

**REPORT OF THE
PUBLIC ACCOUNTS COMMITTEE
ON
REPORT NO. 36 OF THE DIRECTOR OF AUDIT
ON
THE RESULTS OF
VALUE FOR MONEY AUDITS**

July 2001

P.A.C. Report No. 36

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I. INTRODUCTION

The Establishment of the Committee The Public Accounts Committee are established under Rule 72 of the Rules of Procedure of the Legislative Council of the Hong Kong Special Administrative Region, a copy of which is attached in *Appendix 1* to this Report.

2. **Membership of the Committee** The following Members are appointed by the President under Rule 72(3) of the Rules of Procedure to serve on the Committee:

Chairman	The Hon Eric LI Ka-cheung, JP
Deputy Chairman	The Hon Emily LAU Wai-hing, JP
Members	The Hon David CHU Yu-lin The Hon Fred LI Wah-ming, JP The Hon LAU Kong-wah The Hon Abraham SHEK Lai-him, JP The Hon Tommy CHEUNG Yu-yan, JP
Clerk	Ms Miranda HON Lut-fo
Legal Adviser	Mr Jimmy MA Yiu-tim, JP

II. PROCEDURE

The Committee's Procedure The Committee's practice and procedure, as determined by the Committee in accordance with Rule 72 of the Rules of Procedure, are as follows:

- (a) the public officers called before the Committee in accordance with Rule 72 of the Rules of Procedure, shall normally be the Controlling Officers of the Heads of Revenue or Expenditure to which the Director of Audit has referred in his Report except where the matter under consideration affects more than one such Head or involves a question of policy or of principle in which case the relevant Bureau Secretary of the Government or other appropriate officers shall be called. Appearance before the Committee shall be a personal responsibility of the public officer called and whilst he may be accompanied by members of his staff to assist him with points of detail, the responsibility for the information or the production of records or documents required by the Committee shall rest with him alone;
- (b) where any matter referred to in the Director of Audit's Report on the accounts of the Government relates to the affairs of an organisation subvented by the Government, the person normally required to appear before the Committee shall be the Controlling Officer of the vote from which the relevant subvention has been paid, but the Committee shall not preclude the calling of a representative of the subvented body concerned where it is considered that such a representative can assist the Committee in its deliberations;
- (c) the Director of Audit and the Secretary for the Treasury shall be called upon to assist the Committee when Controlling Officers or other persons are providing information or explanations to the Committee;
- (d) the Committee shall take evidence from any parties outside the civil service and the subvented sector before making reference to them in a report;
- (e) the Committee shall not normally make recommendations on a case on the basis solely of the Director of Audit's presentation;
- (f) the Committee shall not allow written submissions from Controlling Officers other than as an adjunct to their personal appearance before the Committee; and

PROCEDURE

- (g) the Committee shall hold informal consultations with the Director of Audit from time to time, so that the Committee can suggest fruitful areas for value for money study by the Director of Audit.

2. **The Committee's Report** This Report by the Public Accounts Committee corresponds with Report No. 36 of the Director of Audit on the results of value for money audits which was tabled in the Legislative Council on 25 April 2001. Value for money audits are conducted in accordance with the guidelines and procedures set out in the Paper on Scope of Government Audit in the Hong Kong Special Administrative Region - 'Value for Money Audits' which was tabled in the Provisional Legislative Council on 11 February 1998. A copy of the Paper is attached in *Appendix 2*.

3. **The Government's Response** The Government's response to the Committee's Report is contained in the Government Minute, which comments as appropriate on the Committee's conclusions and recommendations, indicates what action the Government proposes to take to rectify any irregularities which have been brought to notice by the Committee or by the Director of Audit and, if necessary, explains why it does not intend to take action. It is the Government's stated intention that the Government Minute should be laid on the table of the Legislative Council within three months of the laying of the Report of the Committee to which it relates.

III. COMMITTEE PROCEEDINGS

Consideration of the Director of Audit's Report No. 36 tabled in the Legislative Council on 25 April 2001 As in previous years, the Committee did not consider it necessary to investigate in detail every observation contained in the Director of Audit's Report. The Committee have therefore only selected those chapters in the Director of Audit's Report No. 36 which, in their view, referred to more serious irregularities or shortcomings. It is the investigation of those chapters which constitutes the bulk of this Report.

2. **Meetings** The Committee held a total 11 meetings and 7 public hearings in respect of the Director of Audit's Report No. 36. During the public hearings, the Committee heard evidence from a total of 39 witnesses, including 7 Bureau Secretaries and 12 Heads of Department. The names of the witnesses are listed in *Appendix 3* to this Report. A copy of the Chairman's introductory remarks at the first public hearing on 7 May 2001 is in *Appendix 4*.

3. **Arrangement of the Report** The evidence of the witnesses who appeared before the Committee, and the Committee's specific conclusions and recommendations based on the evidence and on their deliberations on the relevant chapters of the Director of Audit's Reports, are set out in Chapters 1 to 6 below.

4. A verbatim transcript of the Committee's public proceedings will be available in the Library of the Legislative Council and on the Council's Internet Home Page for inspection by the public.

5. **Acknowledgements** The Committee wish to record their appreciation of the co-operative approach adopted by all the persons who were invited to give evidence. In addition, the Committee are grateful for the assistance and constructive advice given by the Secretary for the Treasury, the Legal Adviser and the Clerk. The Committee also wish to thank the Director of Audit for the objective and professional manner in which he completed his Report, and for the many services which he and his staff have rendered to the Committee throughout their deliberations.

Chapter 1

Follow-up review on control of utility openings

The Committee held public hearings on 14 and 17 May 2001 to receive evidence on this subject from the Secretary for Works, the Secretary for Planning and Lands, and the Director of Highways. The Committee also received additional information from the witnesses after the public hearings.

2. To allow themselves more time to consider the various issues involved and the additional information provided by the witnesses, the Committee have decided to defer a full report on this subject.

Chapter 2

Provision of slaughtering facilities for supplying fresh meat

Audit conducted a review to examine:

- the implementation of the privatisation programme of the then Urban Council's (UC's) public slaughterhouses to see if there were any useful lessons to be learned; and
- the feasibility of centralising the slaughtering operation of livestock at the Sheung Shui Slaughterhouse (SSSH).

Implementation of the privatisation programme of public slaughterhouses

2. At the public hearing, **Mrs Lily YAM KWAN Pui-ying, Secretary for the Environment and Food**, made an opening statement. She said that:

- the Administration agreed with Audit's recommendation on the provision of relevant information to decision-making bodies. However, the Administration's Memorandum submitted in March 1987 to the Executive Council (ExCo) mainly concerned the privatisation of public slaughterhouses and the impact of the privatisation programme on the staff concerned. The development of the SSSH site was only one element of the privatisation programme. The purpose of the Memorandum was to seek the ExCo's approval in principle for the Administration to enter into negotiations with Company A¹ on the privatisation programme and the development of the SSSH site. At that time, Company A had not specified how low the land premium was, i.e. the amount of the land premium. As a matter of fact, in the course of a negotiation, the other party would always request the Government to grant the most favourable terms. Although Company A's request for the Government to grant the SSSH site at a low land premium was not mentioned in the ExCo Memorandum, the importance of this piece of information was subject to interpretation;
- actually, before submitting the Memorandum to the ExCo, the department and the policy branch concerned had mentioned Company A's request in a paper submitted to the Lands, Works, Transport, Housing and Environmental Protection Policy Group of the Chief Secretary's Committee (the Policy Group) in September 1986;

¹ Company A in the Audit Report is Ng Fung Hong Limited.

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- Audit pointed out that the then Urban Services Department (USD) did not seem to have immediately attended to the proposal for the privatisation of the Cheung Sha Wan Abattoir (CSWA), thus causing a delay in its privatisation. The Administration had advised in the Audit Report that the strategy of the USD at that time was to conclude the negotiation on the development of the SSSH site before proceeding with the privatisation of the CSWA. Whether the strategy was considered as right or not subsequently, the USD considered at the time that it should adopt such a strategy;
- she was working in the then Civil Service Branch at that time and was responsible for staff benefits, liaison with staff unions and privatisation. In the late 1980s and the early 1990s, the Government was implementing one or two privatisation and corporatisation schemes, among which the establishment of the Hospital Authority was the major one, causing dissatisfaction among the health care workers. At that time, there was a view in the Government that privatisation and corporatisation should proceed with caution. Slaughtering of livestock was a very specialised job. It would not be easy to make suitable arrangements for the staff affected by the privatisation, such as finding other jobs for them or assisting them in switching to other fields, because most of them had been working in the slaughterhouse for decades. The USD did not wish to make hasty privatisation arrangements. If the morale of the staff was undermined by the privatisation, the operation of the slaughterhouse and the supply of fresh meat would be affected consequently. This could explain why the privatisation of the CSWA was not taken forward expeditiously;
- Audit had also made recommendations on the absorption of the Tsuen Wan Slaughterhouse's (TWSH's) throughput of pigs by the SSSH. Audit had reasonably pointed out that if the daily slaughtering throughput of pigs in the territory did not show an increasing trend and there were indications that the SSSH would be capable of absorbing the additional slaughtering throughput of pigs displaced by the TWSH, the Administration should conduct a cost and benefit analysis on centralising the slaughtering operation of pigs at the SSSH. The Administration had agreed to study the issue at an appropriate time. Nevertheless, current information revealed that the daily market demand for fresh pork was still high, exceeding 6,000 pigs a day. Even with full utilisation of the facilities at the SSSH, the daily slaughtering capacity of the SSSH was only 5,000 pigs. During Chinese festivals, such as the recent Lunar New Year period, the daily slaughtering throughput was more than 10,000 pigs. The Administration had to take this factor into account in ascertaining the feasibility of centralising the slaughtering operation of livestock at the SSSH. Another factor was the changes in demand for fresh

Provision of slaughtering facilities for supplying fresh meat

pork and the eating habits of the population. Before there was a clear trend indicating a substantial decline in the demand for fresh pork, the Administration should not hastily make decision to centralise the slaughtering operation at the SSSH. As the SSSH only started full-scale operation from March 2000, close monitoring of its operation was still required and various improvement measures had to be carried out; and

- there were concerns over the environmental impact of the TWSH on the local residents. If the SSSH was to take over the slaughtering operation of the TWSH and, as a result, resolve the environmental problems caused by the TWSH, the environmental nuisance in Sheung Shui might be aggravated instead. Furthermore, before any major changes to the existing operation were implemented, the Administration had to discuss such impending changes with the meat traders.

3. The Committee noted from the Secretary for the Environment and Food's opening statement that as early as September 1986, the Policy Group, which was chaired by the then Chief Secretary, was aware of Company A's request for the Government to grant the SSSH at a low land premium. The Committee questioned whether:

- there was contradiction between this piece of information and the fact that Company A's request was not mentioned in the Memorandum submitted to the ExCo in March 1987; and
- the ExCo was informed of Company A's request in 1987.

4. The **Secretary for the Environment and Food** replied that the Administration could not trace any record concerning whether the information on Company A's request was deliberately not provided to the ExCo. She trusted that as the Policy Group had been informed of Company A's request, the Administration would not have deliberately withheld the information from the ExCo. She guessed that as the ExCo Memorandum was focused on the privatisation of the two slaughterhouses with the development of the SSSH site as one of the elements of the programme, the Administration might not have considered it necessary to report Company A's request in the ExCo Memorandum. Nevertheless, she agreed that the Administration should pay particular attention to the provision of important information when submitting memoranda to the ExCo in future.

Provision of slaughtering facilities for supplying fresh meat

5. Paragraph 2.33(b) of the Audit Report stated that the Food and Environmental Hygiene Department (FEHD) could not trace any record to explain why no report was made in 1987 by the Administration to the ExCo, or by the USD to the Policy Group, regarding Company A's view that the company's participation in the privatisation programme would hinge on favourable and concessionary terms of the private treaty grant for the SSSH site. The Committee asked:

- whether the Administration considered the incident unusual; and
- whether the incident was caused by the mishandling of government files.

6. **Miss Sarah WU, Acting Director of Food and Environmental Hygiene**, explained that:

- when Audit asked the FEHD why Company's A request had not been mentioned in the Memorandum submitted to the ExCo in March 1987, the FEHD gave a reply based on the information in its files. The FEHD had not concealed any information from Audit. Audit was aware that the letter from Company A about the land premium had been submitted to the Policy Group in 1986; and
- as explained by the Secretary for the Environment and Food, the ExCo Memorandum dealt with the matter as a whole and the request from Company A would be discussed in the course of the negotiation with Company A. As a result, the ExCo Memorandum made no specific reference to the letter from Company A requesting a low land premium.

7. As Company A's request for a low land premium was the crux of the implementation of the privatisation programme as well as the cause for the unduly long time, i.e. five years, taken to negotiate with the company, the Committee asked whether the Secretary for the Environment and Food agreed that Company A's request was an important piece of information in the circumstances.

8. **The Secretary for the Environment and Food** stated that:

- after the passage of so many years, she could only give her personal view on the matter. Based on her experience in handling joint projects between the Government and private companies, the latter always requested the Government to grant the most favourable terms, e.g. granting the SSSH site at a low land premium; and

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- if Company A had specified the amount of the low land premium, this piece of information might have been quite useful. However, as Company A had only stated that it requested favourable terms and the concession of a low land premium, such information might not be useful to the ExCo.

9. According to the Secretary for the Environment and Food's opening statement, the USD's negotiation strategy and the impact of privatisation on staff morale might have been the major considerations in the non-reporting of Company A's view that the company's participation in the privatisation programme would hinge on favourable and concessionary terms of the private treaty grant for the SSSH site. The Committee enquired whether there was indeed no minutes of meeting or record in this regard, and whether the major considerations the Secretary had mentioned were only the Secretary's guesswork.

10. In reply, the **Secretary for the Environment and Food** said that:

- the privatisation of the CSWA would have an impact on staff morale and should proceed with caution. This issue was separate from how important the information on Company A's request for a low land premium was to the ExCo;
- she had made enquiries with her colleagues about the reason for not pointing out, in their comments on the draft of the Audit Report, that Company A's request had been reported in the paper to the Policy Group in September 1986. The staff concerned had explained to her that they only focused on Audit's recommendations at that time. As the draft Audit Report only mentioned the submission of the Memorandum to the ExCo in 1987, the staff only paid attention to the papers submitted to the Policy Group after 1987; and
- after an in-depth study of the circumstances surrounding the submission of information to the Policy Group, it was discovered that Company A's request was first mentioned in the submission of the company's proposal to the Policy Group in September 1986.

11. As it was not mentioned in the Audit Report that the policy branch and the department concerned had reported Company A's request for a low land premium in the paper submitted to the Policy Group in September 1986, the Committee considered it necessary to have sight of the relevant paper of the Policy Group. However, the **Secretary for the Environment and Food** did not accede to the Committee's request. She advised

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that it had been the Administration's long-standing principle to keep discussion papers of all Policy Groups of the Chief Secretary's Committee confidential, to ensure free presentation and exchange of views at Policy Group meetings which were internal government meetings.

12. In response to the Committee's view that the refusal would impede their understanding of the issues examined in the Audit Report, thereby preventing the Committee from fully discharging their duty, the **Secretary** subsequently provided, in *Appendix 5*, a copy of the relevant paragraph of the discussion paper submitted to the Policy Group in September 1986, and of Company A's letter mentioned in that paragraph. The **Secretary** also advised that in making them available to the Committee, she had taken into consideration their contents and the length of time that had now elapsed since the events to which they related.

13. With reference to the relationship between the USD and the UC, the Committee enquired whether the USD had reported to the UC the negotiations with Company A as well as the conditions for the construction of the SSSH.

14. The **Acting Director of Food and Environmental Hygiene** informed the Committee that:

- according to the information in the files, the UC mainly dealt with the privatisation of the two slaughterhouses within its purview. The construction of a new slaughterhouse to replace the CSWA was only part of the privatisation programme, which the USD had reported to the UC. Consequent upon the approval given by the ExCo, the USD did make a verbal report on the issue, as recorded in the minutes of meeting of the UC held in May 1987, and the UC had also followed up the progress of the closure of the CSWA and the Kennedy Town Abattoir (KTA); and
- regarding the conditions for the construction of the SSSH, this was a matter for the Government and the operator concerned. She believed that the USD was not accountable to the UC in this regard.

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15. The Committee considered that when Company A made a request for a low land premium, it meant that the company would not build the SSSH unless it was exempted from paying the full land premium for the site. As the Land Commission was in existence at that time, the Administration should inform the ExCo of such terms of the land grant, so that the ExCo would submit an application to the Land Commission for approval of the terms proposed by the company. For instance, both the Hong Kong Housing Society and the Hong Kong Housing Authority were required to submit an application to the Land Commission where a request for a low land premium was made.

16. **The Secretary for the Environment and Food** responded that:

- in March 1987, apart from consulting the ExCo on the privatisation programme of the KTA and the CSWA, the Administration only sought the ExCo's approval in principle for conducting discussions with Company A. Upon the conclusion of the negotiation and prior to the finalisation of the programme, the Administration would report to the ExCo again. As a matter of fact, the USD and Company A were engaged in the negotiation over the low land premium and favourable terms in the two years following the ExCo's approval; and
- she was not familiar with the operation of the Land Commission. Without the relevant information, she was unable to ascertain whether the Administration had to submit to the Land Commission for approval Company A's proposal for a low land premium immediately upon receipt of the proposal or should wait until the company had submitted specific terms of the land grant.

17. According to paragraph 2.12 of the Audit Report, the USD informed Company A in September 1989 of the basic terms of the private treaty grant, which included a land premium of \$34 million, assessed by the then Buildings and Lands Department (BLD) on the basis of the USD's projected profitability of the slaughtering business. In December 1989, Company A expressed serious reservations about the high land premium and counter-proposed, as one of the conditions for building the SSSH, only a nominal land premium for the SSSH site. Paragraph 2.13 further revealed that the then Planning, Environment and Lands Branch (PELB) had commented on Company A's counter-proposal for a nominal land premium. Having regard to several factors, the PELB was not in favour of granting the land to Company A at a concessionary premium. In February 1990, the Policy Group was informed of Company A's counter-proposal and of the PELB's view on the concessionary premium.

