKHA is entitled to subrogate the bank’s rights to the loan. HD, as executive arm of HKHA, will have both the right and the duty to chase the ex-owner for the recovery of the shortfall.

2. Through a complaint case, it came to our knowledge that although HD had been settling MD claims since 1991, it only started chasing ex-owners for the MD debts 18 years later in 2009.

3. Against this background, we initiated a direct investigation to examine the magnitude of the problem and whether there was room for improvement in HD’s debt recovery arrangements.

Our Findings

4. Our investigation showed that HD had no record of any thought or discussion being given to the need to recover these MD debts before 2009.

5. In 2009 an HD internal audit on HOA units under the Secondary Market Scheme revealed that HD had incurred \$230M on 826 cases of MD claims under the Scheme, and recommended that HD should set up a mechanism to review the recoverability of the MD debts and take chasing action where appropriate.

6. In pursuance of this recommendation HD set up arrangements for the recovery of MD debts in late 2009. Although the recommendation was made in respect of Secondary Market Scheme units, HD in fact provided MD guarantees for all HOA units. Therefore, HD extended its recovery action to all HOA units.

¹ The HOA schemes are schemes under which HKHA provides subsidised home ownership flats to qualified persons. HOA schemes include Home Ownership Scheme, Tenant Purchase Scheme, Private Sector Participation Scheme and Secondary Market Scheme.

Annex 6

7. Up to end June 2012, HD had incurred a total of \$973M on 4,407 cases of MD claims. After two and a half years' of recovery action, the amount of debt recovered was about \$3.4M, or 0.3% of the total. The position of the 4,407 cases at end June 2012 was as follows:

- 1,360 cases (31%) were excluded from the review, being time-barred or involving discharged bankruptcy;
- 901 cases (20%) had 1st round review completed;
- 1,398 cases (32%) were in the process of 1st round review; and
- the remaining 748 cases (17%) were pending 1st round review.

Observations

8. The MD debts are public money and \$973M is not a small amount. For as long as HKHA's policy of providing MD guarantees for HOA buyers continues, HKHA will be subject to the potential liability of more MD claims and accumulating more MD debts. HD needs to have a proper system to manage the recovery of the MD debts, both for financial management reasons and to avoid giving the community the wrong message that debts owed to the Government need not be repaid.

9. HD's oversight and failure to take any debt recovery action for 18 years after acquiring the right to the MD debts is unacceptable. Besides, even after the setting up of a mechanism in 2009 for debt recovery, progress has been unsatisfactory and some of the arrangements put in place are inefficient and ineffective.

Recommendations

10. HD should:

Overall

- (1) draw lessons from this experience and adopt a more alert and vigilant approach in managing public money in future;

Debt Recovery Arrangements

- (2) review its operational arrangements to ensure that the appropriate order of priority is followed in handling the case work. It should consider, among other things, whether efforts should continue to be made to pursue time-barred and deceased-debtor cases, taking into account the effectiveness of such efforts, the resources available, and the existing case backlog;
- (3) review its workflow with a view to streamlining the procedures, paying particular attention to, among other things, whether its arrangements for searching addresses

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are efficient and whether the MD team can be given access to use more interview rooms;

- (4) review carefully its guidelines and strengthen training for its staff;
- (5) exercise due care and diligence in handling the MD debt cases and enhance monitoring of staff performance; and
- (6) use its best efforts to meet its target of completing 1st round review of all 4,407 cases by year 2015/16, by staff redeployment or any other means.

11. Our recommendations were generally accepted by HD.