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18. Against the above background, the Committee considered that it appeared that members of the Policy Group, who were senior government officials, had made a decision on the land premium on their own without reporting the updated developments back to the ExCo. The Committee asked whether it was the case at that time.

19. The **Secretary for the Environment and Food** responded that according to the ExCo Memorandum of March 1987, the USD would report to the ExCo again subsequent to the conclusion of an agreement on the land premium and prior to the finalisation of the construction programme of the SSSH. On the other hand, the Policy Group considered in 1990 that the original approach, i.e. granting land to Company A for building the SSSH, was not feasible and therefore a new approach had to be adopted. It could be the case that as the Administration was not required to submit the terms of the land grant to the ExCo for approval, it did not consider it necessary to report the change of approach to the ExCo. She drew the above conclusion on the basis of her analysis of the information.

20. In response to the Committee's enquiry about the need to seek the ExCo's approval of the land grant conditions for the SSSH site, the Director of Audit advised, in his letter of 17 May 2001, in *Appendix 6*, that in this particular case, which involved a private treaty grant, land grant conditions had to be approved by the ExCo. Actually, the ExCo had advised in March 1987 that the private treaty grant for the land in Sheung Shui was approved in principle, subject to the provision that full details of the grant would be submitted for the ExCo's consideration and formal approval in due course.

21. On the submission of papers to the Policy Group and the ExCo, the Committee enquired whether the papers were submitted by the USD. The **Secretary for the Environment and Food** informed the Committee that it was the then Municipal Services Branch which was responsible for the co-ordination and submission of papers to the Policy Group and the ExCo.

22. The Committee considered that the Policy Group and the Administration should be fully aware that whether the Administration and Company A could reach a consensus in the negotiation hinged on the land premium. The Committee queried why the Administration had not reported again or submitted progress reports to the ExCo regarding the crucial issue of the land premium during the five years of negotiation.

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23. The **Secretary for the Environment and Food** explained that:

- between 1987 and 1989, the Administration and Company A had been discussing the company's request for a low land premium. When the BLD assessed the land premium for the SSSH site in 1989, the company indicated that it could not accept the terms offered by the Government. In 1990, the Policy Group decided to depart from the original approach; and
- the Administration was not required to report to the ExCo on all matters. The then ExCo or the current ExCo might request government departments to submit information papers to it at regular intervals. According to her understanding, the ExCo had not made such a request at that time. She trusted that the department and the policy branch concerned had submitted reports to the Policy Group in the course of the negotiation but did not report to the ExCo regularly.

24. In response to the Committee's enquiry about the non-reporting of Company A's counter-proposal for a nominal land premium to the Policy Group until 1990, the **Secretary for the Environment and Food** said that the reports to the Policy Group were about the progress of the privatisation programme, not the negotiations with Company A on low land premium.

25. In order to enhance their understanding of the developments relating to the UC's approval of the privatisation of the KTA and the CSWA and Company A's stance regarding the concessionary land premium, the Committee requested the Director of Food and Environmental Hygiene to provide them with copies of the following documents:

- minutes of the UC Food Hygiene Select Committee meeting held on 5 June 1986;
- minutes of meeting held on 23 September 1987 which representatives from Company A attended; and
- Company A's letter dated 7 December 1989 stating the company's counter-proposal for a nominal land premium.

26. In response, the **Director of Food and Environmental Hygiene** provided the Committee with the minutes of the Select Committee, in *Appendix 7*, and relevant extracts from the minutes of meeting held on 23 September 1987 and Company A's letter in *Appendices 8 and 9* respectively.

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27. According to paragraph 2.37 of the Audit Report, the ExCo had advised in March 1987 that the privatisation programme should be taken forward expeditiously. Audit pointed out that the USD had missed five opportunities to privatise or close down the CSWA during the period January 1991 to February 1994. For instance, in January 1991, Company A had indicated its interest in taking over the CSWA, and in February 1994, Company A suggested that the USD should consider closing down the CSWA. The Committee considered that if the USD had accepted Company A's suggestion, the loss incurred in operating the CSWA could have been reduced. According to the opening statement of the Secretary for the Environment and Food, staff morale and other factors had to be taken into account in the privatisation of the CSWA. The Committee questioned why the Director of Food and Environmental Hygiene had not explained these issues in her response to Audit.

28. The **Acting Director of Food and Environmental Hygiene** said that during the period 1987 to 1992 or later, the main concern was the privatisation of the KTA, which was completed in 1990. Then, both the Government and Company A turned their attention to the follow-up work. Hence, the FEHD had explained to Audit how the Government had decided to fund the SSSH project. As stated by the Secretary for the Environment and Food, the Government was carrying out some privatisation and corporatisation schemes in the 1990s, which had a substantial impact on the implementation of the privatisation of the CSWA. In view of the complicated process, the FEHD had given an explanation to Audit from a macro point of view.

29. The Committee understood from paragraph 2.37(c) of the Audit Report that the Government's priority was to resolve the development of the SSSH site first. However, in view of the continual heavy operating loss of the CSWA, the Committee queried whether the Administration should have addressed the problem while negotiating with Company A over the construction of the SSSH.

30. The **Acting Director of Food and Environmental Hygiene** responded that back in the 1990s, the construction of the SSSH was accorded top priority in the privatisation programme by the branch and the department concerned. At the same time, due regard had to be given to the arrangements for the affected staff and the supply of fresh meat.

31. The Committee were very concerned about the cumulative operating loss of \$591 million incurred by the CSWA during the period from 1995-96 to 1999-2000 and that of \$883 million during the period from 1992-93 to 1999-2000. They considered that if the CSWA had been closed down or privatised at an earlier stage, the UC would have avoided an average annual operating loss of about \$100 million.

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32. Paragraph 2.24 of the Audit Report revealed that as a result of Company A's centralising the slaughtering of roaster pigs at the TWSH, the CSWA's average daily slaughtering throughput of pigs was drastically reduced by 35%. The USD's concern was to reduce the immediate impact of the decrease in the CSWA's slaughtering throughput. The Committee enquired what measures the USD had taken in this regard.

33. The **Acting Director of Food and Environmental Hygiene** informed the Committee that the USD had requested the operator of the TWSH to maintain the slaughtering of pigs at the CSWA. The USD had also adjusted the slaughtering operating hours of the CSWA to meet market demand, with a view to improving the service and keeping the meat traders in business.

34. The Committee noted from paragraph 2.9 of the Audit Report that the Finance Committee of the Legislative Council had approved the staff redundancy package for the privatisation of the KTA in 1990. Hence, the Committee queried whether the problem of staff redundancy had indeed caused a delay in the privatisation or closure of the CSWA.

35. The **Acting Director of Food and Environmental Hygiene** stated that:

- when the Policy Group finally decided in 1992 that the SSSH would be built by the Government, the USD immediately discussed with the policy branch concerned how to inform the affected staff of the programme. The negotiation and consultation with the staff had lasted for a long time. Although the general direction had been set in the funding application to the Finance Committee, the USD had to work out a timetable before negotiating with the staff. The USD had to notify the affected staff of the arrangements 12 months in advance. Several years had lapsed between the decision to fund the SSSH project and the commencement of the negotiation with the affected staff. The USD did not know the target completion date of the SSSH until the Finance Committee approved the funding for the construction of the SSSH in mid-1996; and
- the table in Appendix E to the Audit Report illustrated when the average daily slaughtering throughput of the CSWA could be absorbed by the KTA and the Yuen Long Slaughterhouse. In fact, the USD had formulated a specific policy and prepared a clear timetable in 1995. However, the USD had to address many issues at that time, such as the timetable, the staff redeployment and the notice to the affected staff. The USD did not close the CSWA in 1995 or 1996 in order to avoid introducing too many changes in the mode of slaughtering operation and in the arrangements concerned.

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36. According to paragraph 2.38 of the Audit Report, the USD had failed to assess critically the consequences of the continued operation of the CSWA. As the ExCo had advised in 1987 that the privatisation programme should be taken forward expeditiously, the Committee queried whether the continued operation of the CSWA was cost-effective and in compliance with the ExCo's decision. Furthermore, the Committee considered that if the operating loss of more than \$800 million were to be given as severance payments to the more than 600 staff affected by the privatisation, every member of the staff would receive about \$1.3 million. The Committee wondered whether the Administration agreed that its approach in dealing with the privatisation programme was not sensible.

37. The **Secretary for the Environment and Food** responded that:

- although the ExCo had directed the Administration to take forward the privatisation programme expeditiously, the conditions had to be acceptable to both sides before an agreement could be reached. If problems arose in the course of the negotiation, it would be difficult to complete the privatisation in a short time; and
- the Administration had to implement every corporatisation or privatisation scheme with caution. In the early years, favourable conditions had been offered to the staff affected by the corporatisation of the Kowloon-Canton Railway (KCR). As a result, in the following 10 years or so, whenever the Government negotiated with staff on corporatisation, the staff would make reference to the conditions offered in the KCR case. Hence, when consulting staff on a redundancy package, the Administration always bore in mind that the conditions to be offered would have implications for future corporatisation and privatisation programmes.

38. In the light of the Secretary for the Environment and Food's remarks, the Committee considered that being mean to the staff had resulted in a heavy price for the Government. In the course of the negotiation with the staff of the CSWA, the Administration could have redeployed the staff to other slaughterhouses instead of immediately making them redundant. The Committee further asked whether the Administration admitted that its strategy had been poor.

Provision of slaughtering facilities for supplying fresh meat

39. The **Secretary for the Environment and Food** said that:

- she did not agree that the Administration had been mean to the affected staff. She considered that the Administration had acted responsibly. If the Administration solved a problem hastily so that the consequences had to be borne by the departments which later took over the corporatisation or privatisation programme, this would be a short-sighted approach; and
- there were only a limited number of slaughterhouses in the territory now and then. When the SSSH started operation in 1999, the Administration still needed to find jobs for some staff members of the CSWA. Company A was then requested to absorb some of them. The staff members concerned had been in slaughtering work for decades. Even after attending retraining courses, they would not be able to adapt themselves to other types of work.

40. The Committee understood that the Government was operating the KTA at continual losses, but with the privatisation of the KTA, Company A which took over its operation was able to make a profit. The Committee asked why, under the circumstances, the Administration continued to operate the CSWA rather than simultaneously implementing the privatisation of the KTA and the CSWA.

41. The **Acting Director of the Food and Environmental Hygiene** responded that according to the strategy approved by the ExCo in 1987, the privatisation programme would be completed in two phases. Phase one concerned the privatisation of the KTA. Therefore, during those few years, the Administration had concentrated on the KTA. Following the KTA's privatisation, the Government and Company A turned their attention to the construction of the SSSH. Although it was now difficult to assess the situation at that time, it was understood that while the Government was negotiating with Company A on the construction of the SSSH, the company had its own thinking. During the negotiation, Company A put forward other proposals. As the USD was very concerned about the SSSH project, it did not wish to have the long-term development affected by another item of work.

42. The Committee understood that although the ExCo had directed the Administration to take forward the privatisation programme expeditiously, the USD's policy was to expeditiously deal with the construction of the SSSH before proceeding with the privatisation of other slaughterhouses. The Committee asked why the USD's policy should prevail over the direction set by the ExCo and why the USD had not reported to the ExCo about the change in the policy.

Provision of slaughtering facilities for supplying fresh meat

43. The **Acting Director of Food and Environmental Hygiene** informed the Committee that the ExCo clearly stated that the objective of phase one of the privatisation programme was to privatise the KTA. The Administration took note of the general direction of the policy. However, in the course of the negotiation in the 1990s, the Administration had to implement the policy with due regard to the circumstances at that time.

44. The **Secretary for the Environment and Food** added that according to the ExCo, there were three elements in the expeditious implementation of the privatisation programme. The first element was to privatise the KTA. The second element was to privatise the CSWA. The third element was to build the SSSH in order to replace the CSWA. If the original plan could proceed smoothly, the SSSH would be operated by a private company. That explained why the USD was so concerned about the negotiation on the construction of the SSSH.

45. The Committee noted that the Administration put forward the construction of the SSSH and the staff redundancy arrangements as the reasons for the delay in the closure of the CSWA. However, as early as 1992, the Policy Group had decided that the Government should fund the SSSH project. Moreover, the redundancy terms had been agreed by all slaughterhouse staff in 1991. Against this background, the Committee asked why during the period 1992 to 1994, the USD did not accept Company A's proposals to privatise or close down the CSWA.

46. In response, the **Acting Director of Food and Environmental Hygiene** said that:

- cattle were also slaughtered in the CSWA. Even if the USD had accepted Company A's proposal for transferring the slaughtering throughput of pigs to other slaughterhouses, the CSWA could not have been closed earlier; and
- the USD still had to address operational issues, including the future mode of operation. Therefore, when Company A put forward its suggestion again, the USD had already paid due regard to a number of factors, such as staff redundancy, the supply of fresh meat and the arrangements in preparation for the completion of the construction of the SSSH. Although the affected staff had agreed to the redundancy terms in principle, the USD still had to work out the details of the arrangements with them in 1993 and 1994. Even in 1996 and 1997, when the decision on the SSSH was final and staff redundancy and the overall arrangements were under discussion, the implementation of the programme were not completely free from problems. Hence, the negotiation, Company A's stance, the staff affected and the supply of fresh meat were a series of issues in the matter.

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47. In the light of the Acting Director of Food and Environmental Hygiene's remarks, the Committee enquired whether the continual operating loss incurred in the operation of the CSWA had been taken into account in the overall consideration of the matter.

48. The **Acting Director of Food and Environmental Hygiene** replied that the USD had reported the matter to the UC at that time. In order to reduce the operating loss, the USD had put in place various measures and had all along been reducing the manpower. A plan had been formulated in 1995 and 1996 to implement the measures. The USD considered the arrangement appropriate for the staff and the meat trade.

Feasibility of centralising the slaughtering operation of livestock at the SSSH

49. With regard to the feasibility of centralising the slaughtering operation of livestock at the SSSH, the Committee noted from paragraph 3.20 of the Audit Report that according to the Architectural Services Department (ASD), there might be physical and technical constraints in the SSSH's existing slaughtering and supporting facilities. Paragraph 3.22 of the Audit Report revealed that some modification works to the SSSH would be required for the SSSH to increase the slaughtering throughput of pigs. The Committee asked whether it was feasible to centralise the slaughtering operation at the SSSH and whether it would take some time before centralisation could be implemented.

50. **Mr KWAN Pak-lam, Acting Director of Architectural Services**, advised the Committee that:

- the operation of a slaughterhouse was very complicated. The most complicated issue was the treatment of waste water, which was related to the slaughtering throughput and the water requirement. The additional hot water required would increase the temperature of the bioreactor, which might bring the operation of the waste water treatment plant to a standstill;
- if the daily slaughtering throughput was 5,000 pigs, the waiting lairage was required to have a holding capacity for 12,000 pigs. The increase in the holding capacity of the waiting lairage would cause noise, odour and ventilation problems. The situation would be worst in summer. Pigs generated more odour at high temperatures. Studies were also required for wind speeds in different seasons. The ASD had conducted a number of studies over many years before the construction of the SSSH. Fortunately, no complaints had been received since the commissioning of the SSSH;

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- another problem concerned meat despatch. The existing meat despatch bank was already very crowded. There would be difficulties in handling more carcasses;
- increasing the daily slaughtering throughput would require an increase in the number of parking spaces. It would be very complicated to carry out modification works while the SSSH was in operation. Moreover, although there was a fallback boiler, it was not designed to cope with an increase in the daily slaughtering throughput. There was also the problem of the emergency power supply;
- with the centralisation of the slaughtering throughput at the SSSH, a standstill in its operation would disrupt the overall supply of fresh meat. When the ASD completed a study on the impacts of the constraints, it had to address the technical issue of how to carry out modification works without affecting the normal operation of the SSSH; and
- before undertaking any study, the ASD had to be advised of the proposed slaughtering throughput. Studies were time-consuming and costly exercises. Professionals would have to be hired from outside Hong Kong. According to a preliminary assessment, it would cost \$6 million to conduct a study on the slaughtering throughput of 6,000 pigs.

51. On the question of the slaughtering capacity of the SSSH, the Committee noted from paragraph 3.16(a) of the Audit Report that there were four slaughter lines for pigs at the SSSH. If the number of slaughter lines operated at night was increased from two to three, it would be feasible to increase the SSSH's slaughtering throughput of pigs to more than 6,000. The Committee enquired whether the current daily slaughtering capacity of 5,000 pigs was the maximum if the normal slaughtering operating hours were not adjusted.

52. The **Acting Director of Architectural Services** informed the Committee that:

- the SSSH's design slaughtering throughput was 5,000 pigs per day. It might be possible to increase the slaughtering throughput. However, after the increase, the critical path would rest with an extension to the SSSH rather than the slaughtering hall in the SSSH. The extension might generate problems associated with the holding capacity of the waiting lairage, ventilation, noise and waste water treatment. Therefore, a detailed study must be conducted; and

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- as regards the slaughtering throughput during festive periods, the increase only lasted for a few days. For example, during the Lunar New Year, 10,000 pigs were slaughtered the first day. The SSSH could cope with the surge because the number of pigs slaughtered would drop the next day. There was a balancing tank in the waste water treatment plant, which could relieve the pressure on the operation. However, it would not be feasible to accommodate the surge every day. The crux of the matter was other aspects of the operation rather than the slaughtering hall.

53. Regarding the existing design of the SSSH, the Committee further enquired whether the existing supporting facilities would be able to cater for an increase in the daily slaughtering throughput of pigs.

54. The **Acting Director of Architectural Services** said that the SSSH was designed for handling a daily slaughtering throughput of 5,000 pigs. This meant that in the hot weather in summer, when waste water treatment became more complicated, the SSSH was still able to cope with the slaughtering throughput of 5,000 pigs. As a matter of fact, the slaughtering throughput could be increased in winter. In other words, the slaughtering throughput varied with the season and the wind speed.

55. Paragraph 3.1 of the Audit Report revealed that according to the Metroplan Selected Strategy endorsed by the ExCo in 1991, the TWSH had been classified as a “badly located Government, Institution or Community facility and utility”. As the operation of the TWSH caused nuisance to the local residents, it should be relocated in the long term. However, the Secretary for the Environment and Food commented in paragraph 3.25 of the Audit Report that it was necessary to maintain the TWSH as an indispensable fallback facility to ensure an uninterrupted supply of fresh meat to the community in case of breakdown of the SSSH. Against this background, the Committee asked how the Administration had addressed the issue of maintaining the TWSH, while at the same time the public continued to complain about the environmental problems caused by it.

56. **Mr Robert Law, Director of Environmental Protection**, replied that:

- in the first nine years or so, the Environmental Protection Department (EPD) received hardly any complaints about the environment nuisance caused by the TWSH. Then in 1997, the EPD suddenly received a few hundred complaints against the TWSH as a result of local interest in the issue;

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- the EPD had been working closely with the operator of the TWSH over the years to alleviate the problems. A number of measures had been adopted to minimise the impact of the odour emissions from the TWSH;
- the EPD had been stepping up enforcement against the TWSH for several years. It conducted inspections there at least six times every month on random occasions, such as night-time, weekends and public holidays. However, there was no evidence until now of any actionable offences under either the Noise Control Ordinance (Cap. 400) or the Air Pollution Control Ordinance (Cap. 311); and
- ideally, a slaughterhouse should not be situated within 150 metres of a residential development. However, the TWSH started operation before the occupation of the residential blocks concerned.

57. The **Secretary for the Environment and Food** added that the current distribution of the slaughtering facilities was appropriate. The Administration had taken into account the environmental impact in deciding on the location of the TWSH. Although there were occasionally complaints about the environmental nuisance caused by the TWSH, no incidents of the nuisance in breach of the existing legislation on environmental protection had been detected. In considering whether to centralise the slaughtering operation at the SSSH, the environmental impact on Sheung Shui was also a crucial factor.

58. The Committee noted from paragraph 3.24(d)(i) of the Audit Report that the Director of Food and Environmental Hygiene had said that in view of the less than one year's actual operational experience of the SSSH, it was not an opportune time now to carry out a detailed study to ascertain the feasibility of centralising the slaughtering operation at the SSSH. The Committee asked when it would be the appropriate time to carry out the study.

59. The **Acting Director of Food and Environmental Hygiene** informed the Committee that there was an increase in the total slaughtering throughput of pigs in the year 2000. It was necessary to carry out a forecasting exercise on the slaughtering throughput with due consideration of the total demand for fresh meat for 2001. As the SSSH had been in operation only for the first year, the FEHD hoped to carry out the forecasting exercise a year later, i.e. in early 2002.

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60. In the light of the Acting Director of Food and Environmental Hygiene's remarks, the Committee asked whether there had been any analysis of the reasons for the reversal of the declining trend in the actual daily slaughtering throughput of pigs in 2000 and whether such a sudden increase in the slaughtering throughput was expected to be a recurrent trend.

61. The **Director of Food and Environmental Hygiene**, in her letter of 29 May 2001, in *Appendix 10*, stated that:

- the FEHD had not specifically analysed the cause of the reversal of the declining trend in the actual daily slaughtering throughput of pigs in 2000. However, it had made reference to the USD's study on meat consumption in Hong Kong in 1997, which pointed to the following factors that could affect the demand for slaughtering services of food animals:
 - (a) the breeding method;
 - (b) the growth in population;
 - (c) the substitution effect between fresh pork/beef and other related food products;
 - (d) the price level of fresh pork/beef;
 - (e) the illegal slaughtering and meat smuggling activities; and
 - (f) the disease/contamination among food animals.

The FEHD believed that the above factors were also relevant and that a reversal of the declining trend in 2000 could be attributed to one or a combination of these factors; and

- apart from the increase in slaughtering throughput of pigs in 2000, the FEHD noted that the average daily slaughtering throughput for the past four months since January 2001 had shown a slight increase of 30 pigs, i.e. 0.47%, over the average throughput of 6,323 pigs for 2000. The FEHD considered it necessary to look at the full-year figures for 2001 in order to assess whether the increase in slaughtering throughput was a recurrent trend.

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62. As revealed in paragraph 3.28 of the Audit Report, to allow for the future provision of chilling facilities at the SSSH, additional piling works had been carried out at a cost of about \$30 million to cater for the future extension of the SSSH. The Committee asked whether the chilling facilities could increase the SSSH's practical slaughtering capability due to the enhanced storage capacity.

63. In her letter of 14 June 2001, in *Appendix 11*, the **Director of Food and Environmental Hygiene** informed the Committee that:

- the piling works were designed to support chilling facilities with a maximum storage capacity of 6,000 pigs, 400 cattle and 300 goat carcasses (offals not included) which coincided with the maximum slaughtering capacity of the SSSH. The chilling facilities could not increase the slaughtering capability of the SSSH nor were they planned with such purposes in mind;
- the decision taken at the time to proceed with the incorporation of the additional piling works was made after very thorough and careful deliberations among the bureau and the departments concerned. In brief, it could be regarded as an example of forward planning as:
 - (a) the additional piling works would afford the Government the capability to build the necessary chilling facilities if it decided to do so to upgrade the standard of food hygiene;
 - (b) the incorporation of the additional piling works could be carried out as part of the project with the cost involved being able to be absorbed by the project vote;
 - (c) it would help to optimise the use of the site without affecting the layout and designed operations of meat despatch; and
 - (d) a timely decision to proceed was critical when the opportunity was still available for the piling works to be carried out; and
- at present, the FEHD did not have any immediate plan to build the chilling facilities. It would keep in view changes in the eating habits of the population.

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64. The Committee understood that if the Administration eventually decided to centralise the slaughtering operation of livestock at the SSSH, the TWSH would cease operation. The Committee enquired how the TWSH, which was a licensed private slaughterhouse, could be requested to cease operation in the scenario.

65. The **Director of Audit**, in his letter of 24 May 2001, in *Appendix 12*, advised the Committee that:

- the Government granted the TWSH site to a private company in 1979 only for slaughtering operation under a special-purpose lease which expired in June 1997. In June 1997, the Government extended the lease term of the TWSH site to 30 June 2047; and
- if the Administration considered it feasible to centralise the slaughtering operation of livestock at the SSSH, the Government could cease the TWSH's operation by invoking section 3 of the Lands Resumption Ordinance (Cap. 124) to resume the TWSH site. The Ordinance provided statutory power for the Government to acquire any land required for a public purpose as defined in section 2 of the Ordinance. The Ordinance also provided for the payment of compensation, based on the value of the property, and for business loss, where appropriate, at the date of acquisition.

66. **Conclusions and Recommendations** The Committee:

Implementation of the privatisation programme of public slaughterhouses

- express grave dismay and find it inexcusable that:
 - (a) there was a significant delay in implementing the privatisation programme of the Cheung Sha Wan Abattoir (CSWA), one of the main causes being the unduly long time taken to negotiate with Company A on the land premium of the Sheung Shui Slaughterhouse (SSSH) site;
 - (b) the then Urban Services Department (USD) had failed to fully recognise the heavy costs to the taxpayers in continuing to operate the CSWA and had missed a number of opportunities to privatise or close down the CSWA during the period January 1991 to February 1994; and
 - (c) by allowing the continued operation of the CSWA, the then Urban Council failed to avoid a cumulative operating loss of \$883 million incurred during the eight-year period from 1992-1993 to 1999-2000;

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- express serious concern that important information on the land premium of the SSSH site was not provided to the Executive Council (ExCo) for its meeting held in March 1987 in which the matter was considered;
- express serious concern that while an important strategy was being formulated for its negotiations with Company A, the USD never took the opportunity to report to the ExCo:
 - (a) the average annual operating loss of about \$100 million incurred by the continued operation of the CWSA; and
 - (b) the stance of Company A and that of the then Planning, Environment and Lands Branch regarding the concessionary land premium, which would have required the ExCo's approval,so that further guidance for negotiating the most optimal outcome could be sought and the Government's strategy could be made more flexible;
- recommend that, in order to improve the planning and implementation of future similar programmes, the Administration should provide the ExCo and the other decision-making bodies with all the important information during the critical stages of the negotiation, so as to enable them to fully assess the implications of the programmes (including the continual heavy losses of the existing operation), make informed decisions and approve practicable implementation plans;

Feasibility of centralising the slaughtering operation of livestock at the SSSH

- note that, over the years, the continuing decline in demand for fresh meat in the territory has resulted directly in the declining slaughtering throughput of livestock in the territory;
- acknowledge the undertaking given by the Acting Director of Food and Environmental Hygiene that a new forecasting exercise on the slaughtering throughput of livestock in the territory for the coming years would be carried out early next year, having regard to the demand for fresh meat and the eating habits of the population;
- recommend that the Director of Food and Environmental Hygiene should, based on the results of the forecasting exercise, carry out a detailed study to ascertain the feasibility of centralising the slaughtering operation of livestock at the SSSH;

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- recommend that the Director of Food and Environmental Hygiene should take into account the following factors in the study, before a policy decision is made:
 - (a) the economic costs of the two pieces of land currently occupied by the SSSH and the Tsuen Wan Slaughterhouse (TWSH) respectively and the continuing operation of the TWSH, as well as the potential compensation payable upon the closure of the privately-owned TWSH and the problems involved, such as the elaborate procedures and the justifications for the resumption of the TWSH site, given that the lease of the site has been extended to 2047;
 - (b) the cost of about \$30 million already spent on the piling works dedicated to the construction of chilling facilities at the SSSH, which would allow for more optimal utilisation of the existing slaughtering facilities with the provision of additional chilling facilities and enhanced storage capacity;
 - (c) the full potential capacity of the SSSH site in meeting the need for extension to increase the slaughtering throughput, taking into account the limitations identified, e.g. the capability of the waste water treatment plant and the holding capacity of the waiting lairage for pigs;
 - (d) the changes in demand for fresh and chilled meat and the eating habits of the population;
 - (e) alternative and economical sources of supply of fresh, chilled and frozen meat from outside Hong Kong;
 - (f) the risk of disruption in the supply of fresh meat; and
 - (g) hygiene standards and the environmental impact; and
- wish to be kept informed of the outcome of:
 - (a) the forecasting exercise on the slaughtering throughput of livestock in the territory; and
 - (b) the feasibility study on the centralisation of the slaughtering operation of livestock at the SSSH.

Chapter 3

Provision of staff for Departmental Accounting Units

Departmental accounting units (DAUs) deal with the accounting and financial management matters of government bureaux and departments, and help Controlling Officers discharge their responsibilities under the Public Finance Ordinance (Cap. 2). Audit conducted a review of the provision of staff for DAUs, with particular reference to the provision of staff for the DAUs of the Civil Aviation Department (CAD), the Food and Environmental Hygiene Department (FEHD) and the Leisure and Cultural Services Department (LCSD).

Need for reviews of staff establishment of DAUs based on objective criteria and productivity standards

2. The Committee observed that the Administration provided many justifications for the creation of posts in the civil service in seeking the Legislative Council's (LegCo's) approval of its funding requests. However, there was a lack of yardsticks for determining the subsequent deletion of posts and the restructuring of the staff establishment of the government departments concerned. According to paragraph 2.28 of the Audit Report, Audit considered that there was a need to establish objective criteria and productivity standards to assist Controlling Officers in determining the number and ranking of posts required for their DAUs. The Committee enquired whether the Finance Bureau (FB) would do so in respect of the establishment of DAUs and the overall establishment of government departments.

3. **Miss Denise YUE Chung-ye, Secretary for the Treasury**, replied that:

- regarding the overall establishment of government departments, the FB regularly issued Financial Circulars to remind Controlling Officers of the need to constantly review the establishment. For example, according to Financial Circular No. 4/94 of February 1994, Controlling Officers were required to constantly review the establishment to ascertain whether any posts could be deleted and to ensure that the resources under their control were fully utilised. In this regard, the legal basis was provided in the Public Finance Ordinance. Under section 12 of the Ordinance, a Controlling Officer should be responsible and accountable for all expenditure from any head or subhead for which he was the Controlling Officer; and
- the mechanism also applied to the establishment of DAUs. Controlling Officers were also required to review the establishment of their DAUs to ascertain whether it could meet the accounting needs of the bureaux or departments.

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4. According to paragraph 2.10 of the Audit Report, 20 of the 72 bureaux and departments covered in the audit survey indicated that they had not conducted any establishment reviews. The Committee considered that there was a waste of resources as some bureaux and departments did not conduct such reviews, notwithstanding that they had the responsibility to do so. The Committee also noted from paragraph 2.19 of the Audit Report that the Treasury had established the Financial Management Services Division in its Accounting Services Branch to offer assistance to bureaux and departments. However, paragraph 2.24 stated that, of the bureaux and departments in the above survey, only one department indicated that it had taken into account the accounting and financial support services of the Treasury in reviewing the establishment of its accounting staff. The Committee therefore considered that it was also a waste of resources. Against this background, they asked whether the FB or the Treasury regarded this as double wastage.

5. **Mr SHUM Man-to, Director of Accounting Services**, stated that:

- the Treasury provided support services to bureaux and departments but did not monitor them. When they encountered problems relating to accounting or financial management, they could seek support or advice from the Treasury. They could also consult the Treasury on cost accounting matters or the development of new accounting systems. However, they would not discuss their day-to-day operations with the Treasury unless they were unable to solve particular problems or wished to seek additional advice on them; and
- if there was spare capacity in the Treasury, they would conduct surveys of bureaux and departments to ensure that adequate internal control and accounting procedures existed.

6. In response to the Committee's further enquiry about the lack of objective criteria for establishment reviews of DAUs, the **Director of Accounting Services** advised that:

- he could not comment on whether there had been a waste of resources as the Treasury only offered assistance to bureaux and departments when they encountered problems;
- although Audit considered that there was a need to establish objective productivity standards, it would be difficult for small DAUs to do so. As revealed in the Audit Report, of the 72 bureaux and departments covered in the audit survey, there were not more than 10 staff members in each of the DAUs of 30 bureaux and departments;

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- as accounting work involved many trivial tasks, such as the preparation of estimates, the maintenance of accounts, the processing of payment vouchers and the collection of revenue, the smaller DAUs might have practical difficulties in putting all tasks on record every month. Owing to the small establishment of their DAUs, bureaux and departments might not conduct formal reviews. However, this did not mean that bureaux and departments had not conducted any reviews. For instance, the Treasury conducted a review every year as staffing arrangements would be reviewed when annual estimates were prepared with a view to providing new services through redeployment of manpower. Since the DAU of the Treasury was staffed by a Clerical Officer and an Assistant Clerical Officer, it would not be cost-effective to conduct an establishment review, or establish objective productivity standards and file monthly records; and
- bureaux and departments varied in size and work nature. Depending on the requirements of policy secretaries and heads of department, the functions of one DAU might be different from those of another. It would be difficult to apply one set of criteria to the DAUs of different bureaux and departments.

7. In the light of the Director of Accounting Services' remarks, the Committee were concerned that if there was one redundant staff member in a bureau or department, there would be 30 redundant staff members in 30 bureaux and departments. The Committee also noted from paragraph 2.9 of the Audit Report that in 1985, the FB had already proposed to carry out an enhanced programme of value for money studies in lieu of establishment reviews. Nevertheless, it appeared that the Audit recommendation for the establishment of productivity standards had not been accepted. The Committee queried again why there was a lack of objective criteria for determining the deletion of posts when a bureau or department reached a particular staffing level.

8. The **Director of Accounting Services** explained that:

- it would be easier to establish productivity standards for staff who were involved in a large number of repetitive tasks, such as factory workers in the production lines, tellers in banks and staff at receiving counters in the Treasury. However, individual staff members of small DAUs were assigned different tasks every day. It would not be possible to put all the trivial tasks on record; and

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- as regards whether objective productivity standards should be established for staff of DAUs of bureaux and departments, it depended on the nature, the mode of operation and the size of individual bureaux or departments. Among the 72 bureaux and departments in the audit survey, four departments had DAUs each of over 100 staff members. It would be easier for them to establish productivity standards.

9. The Committee further enquired whether the Treasury had put in place any other alternative measures for supporting small DAUs.

10. In his letter of 4 June 2001, in *Appendix 13*, the **Director of Accounting Services** informed the Committee that:

- as a small DAU would probably consist of less than 10 staff members, it was inevitable that each member of staff would be expected to participate in a number of different activities ranging from preparing estimates, making payments, and presenting reports to defining or designing systems and procedures. It was therefore impossible to set standards or targets that would represent the ideal composition of the DAU or the ideal output from that group of staff;
- what was pertinent, regardless of the size of the DAU, was the evaluation of the qualities expected of the individual staff members of a DAU. The Treasury had always assisted in this regard and made recommendations on the level of staff appropriate to the needs of Controlling Officers by referring to the published core competencies agreed for Treasury Accountant and Accounting Officer grade staff. The Civil Service Bureau would provide similar assistance for General Grade positions;
- a small DAU could not easily cope with sudden or ad hoc demands, because it did not have sufficient manpower or the quality of staff required for the tasks. The Treasury was available to assist bureaux and departments in coping with such demands. In this regard, it was currently involved in two staffing reviews which aimed at reflecting the changing circumstances in the departments concerned. It also regularly provided assistance to some smaller departments in costing exercises. It had been able to provide advice on the accounting procedures and controls appropriate for loan schemes for the poultry industry or for building and fire safety improvement schemes in recent years; and

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- the Treasury's recent and current development work concentrated on making financial systems operate more efficiently and in a more user-friendly style. This had a direct bearing on the working environment of small DAUs, simplifying and streamlining their interfaces with central government requirements and facilitating their access to the information in the systems.

11. The Committee noted from paragraph 2.9 of the Audit Report that the FB had issued three Financial Circulars, i.e. Financial Circular Nos. 6/86, 4/92 and 4/94, which required Controlling Officers to constantly monitor the establishment. According to the survey results stated in paragraph 2.10 of the Audit Report, 20 of the 72 bureaux and departments had not conducted any establishment reviews during the period from 1991-92 to 1999-2000. The Committee considered that without establishment reviews, a lot of posts which should have been deleted might not have been detected. As the Treasury did not play a monitoring role, it did not address the problem of non-compliance by the bureaux and departments with the requirements set out in the Financial Circulars. Against this background, the Committee asked whether a mechanism should be put in place to ensure that establishment reviews of DAUs were conducted.

12. The **Secretary for the Treasury** informed the Committee that:

- according to section 12 of the Public Finance Ordinance, the responsibility rested with a Controlling Officer. There were currently more than 80 Controlling Officers, who were mostly policy secretaries and heads of department. A Controlling Officer was legally responsible for the resources under his control. A Controlling Officer was made accountable through funding applications, responding to the Audit Reports and attending the public hearings of the Committee. The FB was responsible for issuing guidelines to remind Controlling Officers to discharge their duties in accordance with the Public Finance Ordinance. However, the FB did not designate staff to check whether bureaux and departments had conducted establishment reviews of their DAUs or regular reviews of other staff establishments on their own initiative;
- although the Controlling Officers of 20 bureaux and departments had not conducted establishment reviews of their DAUs, they might have conducted general establishment reviews of their bureaux or departments. With the launch of the Enhanced Productivity Programme two years ago and the Voluntary Retirement Scheme for civil servants last year, Controlling Officers were required to review the resources of their bureaux or departments as a whole. As a result, many Controlling Officers had looked into the possibility of deleting posts and reorganising the work procedures in order to achieve automation; and

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- the review pertaining to Financial Circular No. 4/94 was currently in progress. The FB hoped to issue a new Financial Circular in due course in order to remind Controlling Officers again to discharge their duties in accordance with the Public Finance Ordinance.

13. The Committee enquired whether the Secretary for the Treasury would issue instructions to the 20 bureaux and departments which had not conducted any establishment reviews of their DAUs or investigate why they had not conducted the reviews.

14. The **Secretary for the Treasury** replied that the decision on the level and number of staff required for the operation of DAUs entirely rested with Controlling Officers. The same applied to the creation or deletion of posts. However, in creating the post of an Accounting Officer, a Controlling Officer would have to apply to the head of the Treasury grade, i.e. the Director of Accounting Services, for arranging an Accounting Officer to fill the post.

15. According to section 13 of the Public Finance Ordinance, “Every controlling officer shall obey all regulations made and directions or instructions given by the Financial Secretary under section 11 and shall, if so required, account to the Financial Secretary for the performance of his duties as controlling officer”. The Committee understood that the FB was authorised by the Financial Secretary to issue the instructions. They enquired whether, under section 13, the Secretary for the Treasury had the authority to require Controlling Officers to account for the establishment of their bureaux or departments.

16. The **Secretary for the Treasury** stated that:

- as an established practice, when a Controlling Officer requested additional resources for the next financial year in the annual resource allocation exercise, the FB would ascertain whether the existing resources in the area of work concerned were adequate for meeting the needs of additional work proposed, or additional responsibilities to be discharged, by the Controlling Officer; and
- from 1981 to 1985, there were staff in the establishment of the FB to conduct establishment reviews of bureaux and departments. However, in the mid-1980s, the FB delegated to Controlling Officers the power to conduct such reviews. In doing so, Controlling Officers could seek assistance from the Efficiency Unit and the Management Services Agency.

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17. In view of the Secretary for the Treasury's authority under the Public Finance Ordinance and the non-compliance by Controlling Officers with the requirements set out in the Financial Circulars to conduct establishment reviews, the Committee asked whether the Secretary should play a more active role in monitoring the bureaux and departments and would step up efforts to improve the situation.

18. The **Secretary for the Treasury** responded that she would consider whether the FB had the manpower and the capability to do so.

19. Paragraph 2.20 of the Audit Report revealed that in 1999-2000, the system support services had been provided at a cost of about \$145 million. As only one department of the 72 bureaux and departments covered in the audit survey had taken into account the accounting and financial support services of the Treasury in reviewing the establishment of its accounting staff, the Committee asked:

- whether the existing manpower of the Treasury was able to meet the demand for support services from all the 72 bureaux and departments; and
- whether, in view of the lack of demand for support services, there had been a waste of manpower in the Treasury.

20. The **Director of Accounting Services** said that:

- the Treasury was responsible for the operation of a central accounting system for use by government departments. The system was a central computerised system, which served as a general ledger of the Government. The Treasury also operated a government payment system and other supporting systems. The cost of \$145 million covered the operating cost of all these systems;
- there were more than 10 staff members in the Treasury providing support services to bureaux and departments. At the beginning of a year, the officer-in-charge had to submit a work plan for the year to the Director of Accounting Services, and at the end of the year, he was required to submit a report on both completed and outstanding jobs with the reasons for being unable to complete all the jobs as scheduled. In most of the cases, the delay was caused by unforeseeable circumstances, such as requests from other bureaux or departments for assistance. With the formulation and implementation of new work plans every year, there was no waste of manpower at all; and

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- past experience of the Treasury revealed that bureaux and departments often sought assistance mainly on cost accounting and development of accounting systems. The chance of the 72 bureaux and departments seeking assistance simultaneously from the Treasury was very slim. Should this really happen and if their requests only concerned simple enquiries, the Treasury should be able to cope. However, if their requests were related to the development of large-scale computer systems, the Treasury would not have adequate resources to assist them and would have to set priorities.

21. The Committee further asked whether, in setting up a division in the Treasury to provide support services to bureaux and departments, the policy was to reduce the manpower of the DAUs of the bureaux and departments. In response, the **Director of Accounting Services** said that bureaux and departments varied in size. In larger bureaux or departments, the officer-in-charge of the DAU might be a senior officer of the Treasury grade. It might not be the case for medium-sized bureaux or departments. In smaller bureaux or departments, only Executive Officers or Clerical Officers were in charge of the DAUs. As their accounting training, expertise and experience were not adequate, they would need assistance from the Treasury in solving problems. Thus, the main purpose of providing support services was to assist all bureaux and departments.

22. At the invitation of the Committee, **Mr Dominic CHAN Yin-tat, Director of Audit**, supplemented that the purpose of the system support services was to provide technical support rather than to reduce the day-to-day workload of bureaux and departments.

The provision of staff for DAUs of three departments with significant changes in accounting workload and job complexities

23. The Committee noted from paragraph 3.3 of the Audit Report that, after the commencement of operations of the new Hong Kong International Airport, the CAD had handed over a large part of its DAU's work relating to the collection of airport fees and charges to the Airport Authority (AA). The number of revenue items under the responsibility of the DAU of the CAD had decreased by nearly 60%; the CAD's revenue collection had dropped by over 70%. Paragraph 3.4 further revealed that despite the significant reduction in the CAD's revenue portfolio, up to 30 September 2000, the permanent staff establishment of its DAU had only been reduced by 6%. The Committee were not convinced by the Director-General of Civil Aviation's explanation in paragraph 3.8(d) that a significant reduction in revenue did not necessarily entail a corresponding reduction in workload. They therefore asked:

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- with the significant reduction in the accounting workload of the CAD, why only a few posts had been deleted from the establishment of its DAU; and
- whether the CAD would conduct an establishment review of its DAU shortly.

24. **Mr Alex AU, Acting Director-General of Civil Aviation**, replied that:

- the DAU of the CAD had been streamlined. There were more than 700 staff members in the overall establishment of the CAD, but only 29 were in the DAU. Seven of them were of the Treasury grade, and the rest of the clerical grade. In the light of a reduction in the workload, one clerical post had been deleted from the establishment of the DAU. With the deletion of two of the nine Treasury grade officer posts, the number of staff of this grade had actually been reduced by 22%;
- a reduction in revenue of the CAD after the opening of the new airport did not entail a corresponding reduction in its workload, because collection of certain revenue had become more complicated than before. For instance, the planes of some airlines flew through Hong Kong's airspace but did not land in Hong Kong. The process of recovering the charges of a few thousand dollars from the airline operators concerned was cumbersome. Hence, the workload was not proportionate to the amount of revenue. Previously, when the airport was at Kai Tak, planes were required to land there. It was easier to recover the charges. In addition, the CAD was responsible for collecting licence fees from airline operators which had acquired new planes and increased flying crew and engineering staff. The procedure was rather cumbersome; and
- the current procedure for collecting aircraft en route navigation charges was partly automated and partly manual. The CAD had to obtain some of the information from the radar and input it into the computer for calculation, which was a rather cumbersome procedure. The flight routes in the region often changed. They had changed once before the commissioning of the new airport, and there would be further changes at the end of 2001. The CAD hoped that when the flight routes became more stable, it could step up the automation of the procedure and review the staff establishment of its DAU.

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25. The Committee further enquired when the CAD would review the establishment of its DAU. The **Acting Director-General of Civil Aviation** said that:

- the changes in flight routes would come into effect on 1 November 2001. The CAD's past experience revealed that many airlines might not be able to provide accurate information subsequent to changes in flight routes. It would take them half a year to settle down. The CAD also had to carry out testings on its computer system. It was expected that the computer system would be commissioned around the third quarter of 2002. The establishment review would be conducted half a year after the commissioning of the computer system; and
- in the meantime, the CAD would conduct reviews, including monitoring the accuracy of the returns from the airlines and the enhancement of the efficiency of the computer system. The whole exercise would be completed in about two years.

26. According to paragraph 3.8 of the Audit Report, the Director-General of Civil Aviation stated that there was no immediate need to review the staff establishment of the DAU of the CAD as a whole. The Committee asked whether the Director-General still considered that the existing staffing level of the DAU was appropriate.

27. The **Acting Director-General of Civil Aviation** advised the Committee that:

- the CAD had conducted a comprehensive review of its work both before and after the relocation of the airport. Aircraft landing fees were charged by the AA, but the CAD had to recover a portion of the fees for the provision of air traffic control services. As listed in Appendix A to the Audit Report, there was a new revenue item "services to the AA" amounting to \$620 million, which was related to aircraft landing fees; and
- the CAD had to collect aircraft en route navigation charges from the airline operators, which amounted to \$131 million in 1999-2000. The procedure was relatively cumbersome, which had to be dealt with by a computer system. As some airline operators did not set up offices in Hong Kong, the CAD sometimes had to recover the charges from the operators in places such as the Middle East and the United States. It was hoped that the use of the computer system in calculating the charges would speed up the procedure and enhance the efficiency.

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28. The Committee further queried whether there was duplication in terms of the organisation structure and the operating cost of the CAD and the AA, given that each of them had its own pool of accounting staff.

29. The **Acting Director-General of Civil Aviation** responded that on the question of the relationship between the CAD and the AA, as the former provided air traffic control services to the latter, it had to recover the charges from the latter. The recovery of the charges by the AA from other parties was provided in the relevant legislation. Under the law, the AA was required to submit through the CAD proposals on charges to the Chief Executive for approval. Hence, the CAD was involved in the procedure as required by law. This was a matter of legal requirements, not a matter of duplication of the organisation structure.

30. The Committee noted from Note 5 of the Audit Report that two accounting posts were created in 1990-91 to meet the needs of the new airport project. Although the new airport was completed in 1998, the two posts had not been deleted until 2000. The Committee asked about the reasons for this.

31. The **Acting Director-General of Civil Aviation** said that as the two staff members had to perform some follow-up work, they could not leave immediately after the closure of the Kai Tak Airport. The situation had all along been under review. After the transfer of the two staff members, the posts had not been filled, and the deletion was completed at a later stage.

32. The Committee noted that the CAD, the FEHD and the LCSD had stated that there was no immediate need to review the staff establishment of their respective DAUs. The Committee considered that the Controlling Officers concerned should proactively invite the FB and the Treasury to assist them in conducting establishment reviews of their respective DAUs.

33. In response, the **Secretary for the Treasury** said that what was crucial to an establishment review was that a Controlling Officer considered that there was a need to conduct the review, rather than being compelled to do so. Co-operation would enable the review to complete smoothly. The FB attached much importance to the delegation of power to Controlling Officers, because with the delegation, they were required to undertake responsibilities.

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34. In response to the Committee's request for the CAD to reconsider its stance on the need to conduct an establishment review of its DAU, the **Director-General of Civil Aviation**, in his letter of 24 May 2001, in *Appendix 14*, stated that:

- the CAD had undertaken on-going reviews of the staffing requirement of its DAU in order to cope with the changes in accounting work and revenue collection procedures, so that the DAU could provide cost-effective services to the CAD's business partners as well as the department itself. The reviews were conducted through assessments of workload, as well as discussions and consultations with staff at staff meetings; and
- the CAD would review the staff establishment of its DAU as a whole in the last quarter of 2001-02, taking into account the impact of the restructuring of the airspace in November 2001 on the collection of en route navigation charges. The CAD would consult the Director of Accounting Services, the Secretary for the Treasury and other government departments in the process.

35. The Committee asked about the Director of Leisure and Cultural Services' latest stance on the need to review the staff establishment of the DAU of the LCSD.

36. **Mr Paul LEUNG, Director of Leisure and Cultural Services**, stated at the public hearing and in his letter of 22 May 2001, in *Appendix 15*, that:

- the LCSD had only been in operation for over one year. It was too early to determine whether the staff establishment of its DAU was appropriate. Nevertheless, the LCSD would pay due regard to the views of the Director of Audit and the Committee, as well as the importance of providing cost-effective services;
- the supernumerary post of Assistant Director (Finance) created on 1 January 2000 for a period of two years was due for review. The LCSD was considering whether the post should be downgraded to Chief Treasury Accountant. It planned to submit its recommendations to the LegCo Establishment Subcommittee and the LegCo Finance Committee before the end of 2001; and
- as regards the staffing of its DAU, the LCSD was planning to conduct a review in early 2002 to ensure that the establishment was appropriate. The recommendation of the review was expected to be implemented in the second half of 2002.

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37. Regarding the staff establishment of the DAU of the FEHD, the Committee noted from paragraph 3.20(j) of the Audit Report that the Director of Food and Environmental Hygiene did not consider that there was scope for further reduction. The Committee understood that following the dissolution of the two provisional municipal councils, there would be a transitional period in the operation of the departments concerned. The Committee asked whether the FEHD had a timetable for conducting an establishment review.

38. **Miss Sarah WU, Acting Director of Food and Environmental Hygiene**, who attended the public hearing, and the **Director of Food and Environmental Hygiene** in her letter of 24 May 2001, in *Appendix 16*, responded that:

- the FEHD would carry out a staffing review of its DAU in the light of further experience. In the coming six months, the FEHD would set up several major systems, such as those relating to the rental adjustment mechanism and the provision of better licensing services. The reviews of the systems were expected to complete before mid-2002. Then the FEHD would carry out an establishment review; and
- the target commencement date of the establishment review was June 2002. It would take six months to complete the review. Subject to the availability of funding, the FEHD expected to implement the recommendations in May 2003. The FEHD would consult the relevant departments so as to decide the scope of the review and the staffing requirement.

39. The Committee considered that if in the course of their establishment reviews, the FEHD and the LCSD identified some redundant posts, it should delete them immediately and did not need to wait until the completion of the reviews. In response, the **Acting Director of Food and Environmental Hygiene** said that all Controlling Officers already took this into account in drawing up their annual estimates and the plans to enhance productivity.

40. **Conclusions and Recommendations** The Committee:

Need for reviews of staff establishment of departmental accounting units (DAUs) based on objective criteria and productivity standards

- express concern that:
 - (a) the Treasury is currently playing a reactive role in offering assistance to government bureaux and departments; and

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- (b) the support services of the Treasury's Financial Management Services Division were not well-utilised although such services are available to all bureaux and departments;
- note that, in the light of the current review of the Government Financial Management and Information Systems (GFMIS) and the major change in the Government's Financial Reporting Policy, the Treasury is likely to have a more significant role to play in assisting bureaux and departments in assessing their need for financial management and accounting expertise;
- recommend that the Secretary for the Treasury should, in consultation with the Secretary for the Civil Service and the Director of Accounting Services, take proactive action to address the financial management needs of bureaux and departments, especially those which control significant financial resources;
- express concern that:
 - (a) quantifiable measures, such as performance targets and indicators or manning scales, had not been used by bureaux and departments in assessing the workload, and the level and number of accounting staff of their DAUs; and
 - (b) little information was provided by bureaux and departments in the Departmental Establishment Committee papers or the Controlling Officers' Reports of the Annual Estimates on the cost-effectiveness, productivity and performance of the DAUs in terms of the number of staff engaged, the quantity of output, and the DAUs' contributions towards meeting departmental targets;
- recommend that the Secretary for the Treasury should consider issuing guidelines to Controlling Officers:
 - (a) specifying the updated functions and duties of DAUs, and reminding them that they should regularly review the functions and outputs of the DAUs under their control, with due regard to the outcome of the review of the GFMIS and the recommendations arising from the review of the Government's Financial Reporting Policy on the need to use accrual accounting in the Government;
 - (b) requiring them to ensure that the number and ranking of DAU posts meet the current needs of bureaux and departments; and

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- (c) reminding them that if there is a mismatch between the requirement of services to be provided by a DAU and its existing staff resources, the bureau or department concerned should expeditiously deal with the mismatch by the creation, deletion or re-grading of posts;
- note the Director of Accounting Services' comments that it would not be cost-effective for departments with smaller DAUs to conduct establishment reviews of their DAUs and establish objective productivity standards;
- recommend that the Director of Accounting Services should:
 - (a) in conjunction with the Secretary for the Treasury and the Secretary for the Civil Service, consider establishing objective criteria (e.g. the financial resources controlled by a department and the specific job requirements of the DAU posts) and productivity standards for DAUs of a significant size, in order to guide Controlling Officers in assessing the number and ranking of posts required for their DAUs;
 - (b) consider implementing other alternative measures appropriate for smaller DAUs; and
 - (c) extend the scope of the Treasury's on-going review of the requirement for financial management and accounting expertise to cover more bureaux and departments, taking into account the financial resources controlled by them, the complexity of their accounting work and the support services provided by the Treasury;

The provision of staff for DAUs of three departments with significant changes in accounting workload and job complexities

- express concern that:
 - (a) despite the significant reduction in the Civil Aviation Department's (CAD's) revenue portfolio, up to 30 September 2000 the permanent staff establishment of its DAU had only been reduced by 6%;
 - (b) there were no supporting data to indicate how the staff establishment of the DAU of the CAD after the opening of the new Hong Kong International Airport at Chek Lap Kok had been arrived at; and

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- (c) there were no supporting data to indicate how, with the significant changes in the accounting workload and job complexities of the Food and Environmental Hygiene Department (FEHD) and the Leisure and Cultural Services Department (LCSD), the reduction in the staff establishment of the DAUs in the departments had been arrived at;
- note that:
 - (a) the Director-General of Civil Aviation would, in consultation with the Secretary for the Treasury and the Director of Accounting Services, review the staff establishment of the DAU of the CAD in the last quarter of 2001-02;
 - (b) the Director of Food and Environmental Hygiene would, in consultation with the government departments concerned, review the staff establishment of the DAU of the FEHD in June 2002; and
 - (c) the Director of Leisure and Cultural Services would, in consultation with the government departments concerned, review the staff establishment of the DAU of the LCSD in early 2002;

Need to establish a management information system and performance measures

- express concern that:
 - (a) all the 72 bureaux and departments covered in the audit survey did not have a management information system for recording the accounting workload of their DAUs and the related staff costs; and
 - (b) most of the bureaux and departments did not have any performance targets and indicators for measuring the productivity of their DAUs;
- recommend that the Director of Accounting Services should, in conjunction with the Secretary for the Treasury, consider issuing guidelines to Controlling Officers on:
 - (a) the development of a management information system for use by bureaux and departments for recording the workload of each kind of accounting work and the related staff costs;

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- (b) the establishment of performance targets and indicators for measuring the workload and productivity of accounting staff on the different types of accounting work; and
 - (c) such other alternative measures appropriate for smaller DAUs; and
- wish to be kept informed of:
- (a) the progress on issuing guidelines on reviews of the staff establishment of DAUs based on objective criteria and productivity standards;
 - (b) the outcome of the respective staff establishment reviews of the DAUs of the CAD, the FEHD and the LCSD; and
 - (c) the progress on issuing guidelines on the development of a management information system and the establishment of performance measures.

Chapter 4

Review of the Hong Kong Sports Development Board

The Committee held a public hearing on 14 May 2001 to receive evidence on this subject from the Secretary for Home Affairs and the Executive Director, Hong Kong Sports Development Board. The Committee also received additional information from the witnesses after the public hearings.

2. To allow themselves more time to consider the various issues involved and the additional information provided by the witnesses, the Committee have decided to defer a full report on this subject.

Chapter 5

Government's efforts to promote e-business in Hong Kong

Audit conducted a review on the Government's efforts to promote e-business in Hong Kong. The review covered the following areas:

- the Government's efforts to establish a legal framework for conducting e-business;
- the Government's efforts to establish a public key infrastructure (PKI);
- the progress made by the Government in implementing various e-business initiatives;
- the Information Technology and Broadcasting Bureau's (ITBB's) strategy for developing e-government; and
- the Government's efforts to meet common challenges associated with the growth of e-business.

The ITBB's strategy for developing e-government

2. The Committee noted that it was the Government's strategy to lead by example in practising e-business. According to paragraph 5.6 of the Audit Report, the governments of those countries which were advanced in developing e-government, such as the USA, the UK, Singapore and Canada, had set targets for implementing e-government. The Committee asked whether the Administration intended to set a clear target for achieving the full implementation of e-government in the Government of the Hong Kong Special Administrative Region.

3. **Mrs Carrie YAU, Secretary for Information Technology and Broadcasting**, said that:

- the ITBB agreed that the target for the full implementation of the e-government policy should be clearly set out. In the strategic document entitled "The 2001 Digital 21 Strategy: Connecting the World" recently published by the ITBB, the flagship e-government projects were classified into four categories, viz. Government-to-Citizen (G2C), Government-to-Business (G2B), Government-to-Employee (G2E) and Government-to-Government (G2G). The target implementation dates for the various initiatives were laid down; and

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- in setting the target dates, the ITBB had made reference to the best practices of other countries. For instance, the Government aimed to carry out 80% of government procurement tenders through electronic means by the end of 2003. Also, the Government aimed to provide an e-option for 90% of the public services amenable to the electronic mode of service delivery by the end of 2003, as compared to the USA's target of providing such services by 2003 and the UK's target of 2005.

The Government's efforts to establish a PKI for conducting e-business and the logistics service provided by the Hongkong Post (HKP) for e-business

4. The Committee noted from paragraph 3.6 of the Audit Report that in December 1999, the HKP estimated that it would issue 171,000 digital certificates (e-Certs) for the 15-month period ending 31 March 2001, increasing to 494,000 in the year 2004-05. However, up to December 2000, only 5,900 e-Certs had been issued, representing 3.5% of the estimated figure by 31 March 2001. The Committee asked why there was such a huge variance between the estimated and actual numbers.

5. **Mr LUK Ping-chuen, Postmaster General**, informed the Committee that:

- the HKP commenced the planning and data collection stages of its certification authority (CA) service in 1998. After conducting a tendering exercise in early 1999, the service was launched in January 2000; and
- the original forecast of 171,000 e-Certs to be issued up to March 2001 had been made after consulting the industry and was based on the global trend at the time when the HKP's service was launched. At that time, there were a lot of discussions about e-transactions and it was envisaged that the usage of e-Certs would be high. However, by the end of 1999 and the year 2000, many e-commerce companies had ceased operation. The development of a number of business applications that supported the use of digital certificates had to be stopped or deferred, directly affecting the number of e-Certs issued.

6. To ascertain whether the HKP had conducted thorough market research before projecting the popularity of e-Certs, the Committee further asked:

- what the professional experts or bodies the HKP had consulted before making the forecast of 171,000 e-Certs, and what the results of the consultation were; and

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- whether the HKP had carried out any in-depth market research on the growth of e-business and the development of business applications that supported the use of e-Certs.

7. The **Postmaster General**, in his letter of 14 June 2001 in *Appendix 17*, stated that:

- in July 1998, the HKP accepted the invitation of the Secretary for Information Technology and Broadcasting to serve as the public CA in Hong Kong to provide security and trust in the conduct of electronic transactions under a PKI. To tie in with the implementation of the first phase of the Government's Electronic Service Delivery Scheme in 2000, the HKP's CA service was launched in January 2000;
- in view of the complexity of the CA project and the tight schedule for completion, the HKP created a dedicated project team. Among other things, the project team interviewed and discussed with information technology (IT) professionals and business analysts of major businesses and industries in Hong Kong. Almost all of them, including those from the banking, finance, telecommunications, health, trading, entertainment and education sectors, expressed keen interest in developing PKI-based applications. At the conclusion of the business interviews, the HKP had also ascertained the size of the potential market for e-Certs;
- to re-affirm the business potential of CA services as a trusted third party, the HKP commissioned the Hong Kong University of Science and Technology (HKUST) to conduct a market research from September to October 1998. The research took the form of a mail questionnaire (followed up by telephone calls) sent to 3,000 companies randomly selected from different industrial sectors. In addition, a number of IT professionals and business executives were interviewed;
- as both the HKP's direct interviews with potential users and the results of the HKUST's market research indicated optimism for growth of e-commerce in Hong Kong and a high demand for the HKP's CA services, the forecast of 171,000 e-Certs was made; and

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- by the end of 1999 when the HKP's CA service was about to be launched, the market sentiment for all e-commerce businesses turned low. Many e-commerce companies had been downsized or wound up. As a result, many PKI-based applications were either deferred or aborted, affecting the demand of e-Certs for various businesses and industries. Therefore, the actual number of e-Certs issued in 2000 fell below the original forecast.

8. In the same letter, the **Postmaster General** said that:

- with the launch of the Electronic Service Delivery Scheme in December 2000 and some other PKI-based applications in the private sector, the number of e-Certs issued had risen to 20,106 as at 8 June 2001. It was envisaged that by working with banks and many other e-commerce businesses, the number of e-Certs would grow steadily; and
- the HKP considered that the assessment of the business viability of the CA service based on the performance of the first year of operation was not appropriate.

9. Regarding the CA service and logistics service provided by the HKP, the Committee noted that the actual revenue of these two services fell far short of the original estimated revenue. Paragraphs 3.13 and 3.14 of the Audit Report revealed that the CA service was intended to be financially self-sufficient. Yet it turned out to be operating at a loss of \$8 million in 2000-01 (for the seven months up to October 2000). According to paragraphs 4.65 and 4.66, the HKP estimated that its logistics service could earn revenue of some \$2.7 million for 2000-01. However, for the first 11 months of operation, the actual revenue earned was only \$2,000. Under the circumstances, the Committee enquired:

- when the HKP expected its CA service to be financially self-sufficient; and
- whether the low business volume of the logistics service was due to a lack of competitiveness of the HKP's service.

10. The **Secretary for Information Technology and Broadcasting** responded that:

- the CA service, being part of the PKI, was different from other kinds of services for which cost recovery could be achieved within a short time. The provision of the PKI by the Government was essential for ensuring a successful future for e-business in Hong Kong. Hence, the HKP might need to continue to provide the CA service even if the service was not financially self-sufficient; and

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- as the HKP's CA service had been in operation for only one year, it was too early to assess its financial viability. The popularity level of e-Certs was bound to increase when more business applications were developed.

11. The **Postmaster General** supplemented that:

- as the provision of CA service was an infrastructural project, the Government must take the lead in providing such service. Only then would the entire community move in the direction of e-business;
- it was estimated that, given the present situation, the CA service would be able to achieve operational balance and recover the setting-up cost of \$60 million in the next five years. Although the development of e-commerce was rather slow currently, the estimate throughout the world was that there would be a peak in three years' time. Notwithstanding the optimistic forecast, the actual situation would hinge on the development of e-commerce and the development of technology in the e-Cert field;
- the HKP launched the logistics service to support e-business so that small and medium enterprises could be provided with one-stop supply chain management services for their e-business. The estimated business volume was made in January 2000 when the service was commissioned. Since then, many e-commerce companies had been closed down. Although the HKP had discussions with many potential customers, the discussions failed to reach agreement at the last stage of the negotiation due to the unfavourable e-business environment; and
- while the logistics service provided by the HKP included all the seven items listed in paragraph 4.63(a) to 4.63(g) of the Audit Report, some customers required only part instead of the full range of the service. The HKP provided the service as requested by the customers but the revenue so generated was not classified as revenue from the logistics service. In other words, the actual revenue generated from the provision of logistics service was more than \$2,000.

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12. The Committee enquired whether the HKP was the sole provider of the CA service or whether there were other CAs in the private sector. The Committee considered that if the HKP was providing the service at a loss and thereby the Government was in fact subsidising the service, that would be unfair to other service providers. Referring to the Postmaster General's statement that the HKP's CA service would be able to achieve financial balance in the next five years, the Committee further asked how the estimate was arrived at and whether, in calculating the estimate, the HKP had taken into account its recurrent operational costs.

13. The **Secretary for Information Technology and Broadcasting** and **Mr CHENG Yan-chee, Acting Director of Information Technology Services**, said that:

- the policy objective of the Government was to encourage the emergence of more CAs in the market while the Government's role was to take the lead in the provision of the CA service. Actually, the HKP was the first organisation in Hong Kong which complied with all the international standards for a CA;
- under the Electronic Transactions Ordinance, the Director of Information Technology Services was vested with the authority to recognise CAs in order to ensure that the CAs met international standards. The Information Technology Services Department had in the past received a number of enquiries about how to apply for recognition. Several organisations had already applied for approval to appoint examiners to examine their operation, which was a prerequisite for applying for recognition as a CA; and
- the Government did not want to compete with the private sector. When there were other CAs available in the market, the Government would achieve its target of playing the role as a pioneer in the field. In fact, the HKP was already developing new service such as mobile certification. Venturing into new areas was very risky. Without the pioneering work and resources of the Government, it would be difficult for the private sector to develop such new services.

14. Regarding the cost recovery for the CA service, the **Postmaster General** explained that:

- the HKP's estimate that its CA service could be financially self-sufficient in five years' time was based on the discussions with those organisations which were interested in using the HKP's existing CA service, as to when they would use the HKP's service and the estimated usage level. The estimated

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revenue included the e-Cert fees and the income that might be generated from joint projects with these organisations. In calculating the estimated expenditure, the HKP had taken into account all the capital and operational costs, including the setting-up cost of \$60 million after allowing for depreciation, salaries and accommodation cost;

- the HKP had not subsidised the CA service with income from the postal service. Indeed, the two services were operated under two separate cost centres of the HKP and each had its own revenue and expenditure. This was published in the HKP's annual report. Being a trading fund department, the HKP operated according to business principles;
- the HKP estimated that its CA service would only be able to break even in the next five years, but would not make a profit. The HKP's efforts had enabled the Government to achieve its aim of being a leader in providing the service. This was reflected by the fact that applications for recognition as CAs were now coming in. Had the HKP not assumed the pioneering role, it was uncertain when companies in the private sector would be interested in taking up the work; and
- since the launching of the service in January 2000, the HKP had been actively promoting the service. In the 14 months between February 2000 and April 2001, 160 seminars had been organised on this subject. Through the Hong Kong Trade Development Council and the Hong Kong Productivity Council, the HKP had been able to meet interested organisations and a lot of small and medium enterprises for promotion and educational purposes. All these proved that the Government had indeed played a leading role on this front.

15. As many e-commerce companies nowadays had taken drastic actions to downsize in the light of the current market environment, the Committee asked whether, since the launching of its CA service in January 2000, the HKP had taken any action to reduce the size of its CA operation so as to minimise its recurrent cost and operating loss.

16. The **Postmaster General** informed the Committee in his letter of 21 June 2001, in *Appendix 18*, that:

- the HKP's CA project had all along been managed by a small establishment of staff which was just enough to cope with the daily operation work. Since the launching of the service in January 2000, the HKP had gradually strengthened the team by a number of additional marketing and technical staff dedicated to promoting the CA service, educating the general public on

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the use of e-Certs, and exploring and implementing specific business applications of the CA service with relevant government departments and private-sector e-business partners. These staff were employed on contract;

- the value of the staff members' efforts was evidenced by the recent increase in the quantity of e-Certs issued. The HKP considered that it made business sense to sustain the momentum of the marketing and business development efforts as additional applications of the CA service would be generated, bringing in revenue that could offset the sunk cost of the HKP's investment; and
- the HKP was fully aware of the need to ensure value for money for its recurrent expenditure on the CA operation and would continue to monitor its expenditure and revenue position on a regular basis.

17. The Committee noted Audit's recommendation in paragraph 3.20 that a review of the Government's strategy for funding the HKP's CA service should be conducted in order to resolve any conflict between the Government's financial objective (i.e. self-sufficiency of the CA service) and its broader objective of promoting e-business. According to paragraph 3.21, the Secretary for Information Technology and Broadcasting had agreed to undertake the review when the ITBB and the HKP had gained more experience in the operation of the service. The Committee asked whether a target date for conducting the review had been set.

18. In her letter of 19 June 2001 in *Appendix 19*, the **Secretary for Information Technology and Broadcasting** advised the Committee that:

- the HKP's CA facility was a new infrastructural service in Hong Kong and it took time to build up confidence in the businesses and the community and gain widespread adoption. The HKP was implementing various initiatives to enhance the CA service and was exploring new business opportunities with outside business organisations on electronic applications to drive the use of digital certificates. The ITBB therefore considered that it would be premature to carry out the review of the financial viability and funding strategy for the HKP's CA service at this stage, particularly at the time when e-commerce activities had been affected by the current economic environment; and

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- with the above considerations, the ITBB intended to conduct a review in late 2002, taking into account the readiness of the community in adopting digital certificates, the maturity of applications using digital certificates in the market and the general development of CA market in Hong Kong.

19. As for the business viability of the HKP's logistics service, the Committee wondered whether the poor performance of the service reflected that the HKP's way of operation could not meet customers' requirements. In view of the fact that companies which suffered annual losses would normally be closed down, the Committee asked at what point the HKP would decide to stop providing the logistics service.

20. The **Postmaster General** replied that:

- from the outset the HKP was fully aware of the difficulties involved in starting up the logistics service which was a new concept and new service. Therefore, it was cautious in committing resources to this service. The only setting up cost incurred was in the development of a new computer system. No additional staff had been involved as existing staff were redeployed to take up the work. The recurrent cost was only \$132,000 a year, which was mainly for computer hardware maintenance and software licence fees;
- although many large companies had been closed down in the past two years, the HKP still considered that the logistics service had room for development in Hong Kong. Indeed, the HKP had special strength in the delivery of articles. Although the HKP's costs might be higher than other logistics service providers in the private sector due to its higher wages, the costs could be lowered if it made use of existing resources to provide the service. Moreover, the HKP had a reputable brand name. Given the HKP's strength and the small annual recurrent cost, the HKP would continue to provide the service for small and medium enterprises for the time being; and
- there was a committee in the HKP chaired by himself which was responsible for reviewing the logistics service, including the direction of future development as well as the progress. Based on the review results, the HKP would adjust the operation for the service. The committee would conduct a major review in 2002 and the HKP would then decide whether to continue with the logistics service.

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The Government's progress in implementing various e-business initiatives

21. Turning to the Community Electronic Trading Service, the Committee understood from paragraphs 4.10 to 4.13 of the Audit Report that in the light of developments in Internet technology and e-business, and in order to introduce competition, the Commerce and Industry Bureau (CIB) had concluded that additional service providers should be engaged upon the expiry of Tradelink's franchise on 31 December 2003. According to the CIB's action plan, a lead time of 29 months would be needed to complete the necessary tasks for introducing additional service providers. The Committee also noted Audit's comment that as many of these tasks were complex and time-consuming, careful forward planning and close monitoring were crucial to ensure that competition was introduced successfully, and that the provision of essential services would not be disrupted upon the expiry of Tradelink's franchise.

22. In the light of Audit's observations, the Committee asked about the CIB's action plan and whether there would be a possibility of disruption of service.

23. **Mr CHAU Tak-hay, Secretary for Commerce and Industry**, responded that:

- the Government was the major shareholder of Tradelink and, as the Secretary for Commerce and Industry, he was the non-executive chairman of Tradelink. Such a dual role could help avoid the scenario where the negotiations between Tradelink and the Government could not arrive at a conclusion and thereby disrupting the service. The CIB agreed that the issue was complicated and important, and would certainly deal with it cautiously;
- according to the CIB's timetable, it would take two and a half years to engage new service providers. That should be able to tie in with the expiry of Tradelink's franchise. By the middle of this year, the Government would make final decisions with regard to the arrangements for front-end services upon the expiry of Tradelink's franchise. Then the Government would invite interested companies to submit expressions of interest. The CIB would monitor the work progress according to its action plan and ensure service continuity; and
- as regards Audit's recommendation that the CIB should consult the ITBB in the formulation and execution of the action plan, actually the CIB had always drawn on the expertise of the ITBB and the Information Technology Services Department and would continue to do so.

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24. In response to the Committee's question on the CIB's plan to consult the Legislative Council, the **Secretary for Commerce and Industry** replied that the Council's Panel on Commerce and Industry had been consulted in February 2001 and the Panel had endorsed the Government's proposal on the arrangement for provision of electronic trade transaction services for the Government after Tradelink's franchise expired in end 2003.

25. Regarding the dissemination of information through the Government's homepages, the Committee understood that there was scope for improving the time required to download the homepages. They also noted from paragraph 4.19 of the Audit Report that the survey conducted in mid-2000 by the Information Services Department (ISD) revealed that using government homepages "as a means to communicate with the Government" was the least satisfactory aspect, on which 30% of the respondents gave a below average rating. Against this background, the Committee asked:

- whether surveys would be conducted regularly to gauge users' views on government homepages; and
- whether, apart from the long downloading time, there were other reasons for the respondents' adverse comments on using the homepages to communicate with the Government.

26. **Mr NG Hon-wah, Principal Assistant Secretary (Home Affairs)**, said that:

- the ISD conducted a survey to collect users' views on government homepages every year. The next survey would be conducted in the middle of this year. The surveys were conducted online where users of government homepages were asked to fill in a questionnaire on the Internet. Although the surveys did serve a purpose, statistically speaking, they were not really scientific as the users could decide by themselves whether to respond or not. Moreover, the questionnaire only asked for the users' relative impression on different aspects;
- in designing the homepages, the Government's main objective was to disseminate information through them, rather than receive information. That might explain why some users thought that if they were to pass on messages to the Government, the homepages might not be an effective instrument;

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- the survey result referred to in the Audit Report was that of last year. Starting from this year, the e-mail address of the government department had been placed at a prominent location in the homepage concerned. Members of the public who would like to communicate with a department through electronic means could simply access the address given. The Home Affairs Bureau had also issued guidelines to all departments, advising them to designate staff to check the e-mails sent to their departments twice a day, and to refer the e-mails to responsible staff immediately. For special issues, such as consultation papers or other subjects on which the public might have views, there would be a column on the homepages which enabled the users to give their views directly to the departments concerned; and
- with the development of e-service, more and more members of the public would communicate with bureaux and departments through government homepages. The HAB was confident that there would be improvement in this aspect when the survey was conducted again.

27. With reference to the Electronic Tendering System (ETS), paragraph 4.48 of the Audit Report revealed that only 6.6% of the suppliers' tenders were submitted to the Government Supplies Department (GSD) through the ETS. The results of Audit's survey indicated that 39% of the respondents were satisfied with the overall performance of the ETS while 19% were not satisfied. Paragraph 4.49 further revealed that there were risks in using the i-Cert under the ETS. The Committee asked whether the ETS was lacking credibility and hence the users were not willing to use the system.

28. **Mr Gregory LEUNG Wing-lup, Director of Government Supplies**, replied that:

- the risk of using the ETS was on the GSD, not the users. This was because the i-Cert was not a recognised digital certificate under the Electronic Transactions Ordinance. If a successful tenderer's offer was submitted through the ETS, there would be a risk of repudiation of the offer as, legally speaking, the offer was not binding on the tenderer. Hence, for the sake of security and to overcome the concerns about the recognition of the i-Cert, it had been the GSD's practice to issue to a successful tenderer a request to acknowledge receipt together with the letter of acceptance; and

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- according to legal advice, the best approach to address the problem was to introduce the HKP's e-Cert to the ETS. However, the i-Cert would still have to be accepted by the GSD even after the e-Cert had been introduced because overseas suppliers would have difficulty in obtaining the e-Cert. In short, although there were operational difficulties, they could be overcome.

29. In response to the Committee's questions about the reason for the low usage rate of the ETS and the improvement measures, the **Director of Government Supplies** stated that:

- the usage rate of the ETS was growing steadily from 6.6% in early February 2001 to about 7.2% by early April 2001. In the past year, the GSD had discussed with the suppliers to gauge their views on the ETS and the difficulties they encountered in using the ETS. For instance, one of the problems was related to the private key for the i-Cert. The private key was held by the person in charge of the company, meaning that the person had to handle personally all the work relating to the ETS, including downloading tender documents and submitting tenders, etc. Under the conventional arrangement, such work could be handled by his subordinates. In the circumstances, the companies found it troublesome to use the ETS;
- another difficulty was caused by the security feature of the ETS. In order to prevent leakage, the ETS did not allow a company to download a tender document again after it had submitted the tender. This meant that the company could not change its tender price. The companies felt that such a restriction caused inconvenience and hindered their efficient operation; and
- the GSD planned to make various improvements in the coming six months to address the users' concerns. In doing so, the GSD would strike a balance between convenience and security. The GSD would consult the suppliers again on the matter.

30. Regarding the assistance that could be rendered by the ITBB to government departments in tackling the problems encountered in the implementation of e-government, the **Secretary for Information Technology and Broadcasting** said that:

- the development of e-government entailed a lot of small technical matters which required much co-ordination and assistance. The Government considered that the implementation of e-government would be very important for Hong Kong's future. Many countries would assess whether Hong Kong was an advanced city based on its ability to meet the targets for developing e-government; and

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- the ITBB had reviewed its manpower situation to ascertain if additional staff were needed for the co-ordination work. At present the work was undertaken by a deputy secretary of the ITBB who had other duties as well. For the time being, the ITBB would try to absorb the work by internal resources. If additional resources were eventually required, such as for establishing an e-government co-ordination office, the ITBB would consult the Legislative Council and seek its support.

31. **Conclusions and recommendations** The Committee:

- express serious concern that:
 - (a) there is a significant variance between the estimated and actual number of e-Certs issued (i.e. 171,000 versus 5,900) and that, although the popularity level of e-Certs has improved recently, the number of e-Certs issued (i.e. 20,106 as at 8 June 2001) is still far below expectations; and
 - (b) although the Hongkong Post's (HKP's) certification authority (CA) service is intended to be financially self-sufficient, it is in fact operating at a significant loss;
- recommend that the Postmaster General should closely monitor the usage level of e-Certs, make vigorous efforts to promote the wider use of the CA service and liaise closely with CAs abroad to meet future challenges;
- urge the Postmaster General to keep the size of the HKP's CA operation under constant review, so as to minimise the recurrent cost and operating loss and ensure that it is appropriate for the level of demand in the market;
- note that the Secretary for Information Technology and Broadcasting has undertaken to review the Government's strategy for funding the HKP's CA service in late 2002 when the Information Technology and Broadcasting Bureau and the HKP have gained more experience in the operation of the service; and
- wish to be kept informed of:
 - (a) the review of the size of the HKP's CA operation; and
 - (b) the review of the Government's strategy for funding the HKP's CA service.

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32. In respect of the other findings in the Audit Report, the Committee support Audit's recommendations in paragraphs 2.22, 4.14, 4.27, 4.39, 4.50, 4.61, 4.69, 5.20 and 6.6 of the Audit Report, urge the Administration to expeditiously follow up the recommendations and wish to be kept informed of the progress made.

Chapter 6

Management of public housing construction

Audit has reviewed the management of public housing construction projects and recommended that improvements could be made in the following areas:

- standard designs of the Housing Authority's (HA's) housing blocks;
- tendering process;
- piling works;
- monitoring of the performance of contractors;
- different roles of the HA; and
- quality housing reform.

The HA's standard designs

2. According to paragraph 2.12 of the Audit Report, the efficiency ratios (ERs) of Home Ownership Scheme (HOS) courts were lower than those of the buildings designed by private-sector developers under the Private Sector Participation Scheme (PSPS). The Committee asked whether the Housing Department (HD) agreed with Audit's view that this was partly caused by the fact that, in the HA's standard designs, the floor areas provided for common areas, such as common corridors and lift lobbies, were more generous than those provided in PSPS and private-sector blocks.

3. **Mr Marco WU, Acting Director of Housing**, responded that:

- as revealed in Table 1 of the Audit Report, some PSPS projects had an ER of 86%. Generally speaking, the ERs of PSPS projects were higher than those of HOS courts and private-sector developments. The main reason was that for PSPS projects, the sales proceeds were calculated according to the saleable area. Hence, there was no incentive for the developers to maximise the gross floor area (GFA) or to provide wider corridors and bigger common areas;
- the ER of 86% quoted in the Audit Report was to a certain extent the result of the cap imposed by the Government to ensure that the ERs achieved in PSPS projects were reasonable. The ER in PSPS projects had been capped at 86% since 1988 because at that time some PSPS developers were achieving even higher ERs at the expense of the quality of public areas; and

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- it was not the HA's objective to minimise the width of corridors or the size of lobbies. Thus, the ERs of the HA's standard block designs were lower compared to those of private-sector projects.

4. The Committee noted the Director of Housing's response recorded in paragraph 2.18(e) and (h) of the Audit Report that it had been the HA's conscious decision to provide more generous public areas in public housing blocks. The Committee asked about the rationale of the policy.

5. **Mr TONG Wing-shing, Business Director (Development) of the HD,** explained that:

- the decision was made by the HA back at a time when every tenant was entitled to only five to seven square metres. The HA decided that better and more generous public areas should be provided to compensate for the tight space allocation; and
- larger public areas were also provided to enable persons on wheelchairs to use the areas with ease.

6. While concurring that it was a good practice to provide a better living environment and better facilities for residents in HOS courts and public housing estates, the Committee were also concerned about the need for the HD to make full use of the land allocated for building more public housing flats. This would in turn help shorten the waiting time for public housing. According to the supplementary information provided by Audit, in *Appendix 20*, the total GFA of HOS courts completed in the past five years were 43,700,000 square feet. If the ER had been improved by 1%, 553 more HOS flats could have been built. Under the circumstances, the Committee enquired:

- how the HD struck a balance between the provision of a good living environment and the need to optimise the use of the land allocated to the HA; and
- whether the HD would consider increasing the ERs of HOS courts.

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7. The **Acting Director of Housing** replied that unlike the private sector, the number of flats, the population, and the number and areas of supporting facilities, such as schools, shopping and welfare facilities, in each public housing site were determined by a Planning Brief. The potential of a site had already been optimised when the requirements of the Planning Brief were met. It might not be possible for the HD to build more flats in a site simply by increasing the ER.

8. The Committee pointed out to the Acting Director of Housing that in the Planning Brief, a 10% flexibility was normally allowed for the number of new flats and the population of housing projects. As a 1% increase in the ER could already result in additional flats, the Committee asked whether the HD would make use of the flexibility to increase its flat production.

9. The Committee also noted from paragraph 2.18(a) of the Audit Report that the HA had already agreed to pursue more non-standard designs in future housing projects. While housing blocks using standard designs could be built with prefabricated building components and hence were more economical, non-standard designs allowed greater flexibility. The Committee asked whether there would be incentive for the HD to use non-standard designs and what the ratio between standard and non-standard designs would be.

10. The **Acting Director of Housing** and the **Business Director (Development)** stated that:

- the HD was indeed moving towards more flexible designs. For the Department's recent housing developments, it adopted a site-specific approach by using non-standard designs. Nevertheless, even with the adoption of non-standard designs, the HD did not aim to provide public areas of minimum standards. The HD would have to take into consideration the expectations of residents and the need to provide a decent living environment. It aimed to achieve a more efficient design without sacrificing the living environment. This was also in line with the Government's current thinking in granting more exempted GFA to encourage private developers to provide larger common areas;

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- the HA was aware that there was room for improvement to the standard designs. The HA had decided that, in future, standard designs would continue to be used, while non-standard designs which suited individual sites would also be used, so as to fully utilise the land. Currently, there was a non-standard design which achieved an ER of 82%, approaching that of PSPS or private-sector developments. In other words, using non-standard designs could probably improve the ER;
- it would be difficult to specify a ratio between standard and non-standard designs. For some sites the standard design might already be good enough to be used. But for other sites, a non-standard design might be more suitable for adoption. However, generally speaking, the HD planned to adopt non-standard designs for Group 2 HOS courts, which would account for about 20% of future developments. Therefore, non-standard designs would be used in at least 20% of the sites. For the remaining 80%, there would still be room for changing over to non-standard designs. But the proportion could not be specified in advance; and
- there were many incentives for using non-standard designs. For instance, after consultation with the public, the HD realised that the standard designs were considered too uniform and had a negative impact on the cityscape. Taking Tseung Kwan O and Tin Shui Wai as examples, many people had complained that every block there looked the same. Furthermore, from an architect's perspective, a standard design limited the room for creativity. Ultimately, the HD's objective was to make full use of the land.

11. The Committee shared the view that for some districts such as Tseung Kwan O and Tin Shui Wai, the appearance and height of the buildings were so uniform that even the mental health of the residents might be affected. The Committee further asked whether the use a site-specific layout approach to building designs would help achieve a higher ER. **Dr CHENG Hon-kwan, Chairman, HA**, said that:

- apart from using more non-standard designs, he had also suggested that HD should review the standard designs with a view to making improvements because such designs had been in use for many years. The review would not be limited to the ER, but would cover other aspects such as structure, building services and compliance with the Buildings Ordinance;

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- the HA's decision to adopt the site-specific layout approach was to ensure full optimisation of the development potential of the HA's sites. Increasing the ER did not necessarily mean that the living environment would be improved. A case in point was a block facing a highway. The Environmental Protection Department prohibited the rooms from facing the highway. This imposed constraints on the design and adversely affected the ER; and
- recently, the HA had held a design competition and the ER in the champion's design was 82%, which was a very good design. All these boiled down to the fact that whether a design was good depended on whether it suited the topography of individual sites and other relevant factors.

12. The Committee understood from paragraph 2.20 of the Audit Report that following the issue of the joint Practice Note in February 2001, some common area in the HA's current standard designs was exempted from the GFA calculation. In Note 6, Audit had commented that the HD should incorporate the exempted GFA into the saleable area. This would improve the ER and increase flat production. The Committee asked about the HD's views on Audit's suggestion and the impact of the Practice Note on the HD's design of flats.

13. The **Acting Director of Housing** replied that:

- the exempted GFA under the Practice Note provided the HD with greater flexibility for revising its designs. If it was possible to build more flats while providing more or similar common areas by making use of the exempted GFA or the flexibility allowed under the Planning Brief, the HD would certainly be willing to do so; and
- as the number of flats and the population in a public housing site was fixed by the Planning Brief, additional flats could not be built if the limits set out in the Planning Brief had already been reached.

14. According to paragraph 2.19 of the Audit Report, the Administration was reviewing the Buildings Ordinance to encourage the provision of green features. The Committee asked what resources could be saved and what the objective and progress of the review were.

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15. **Mr Gordon SIU, Secretary for Planning and Lands**, stated that:

- it was a matter of striking a balance between the provision of more flats and the provision of a good living environment to residents. To a certain extent, in order to build more flats on a piece of land, it would be necessary to build narrower staircases and narrower lift shafts, or to use enclosed designs. But that would affect the quality of the living environment; and
- the Administration encouraged the use of natural resources. For example, larger public areas would provide better natural ventilation. The use of natural lighting would reduce the need for artificial lighting. However, it would not be easy to quantify the amount of resources that could be saved. The Administration had already issued guidelines on the provision of green features in private buildings. The concept was well received.

16. **Mr LEUNG Chin-man, Director of Buildings**, supplemented that:

- in February 2001, the Buildings Department (BD) had issued a Practice Note jointly with the Lands Department and the Planning Department providing incentives to encourage developers to build green buildings. The aim was to provide the impetus to the industry to adopt more green features in building design. As this was a new initiative, its effectiveness had yet to be seen;
- the Administration was conducting a comprehensive review on the Buildings Ordinance with a view to determining the appropriate minimum standard in the provision of green features. The BD had set up a Building Innovation Unit to study the most updated designs in other territories to ascertain how energy savings were achieved in the most cost-effective manner. The Administration would take into account the effectiveness of the new initiative and the latest developments before finalising its recommendations. So far, the response of the industry and green groups was very positive; and
- the existing legislation allowed the Director of Buildings to adopt a flexible approach in approving building designs so that the environment could be improved without affecting the maximum permitted GFA. He would exercise discretion to exempt certain areas from GFA calculations, provided that safety and hygiene requirements were met.

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17. The Committee enquired whether the initiative to encourage more green features in private developments would be implemented in public housing developments. The **Business Director (Development)** replied in the affirmative. He said that improvements would be realised in the next generation of public housing. For example, the HA had recently decided to provide balconies in a redevelopment project in Hung Hom.

Tendering process

18. According to paragraphs 3.3 to 3.9 of the Audit Report, in September 1999, the HA introduced the Preferential Tender Award System (PTAS) for the award of building contracts to guard against accepting a low bid submitted by contractors who had performed poorly in the past. Under the PTAS, apart from the tender sum, the past performance of the tenderers was also taken into account in tender evaluation. In January 2000, the HA agreed to extend the PTAS to cover building services and piling contracts. However, due to the lack of a performance scoring system for such contractors, the progress of extending the PTAS had been slow. The target implementation date for the Building Services Performance Assessment Scoring System (BS PASS) 2000 had been deferred by 18 months from 1 January 2000 to June 2001. The progress of developing a performance scoring system for piling contractors was even slower. The HD expected to implement this system only by mid-2002.

19. The Committee also noted the Director of Housing's response in paragraph 3.11 that the target implementation date for the BS PASS 2000 had been revised from January 2000 to the third quarter of 2001 because it was expected that the HA's housing production would be reaching an unprecedented peak level. It was considered prudent not to fully roll out the System until the production peak was over.

20. Against the above background, the Committee queried:

- whether, apart from insufficient manpower, there were other reasons for the delay; and
- as the HA's housing production was expected to be near its peak, whether it would have been more prudent to implement the System as soon as possible before the peak level was reached rather than wait until the peak was over, so that the HD could have in place an effective system for monitoring its housing production.

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21. The **Acting Director of Housing** and the **Business Director (Development)** informed the Committee that:

- a prerequisite for implementing the PTAS was a performance scoring system for comparing contractors' past performance. In respect of building contracts, a scoring system had been in place for a long time. Hence, the PTAS could be applied to building contracts readily. For piling works, the HA had established its list of piling contractors only in August 2000. It would take some time to accumulate the scores on contractors' performance before the HD could apply the PTAS to assess tenders for piling works. For building services contracts, the development of the BS PASS 2000 had been substantially completed in early 2000. Similarly, the System could be implemented when sufficient scores had been accumulated. Actually, a trial run of the BS PASS 2000 had been launched in May and June last year. A lot of feedback was received and the System would have to be revised before implementation. This would again take quite some time;
- the PTAS was a system for selecting tenders offered by contractors. Its main purpose was to ensure that other than the tender price, the contractors' past performance would also be taken into consideration. As such, it was related to future projects and had no direct bearing on projects which were under way; and
- the HD admitted that the time taken to develop the performance scoring system had been longer than expected. However, the Department's housing production had reached a peak level. In 2000-01, 89,000 flats were built. If the HD was to implement the BS PASS 2000 despite the advent of the peak, there was bound to be undesirable impact. For the HD staff, they would have to shoulder additional work associated with the new System while at the same time dealing with the production peak. There would also be pressure on the contractors as they would have to proceed with the construction work while having to get used to a new scoring system. Under the circumstances, the HA accepted the HD's recommendation that the System should be launched later this year when the peak was over.

22. In the light of the above reply, the Committee were concerned about the quality of those housing projects which were under way. As the PTAS was intended to enable the HD to select the most suitable contractors for carrying out future projects, the Committee wondered whether the delay in implementing the PTAS for piling and building services contracts would mean that the blocks being constructed under the existing system were not monitored stringently enough. The Committee also queried whether the HD had over-estimated its abilities and thereby resulted in failure to achieve the targets set by itself.

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23. The **Acting Director of Housing** and the **Business Director (Development)** clarified that:

- the PTAS assisted the HD in choosing the most suitable bidders for its jobs, which was a separate issue from the monitoring of construction works. Even without the new performance scoring system, there were already systems in place for monitoring the contractors' performance. The aim of introducing the new system was to develop a more objective basis for evaluating the contractors' performance; and
- when the target implementation date was set, the HD had indeed underestimated the impact of the housing production peak.

24. The Committee noted that there was wide public concern about the quality of the HA's piling projects. As the HA had already established its list of piling contractors and hence scores could be given to those contractors of on-going piling contracts, the Committee questioned why the performance scoring system for piling contracts could not be implemented this year but had to wait until mid-2002.

25. The **Business Director (Development)** responded that:

- the HA was fully aware of the public's expectation. Mid-2002 was the target set earlier. The target implementation date of the scoring system for piling contracts had been revised to the fourth quarter of 2001. It was not possible to further advance the implementation date because it took time to develop an objective assessment system; and
- the HD did not just rely on a performance scoring system to monitor piling projects. In fact, many of the 50 initiatives to enhance the building quality aimed at revamping the piling process and reinforcing site supervision. These initiatives had already been implemented.

26. The Committee understood from paragraph 3.4 of the Audit Report that under the PTAS, the weightings given to tender sum and past performance were 80% and 20% respectively. The Committee enquired about the basis for the weighting ratio.

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27. The **Business Director (Development)** replied that:

- the 80:20 ratio was adopted in many engineering contracts. The HD considered that it was not desirable to award contracts purely on price and the past performance of a contractor should be given weight; and
- with the present arrangement, a message was sent to the contractors that they could not solely compete on price. Instead, they had to compete on performance as well and hence had to make greater effort to improve their performance. The system had worked well so far and the HD had no intention of changing the ratio.

28. The Committee were concerned about the short probationary period for contractors. Paragraphs 3.13 and 3.14 of the Audit Report revealed that, in November 1997, the HA had shortened the probationary period of contractors from 18 months to 12 months. Audit pointed out that by the time the 12-month probationary period expired, many parts of the building project were only in their early stages of construction and some of the works had not yet commenced. Hence, a 12-month probationary period appeared to be too short for determining whether the contractor was competent enough for promotion to the confirmed status. The Committee asked:

- whether, for those contractors which had taken up construction projects with other government departments, the HD would make reference to their track records with other departments and recognise their experience in those projects as the experience under the HA's system;
- what the background was to the HD's decision to shorten the probationary period from 18 months to 12 months; and
- whether the HD agreed with Audit's recommendation that it should consider extending the probationary period to the expected completion date of the relevant project, or to 24 months, in line with the practice of other government departments.

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29. The **Acting Director of Housing** and the **Business Director (Development)** explained that:

- if a contractor wanted to be included in the HA's lists of contractors, even the probation list, it would be vetted for financial standing, competency and track record. In other words, the HA would take into account the company's past performance in non-HA contracts. The 12-month probationary period referred to the contractor's performance exclusively on HA contracts;
- in November 1997, the HA had decided to reduce the probationary period of its contractors because, at that time, it was foreseen that there would be a lot of contracts to be awarded. The HA wanted to have more bidders rather than awarding the contracts to a small group of contractors. Also, from the perspective of risk management, the HA wanted to spread out the risk and did not wish to put too much work in the hands of a small number of contractors;
- despite the fast-track approach, the HA still paid due regard to the performance and quality of the contractors. Although the HA allowed the contractors to apply for confirmation after they had been admitted to the list of contractors on probation for 12 months, in the end they were confirmed only after 20 months; and
- as the housing production peak was over, there would be fewer contracts to be awarded than in 1997. Moreover, there were already enough competitors in the HA's lists of approved contractors. Hence, there was no longer a need to adopt the fast-track approach, and the probationary period could be extended to 24 months.

30. Paragraph 3.17(c) of the Audit Report revealed that the HA had recently established a premier league of contractors as the basis for developing strategic partnership. The Committee asked about the details of the mechanism, the nature of the strategic partnership and how the contractors were selected.

31. The **Acting Director of Housing** and the **Business Director (Development)** replied that:

- the purpose of setting up the premier league was to encourage the contractors to upgrade their quality of work. Under this mechanism, the contractors were encouraged to bid for more complicated contracts. The nature of such contracts would be different from ordinary contracts;

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- the relationship between the HA and the contractors was sometimes seen as adversarial. The contractors worked for the HA purely for money whereas the HA paid them for their work. The HA wanted to identify some contractors with which it could develop a partnership relationship and share a common goal, i.e. building quality public housing. Towards the end of 2000 and early 2001, the HD had identified some contractors from its approved lists which had the same objective as the HA, were of a bigger scale and had better management. These contractors were included in the premier league. In future, the HD could discuss with these contractors directly regarding more complicated projects. Nevertheless, they would still have to go through the tendering process to bid for the contracts; and
- in order to join the premier league, the contractors had to prove that they performed better than other contractors over a long period of time. The assessment mechanism was transparent and very objective. All eligible contractors could apply to join the league.

32. The Committee further enquired about the names of the contractors in the premier league and the track record of their performance. The **Director of Housing**, in his letters of 14 and 18 May 2001 in *Appendices 21 and 22* respectively, advised the Committee of the names of the six contractors in the premier league. It was also stated that:

- a contractor's performance was reviewed on a quarterly basis. During the review, a contractor would be given an adverse report on a project basis when certain aspect of its performance fell below a threshold of specified requirements, so as to alert the contractor to improve. One of the admission criteria for the premier league was that the maximum number of adverse reports received on the contractor during the past three years was less than 10% of the total number of reports on it during the same period; and
- five of the six contractors in the premier league had been given adverse reports on a project basis, but they had all met the above admission criterion.

33. The Committee were concerned that the establishment of the premier league by the HA might discourage potential bidders and inhibit fair competition among bidders in the tendering exercises for HA contracts. As such, the Committee asked:

- about the admission criteria for the premier league, including whether and how the admission criteria took into account the gravity and nature of the offence committed by a contractor;

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- the rationale for setting the percentage of adverse report permissible under the scheme at 10%;
- whether the HD had consulted other government departments on the contractors' performance before they were admitted to the premier league;
- whether contractors in the premier league would be considered more favourably than other bidders in the tendering exercises for HA contracts; and
- how the HD ensured that the scheme would not discourage potential bidders for HA contracts and that there would be fair and sufficient competition in the tendering exercises.

34. In his letter of 15 June 2001, in *Appendix 23*, the **Director of Housing** informed the Committee of the requirements of the premier league scheme. He also stated that:

- the scheme was to encourage and give incentive to HA contractors which adopted sound management systems and practices and were able to deliver good and reliable services. It aimed to induce contractors to upgrade their professional and technical competency and to invest in new technologies by recognising and rewarding their consistently good performance. The scheme was open to contractors which met the following requirements:
 - (a) basic entry criteria;
 - (b) satisfactory project performance history with the HA; and
 - (c) best practice requirements;
- in view of the objective of the scheme, it was considered not appropriate to take into account contractors' performance in non-HA works;
- the gravity and nature of the offence committed by a contractor were reflected by the disciplinary actions that were taken against it. It was in fact one of the considerations under the "satisfactory project performance history";
- for a typical new works project, 12 quarterly performance reports were compiled for a contractor during the 24-month construction period as well as the 12-month maintenance period. The 10% ceiling line was devised to reflect that no more than one "Adverse Report" on the contractor in a project was permissible. Similar to the limit for suspension from tendering, such one-time allowance was considered by the HA to be reasonable; and

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- besides being given unqualified opportunity to tender for special projects of a large scale or with great technical complexity, the contractors in the premier league were not treated more favourably than other bidders in an ordinary HA tendering exercise. It was the policy of the HA to keep the list of premier league contractors open-ended. Any contractors currently on the HA's list were encouraged to upgrade themselves to the premier league, should they meet the admission criteria.

Piling Works

35. According to paragraph 4.21 of the Audit Report, using pre-stressed precast concrete (PPC) piles at building sites where the geological conditions were known to be difficult required close supervision. In paragraph 4.23, the Director of Housing said that a series of initiatives for stepping up the monitoring of piling contracts had been implemented. The Committee asked about the details of the measures.

36. Paragraph 4.30(b) revealed that the HA had decided in June 2000 that PPC piles would only be used in very exceptional circumstances. Noting that the cost of PCC piles were substantially lower than that of other types of piles, the Committee asked whether the HD would still use PPC piles in sites where the geological conditions were suitable while at the same time enhancing the monitoring system.

37. The **Acting Director of Housing** and the **Business Director (Development)** said that:

- although the HA had decided that PPC piles would only be accepted for use in very exceptional circumstances, this did not mean that such piles could not be used any more. Rather, the HD had tightened the criteria for choosing PPC piles as an acceptable pile type. For instance, if PPC piles were to be used, detailed site investigation would have to be conducted and the piles would be provided with a stiffened driving shoe so that they could penetrate dense materials. All these measures were stipulated in the HD's manual; and
- the HD had set up a Foundation Advisory Panel consisting of chief structural engineers for vetting all proposals for using PPC piles. The Panel decided whether PPC piles could be used for particular projects.

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38. The Committee noted from paragraph 4.19 of the Audit Report that in the case of the foundation works in Tin Shui Wai Area 102 Phase 3, there was serious delay in the installation and testing of the preliminary piles. The installation of the preliminary piles only commenced in November 1997, after 27 % of the overall foundation works had been completed. Moreover, the pile testing work was only completed in January 1998, after 53% of the overall foundation works had already been completed.

39. Audit commented in paragraph 4.20 that this case illustrated that there were control weaknesses in the piling process. The contractor had failed to keep pace with the master programme on the installation and testing of the preliminary piles. Furthermore, the HD had not taken any effective action to ensure that the works for the preliminary piles were completed on time. In view of Audit's observations, the Committee asked:

- why the HD allowed the contractor to complete the pile testing work after half of the overall foundation works had already been completed; and
- whether the HD agreed that there was a lack of monitoring on its part in this case.

40. The **Business Director (Development)** explained that:

- this case concerned a matter of work procedure. It was not stated in the contract that preliminary piles must be driven in before the working pilings were installed. The contractor in question had proceeded with the two stages in parallel, i.e. the preliminary piles and the working piles were installed at the same time. However, the working piles were only partly installed and had not been driven to final set. The installed working piles would only be driven to final set after the preliminary piles had been tested to satisfaction and accepted by the HD; and
- such a procedure enabled the contractor to speed up the works. As long as the working piles were not driven to final set before confirmation of the test results of the preliminary piles, the contractor was allowed to proceed with this procedure.

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41. In the light of the reply that the HA's contractor was allowed to install working piles before the test results of the preliminary piles were known, the Committee asked:

- in the event that the negative test results were only known after the foundation works had been substantially completed, and hence the contractor would have to revise the design parameters, whether there would be a waste of time and resources;
- whether there was a possibility of the contractors cutting corners; and
- whether one of the conditions for using PPC piles in future was that the test results of preliminary piles must be known before commencement of the installation of working piles.

42. The **Business Director (Development)** responded that:

- the risk of adopting such a work procedure lay with the contractor, not the HD. As long as the working pilings had not been driven to final set, the HD would not regard the work as having been completed. If subsequently there were problems with the preliminary piles, the work that had been completed would have to be rectified. The contractor was aware of the risk and would adopt the parallel procedure only when it felt that the piles had been driven in very smoothly; and
- when working piles were to be driven to final set, there must be HD staff at site to supervise the work. There was thus no question of the contractor cutting corners in this step; and if the HD allowed PPC piles to be used, the geological conditions of the site must be suitable for this pile type. As such, the HD would still consider allowing the contractor to proceed with the installation of preliminary piles and working piles in parallel.

Monitoring of the performance of contractors

43. According to paragraphs 5.12 to 5.17 of the Audit Report, the HD was currently using a manual system to record site inspection results. The system involved significant amount of administrative and paper work. In May 1999, the HA agreed to develop a new computerised system for site inspections. However, up to the end of December 2000, the HD had not drawn up any timetable for the development and implementation of the new system. The Committee asked about the current progress.

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44. The **Acting Director of Housing** replied that the HD agreed with Audit's recommendation in this regard. Actually, it was stated in the HA's consultation paper on quality housing that the HD wanted to reduce the amount of paper work and form-filling. However, it took time to develop the computerised system. The HD was actively developing the system and was working closely with the contractors with a view to implementing it as soon as possible.

45. The Committee were concerned about the delay in the handing over of new flats due to the HD's current practice of requiring two final flat-to-flat inspections by two separate teams. According to paragraphs 5.21 to 5.25 of the Audit Report, the HD's Development and Construction Branch carried out the first final flat-to-flat inspection while the Management Branch conducted the second inspection. Audit found that such an arrangement delayed the occupation of the new flats by 1.5 months on average. The Committee asked whether it was possible for the staff of the two Branches to conduct a joint final flat-to-flat inspection at the same time so as to avoid delay.

46. The **Acting Director of Housing** responded that:

- the HD agreed that the practice of having two separate teams of staff conducting two separate final flat-to-flat inspections should be reviewed. It would try to rationalise the arrangements; and
- it was stated in Table 3 of the Audit Report that the delay due to the second inspection was 45 days on average. In fact, during that period, the contractors were required to rectify the defects identified in the first inspection. Therefore, even after the process had been streamlined, it might not be possible to reduce the time gap to less than 45 days. In any case, the HD required the contractors to rectify all the defects before the flats were handed over to tenants or owners.

47. The **Chairman, HA** said that he fully agreed with Audit's recommendation that the two inspections should be combined into one. If different teams were responsible for the inspection, there might be conflict of opinions and the situation would become complicated. Certainly, if there were defects and outstanding works in a flat, all these would have to be rectified and completed by the contractor. A re-inspection should then follow.

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48. The Committee considered that combining the two final flat-to flat inspections into one would not necessarily eliminate the delay in the handing over of new flats because the delay was sometimes caused by the work procedure. They enquired whether the HA had set a target time gap between the date of completion of the flat and the date of completion of the second inspection.

49. The **Chairman, HA** and the **Acting Director of Housing** responded that:

- although the final flat-to-flat inspection was very important, the supervision and inspection could be carried out in the early stage of the works process and from time to time. If there were regular inspections, there would be less problems during the final inspection; and
- it would be reasonable for the final inspection to be conducted two or three days after the date of completion, regardless of whether the final inspection was a joint inspection by two teams at the same time or was carried out by two separate teams. While the HD aimed at completing the inspection as soon as possible after completion of the flat, the actual time gap would depend on the performance of the contractor. Even if a joint inspection by two teams of staff was to be conducted in future, if defects were identified during the inspection, a period of time must be allowed for the contractor to rectify the defects. Then a re-inspection would have to be carried out. The HD would not take over the flats until all the defects had been rectified.

50. The Committee understood from paragraph 5.27(b) of the Audit Report that the HD had decided to adopt more stringent inspection procedures even though they might mean delay in the occupation of the flats. The Committee enquired whether the inspection procedures would delay the occupation of the flats.

51. The **Acting Director of Housing** and the **Business Director (Development)** clarified that:

- the stringent inspection procedures would not cause delay. The HD had constructed benchmark sample flats to demonstrate to the contractors the level of workmanship required so that they need not speculate on the HD's standard. As the contractors understood the HD's requirement in advance, they would try to meet the standard during the works process. As such, the inspection process would be facilitated; and

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- to ensure customer satisfaction, the HD would not relax its standard even if there would be delay in the occupation of the flats due to the stringent inspection procedures.

Different roles of the HA

52. Paragraphs 6.2 to 6.7 of the Audit Report revealed that the HA had been playing different roles in the development of public housing, i.e. as developer, project manager and supervisor professional, and regulatory agency. In April 2000, the HA had agreed to implement the initiative of putting its building projects within the purview of the Buildings Ordinance. However, the HA had not established any target implementation date for this initiative.

53. The Committee shared the concern that there was potential conflict of interests as the HA had different roles to play in public housing development, and considered that the initiative of putting the HA's projects within the purview of the Buildings Ordinance should be implemented without delay. The Committee therefore asked:

- whether the HA had allocated any resources to take the matter forward and whether an implementation timetable had been drawn up; and
- having regard to the manpower implications for the BD if it was to supervise the HA's projects, whether the BD had sufficient resources to absorb the work.

54. The **Chairman, HA** and the **Acting Director of Housing** informed the Committee that:

- the HD was working closely with the BD on the initiative. However, a specific timetable had not been drawn up because the matter was complex, involving consideration of different aspects such as legislation and resources; and
- the HD had already taken preparatory steps to implement the initiative. In the interim period, the HD had set up an Independent Checking Unit (ICU) to perform formal structural and building plans vetting functions. The ICU, established in November 2000, was directly responsible to the Director of Housing and operated in a similar manner as the BD. The ICU would perform a third party checking role at all key stages of projects, similar to the functions performed by the BD under the Buildings Ordinance, while legal and resource implications etc. were being sorted out.

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55. The **Director of Buildings** said that:

- the Government was still studying the matter and had not made a decision yet. Actually, the issue was very complex and the difficulties involved should not be under-estimated. The BD had seconded some experienced officers to the ICU in the HD to assist in adopting the BD's monitoring system;
- although a final decision had not yet been made, the BD had been working on it together with the HD. The BD had already carried out preparatory work, such as studying the mechanism to be set up, the resources involved and the procedure for taking over the work from the HA, in the event that the Government decided that the proposal should be proceeded with; and
- apart from the BD and the HD, other policy bureaux and departments were also involved. For example, the Housing Bureau would be responsible for making legislative amendment and financial arrangement, and discussing with the Government about resource allocation between the two departments.

56. The Committee further asked whether, after the HA's projects were put within the purview of the Buildings Ordinance, the problem of potential conflict of interests arising from the HA's different roles could be solved. The **Director of Buildings** responded that:

- as the regulatory body, the BD's role was similar to the role of an auditor. The BD performed checking functions in accordance with the Buildings Ordinance. It monitored the planning, design and construction and associated works during each stage of the construction process and checked if the provisions of the legislation had been complied with. If negligence was identified, the BD would take prosecution action and the responsible party would be criminally liable. If a particular project was not under the control of the Buildings Ordinance, the responsible party would not be subject to statutory sanctions;
- if the HA's building projects were brought under the control of the Buildings Ordinance, there would be a third party who independently monitored the projects. The parties who did not comply with the legislation, whether they were works staff, professionals or contractors, would be subject to statutory sanctions under the Buildings Ordinance. This could achieve a significant deterrent effect; and

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- under the BD's current system, there was a vetting strategy at each stage of the construction process with a view to increasing the burden on those concerned to comply with the law. For instance, currently the BD required a 100% inspection of the piles in foundation projects. However, although a stringent system was in place, there would still be people who were willing to take the risk. By adopting stringent requirements, the BD aimed to maximise the use of its resources to ensure the building quality.

57. In the light of the Director of Buildings' reply, the Committee considered that the ICU set up by the HD could not take the place of the BD in performing third-party checking functions. They therefore asked who was responsible for making a decision regarding the proposal to put the HA projects under the control of the Buildings Ordinance. Responding to the Committee's question, the **Secretary for Planning and Lands** advised that the matter was being considered by the Committee on the Review of the Institutional Framework for Public Housing (CRIFPH) chaired by the Chief Secretary for Administration.

58. Upon the Committee's enquiry, the **Administrative Assistant to the Chief Secretary for Administration** informed the Committee in her letter of 16 May 2001, in *Appendix 24*, that:

- the CRIFPH had reached some initial conclusions on the HA's initiative to place all its buildings within the purview of the Buildings Ordinance; and
- the CRIFPH would further consult the HA, the Hong Kong Housing Society, the Legislative Council Panel on Housing and other concerned organisations before it finalised its recommendations.

Quality housing reform

59. According to paragraphs 7.2 to 7.5 of the Audit Report, in April 2000, the HA endorsed a two-phase implementation plan containing 50 improvement initiatives to enhance the building quality. However, the HD had not set implementation dates for 23 of these 50 initiatives. The Committee enquired whether action plans for the implementation of the remaining initiatives had been prepared.

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60. In his letter of 18 May 2001, in *Appendix 22*, the **Director of Housing** informed the Committee of the timeframe for implementing the remaining quality housing initiatives. He also stated that:

- the HD had been making good progress in implementing the quality housing initiatives. As at 31 March 2001, 19 of the initiatives had been implemented and another 18 had already been partially implemented or launched as pilot schemes. The HD would review the effectiveness of the pilot schemes in 2001-2002. The remaining 13 initiatives would be implemented progressively according to the timeframe set out in *Appendix 22*; and
- the HD's Progress Monitoring Committee would monitor the progress of implementation and review the effectiveness of the initiatives on a regular basis. Quarterly progress reports would also be submitted to the HA's Building Committee.

61. **Conclusions and recommendations** The Committee:

The Housing Authority's (HA's) standard designs

- acknowledge the Chairman, HA's statement that the HA would use more non-standard designs by adopting a site-specific layout approach and review the standard designs in order that there would be further improvement;
- note that:
 - (a) the joint Practice Note issued in February 2001 will provide further flexibility for the HA to revise the existing standard designs of public housing; and
 - (b) the Housing Department (HD) has, where appropriate, adopted some design features of private-sector developments, which may improve the efficiency ratio;
- recommend that the Director of Housing, in reviewing the standard designs, should take into account the HA's core value of providing quality housing, the impact of innovative façade designs and varied building heights on the environment of the whole district, the need to provide sufficient public areas to the residents, and the efficiency ratio to be achieved;

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Tendering process

- express grave concern and find it unacceptable that the progress of extending the Preferential Tender Award System (PTAS) for building services and piling contracts has been slow;
- acknowledge that the Director of Housing has:
 - (a) undertaken to extend the application of the PTAS to the building services and piling contracts after the performance scoring systems for such contracts are implemented in the third quarter and fourth quarter of 2001 respectively; and
 - (b) agreed to review the probationary period for contractors;
- express serious concern that the establishment of a premier league of contractors by the HA may discourage potential bidders and inhibit fair competition among bidders in the tendering exercises for HA contracts;
- urge the Director of Housing to review the premier league scheme to ensure that there is fair and sufficient competition in the tendering exercises for HA contracts, and to consult the Legislative Council in the course of the review;

Piling works

- note that the HA has been implementing a series of initiatives to enhance the mechanism for monitoring piling contracts;
- recommend that the Director of Housing should:
 - (a) require the site staff concerned to properly document and notify senior management of significant problems encountered; and
 - (b) ensure that preliminary piles are installed and tested at the initial phase of piling contracts;
- express concern that the HD's manual for providing guidance to the HD's staff does not provide specific guidelines to deal with different types of piles;
- recommend that the Director of Housing should critically review the HD's manual to see if the existing guidelines are sufficient and specific enough for planning and supervising the piling process of the HA's projects;

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Monitoring the performance of contractors

- express grave concern and find it unacceptable that the implementation of the Performance Assessment Scoring System (PASS) 2000 had been delayed by 18 months;
- urge the Director of Housing to take action to ensure that the implementation of the PASS 2000 will not be further delayed;
- express serious dismay that the HA was not informed of the delay until some four months after the original target implementation date;
- recommend that the Director of Housing should inform the HA on a timely basis of any delay that may affect the implementation of major management control systems so as to enable the HA to provide necessary policy input and to make informed decision;
- express serious dismay that the HD's current practice of requiring two final flat-to-flat inspections by separate teams delays the handover of new flats to occupants;
- note that the Chairman, HA has agreed to streamline the final flat-to-flat inspection process;

Different roles of the HA

- express concern that the HA has different roles to play in public housing development which may result in conflict of interests;
- note that the Committee on the Review of the Institutional Framework for Public Housing (CRIFPH) chaired by the Chief Secretary for Administration will further consult the HA, the Hong Kong Housing Society, the Legislative Council Panel on Housing, and other concerned organisations before finalising its recommendations on the HA's initiative to put its building projects within the purview of the Buildings Ordinance (BO);
- urge the Chief Secretary for Administration to expeditiously finalise and announce the CRIFPH's recommendations on the initiative to put the HA's building projects within the purview of the BO;

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Quality housing reform

- note that the HD has set target implementation dates for the remaining quality housing reform initiatives, and that the HD's Progress Monitoring Committee will monitor the progress of implementation and review the effectiveness of the initiatives on a regular basis. The HD will also propose changes to the HA's mission statement accordingly;
- recommend that the Director of Housing should take action to promote the provision of quality housing as a core value, so as to ensure that it is recognised and accepted by all staff concerned; and
- wish to be kept informed of:
 - (a) the progress made regarding the application of the PTAS to building services and piling contracts;
 - (b) the progress made in reviewing the probationary period for contractors;
 - (c) the review of premier league scheme;
 - (d) the progress made in implementing the HA initiatives for improving the monitoring of piling contracts;
 - (e) the progress made in streamlining the final flat-to-flat inspection process;
 - (f) the CRIFPH's recommendations on the initiative to put the HA's building projects within the purview of the BO; and
 - (g) the progress made in implementing the quality housing reform initiatives.

**SIGNATURES OF THE CHAIRMAN, DEPUTY CHAIRMAN AND
MEMBERS OF THE COMMITTEE**

Eric LI Ka-cheung
(Chairman)

Emily LAU Wai-hing
(Deputy Chairman)

David CHU Yu-lin

Fred LI Wah-ming

LAU Kong-wah

Abraham SHEK Lai-him

Tommy CHEUNG Yu-yan

20 June 2001

**CHAPTERS IN THE DIRECTOR OF AUDIT'S REPORT NO. 36
DEALT WITH IN THE PUBLIC ACCOUNTS COMMITTEE'S REPORT**

**Director of
Audit's Report
No. 36**

**P.A.C. Report
No. 36**

<u>Chapter</u>	<u>Subject</u>	<u>Chapter</u>
1	Follow-up review on control of utility openings	1
2	Provision of slaughtering facilities for supply fresh meat	2
5	Provision of staff for Departmental Accounting Units	3
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9	Government's efforts to promote e-business in Hong Kong	5
10	Management of public housing construction	6

**RULES OF PROCEDURE OF
THE LEGISLATIVE COUNCIL OF
THE HONG KONG SPECIAL ADMINISTRATIVE REGION**

72. Public Accounts Committee

(1) There shall be a standing committee, to be called the Public Accounts Committee, to consider reports of the Director of Audit –

- (a) on the accounts of the Government;
- (b) on such other accounts required to be laid before the Council as the committee may think fit; and
- (c) on any matter incidental to the performance of his duties or the exercise of his powers as the committee may think fit.

(2) The committee shall also consider any report of the Director of Audit laid on the Table of the Council which deals with examinations (value for money audit) carried out by the Director relating to the economy, efficiency and effectiveness of any Government department or public body or any organization to which his functions as Director of Audit extend by virtue of any Ordinance or which receives public moneys by way of subvention.

(3) The committee shall consist of a chairman, deputy chairman and 5 members who shall be Members appointed by the President in accordance with an election procedure determined by the House Committee. In the event of the temporary absence of the chairman and deputy chairman, the committee may elect a chairman to act during such absence. The chairman and 2 other members shall constitute a quorum.

(4) A report mentioned in subrules (1) and (2) shall be deemed to have been referred by the Council to the committee when it is laid on the Table of the Council.

(5) Unless the chairman otherwise orders, members of the press and of the public shall be admitted as spectators at meetings of the committee attended by any person invited by the committee under subrule (8).

(6) The committee shall meet at the time and the place determined by the chairman. Written notice of every meeting shall be given to the members and to any person invited to attend a meeting at least 5 clear days before the day of the meeting but shorter notice may be given in any case where the chairman so directs.

(7) All matters before the committee shall be decided by a majority of the members voting. Neither the chairman nor any other member presiding shall vote, unless the votes of the other members are equally divided, in which case he shall have a casting vote.

(8) The chairman or the committee may invite any public officer, or, in the case of a report on the accounts of or relating to a non-government body or organization, any member or employee of that body or organization, to give information or any explanation or to produce any records or documents which the committee may require in the performance of its duties; and the committee may also invite any other person to assist the committee in relation to any such information, explanation, records or documents.

(9) The committee shall make their report upon the report of the Director of Audit on the accounts of the Government within 3 months (or such longer period as may be determined under section 12 of the Audit Ordinance (Cap. 122)) of the date on which the Director's report is laid on the Table of the Council.

(10) The committee shall make their report upon the report of the Director of Audit mentioned in subrule (2) within 3 months (or such longer period as may be determined by the Council) of the date on which the Director's report is laid on the Table of the Council.

(11) Subject to these Rules of Procedure, the practice and procedure of the committee shall be determined by the committee.

**Paper presented to the Provisional Legislative Council
by the Chairman of the Public Accounts Committee
at the meeting on 11 February 1998 on
Scope of Government Audit in the
Hong Kong Special Administrative Region -
'Value for Money Audits'**

SCOPE OF WORK

1. The Director of Audit may carry out examinations into the economy, efficiency and effectiveness with which any bureau, department, agency, other public body, public office, or audited organisation has discharged its functions.

2. The term "audited organisation" shall include -
 - (i) any person, body corporate or other body whose accounts the Director of Audit is empowered under any Ordinance to audit;
 - (ii) any organisation which receives more than half its income from public moneys (this should not preclude the Director from carrying out similar examinations in any organisation which receives less than half its income from public moneys by virtue of an agreement made as a condition of subvention); and
 - (iii) any organisation the accounts and records of which the Director is authorised in writing by the Chief Executive to audit in the public interest under section 15 of the Audit Ordinance (Cap. 122).

3. This definition of scope of work shall not be construed as entitling the Director of Audit to question the merits of the policy objectives of any bureau, department, agency, other public body, public office, or audited organisation in respect of which an examination is being carried out or, subject to the following Guidelines, the methods by which such policy objectives have been sought, but he may question the economy, efficiency and effectiveness of the means used to achieve them.

GUIDELINES

4. The Director of Audit should have great freedom in presenting his reports to the Legislative Council. He may draw attention to any circumstance which comes to his knowledge in the course of audit, and point out its financial implications. Subject to these Guidelines, he will not comment on policy decisions of the Executive Council and the Legislative Council, save from the point of view of their effect on the public purse.

5. In the event that the Director of Audit, during the course of carrying out an examination into the implementation of policy objectives, reasonably believes that at the time policy objectives were set and decisions made there may have been a lack of sufficient, relevant and reliable financial and other data available upon which to set such policy objectives or to make such decisions, and that critical underlying assumptions may not have been made explicit, he may carry out an investigation as to whether that belief is well founded. If it appears to be so, he should bring the matter to the attention of the Legislative Council with a view to further inquiry by the Public Accounts Committee. As such an investigation may involve consideration of the methods by which policy objectives have been sought, the Director should, in his report to the Legislative Council on the matter in question, not make any judgement on the issue, but rather present facts upon which the Public Accounts Committee may make inquiry.

6. The Director of Audit may also -

- (i) consider as to whether policy objectives have been determined, and policy decisions taken, with appropriate authority;
- (ii) consider whether there are satisfactory arrangements for considering alternative options in the implementation of policy, including the identification, selection and evaluation of such options;
- (iii) consider as to whether established policy aims and objectives have been clearly set out; whether subsequent decisions on the implementation of policy are consistent with the approved aims and objectives, and have been taken with proper authority at the appropriate level; and whether the resultant instructions to staff accord with the approved policy aims and decisions and are clearly understood by those concerned;

- (iv) consider as to whether there is conflict or potential conflict between different policy aims or objectives, or between the means chosen to implement them;
- (v) consider how far, and how effectively, policy aims and objectives have been translated into operational targets and measures of performance and whether the costs of alternative levels of service and other relevant factors have been considered, and are reviewed as costs change; and
- (vi) be entitled to exercise the powers given to him under section 9 of the Audit Ordinance (Cap. 122).

PROCEDURES

7. The Director of Audit shall report his findings on value for money audits in the Legislative Council twice each year. The first report shall be submitted to the President of the Legislative Council within seven months of the end of the financial year, or such longer period as the Chief Executive may determine. Within one month, or such longer period as the President may determine, copies shall be laid before the Legislative Council. The second report shall be submitted to the President of the Legislative Council by the 7th of April each year, or such date as the Chief Executive may determine. By the 30th April, or such date as the President may determine, copies shall be laid before the Legislative Council.

8. The Director's report shall be referred to the Public Accounts Committee for consideration when it is laid on the table of the Legislative Council. The Public Accounts Committee shall follow the rules governing the procedures of the Legislative Council in considering the Director's reports.

9. A Government minute commenting on the action Government proposes to take in respect of the Public Accounts Committee's report shall be laid on the table of the Legislative Council within three months of the laying of the report of the Committee to which it relates.

10. In this paper, reference to the Legislative Council shall, during the existence of the Provisional Legislative Council, be construed as the Provisional Legislative Council.

**Witnesses who appeared before the Committee
(in order of appearance)**

Mrs Lily YAM KWAN Pui-ying, JP	Secretary for the Environment and Food
Mrs Ingrid YEUNG	Principal Assistant Secretary (Environment and Food)
Miss Sarah WU, JP	Acting Director of Food and Environmental Hygiene
Ms Rhonda LO	Assistant Director (Operations) Food and Environmental Hygiene Department
Mr KWAN Pak-lam, JP	Acting Director of Architectural Services
Mr LEE Yuk-shing	Project Manager Architectural Services Department
Mr Robert LAW, JP	Director of Environmental Protection
Dr Michael CHIU	Assistant Director (Local Control) Environmental Protection Department
Mrs Carrie YAU, JP	Secretary for Information Technology and Broadcasting
Mr Alan SIU	Deputy Secretary for Information Technology and Broadcasting
Ms Joyce TAM	Principal Assistant Secretary (Information Technology and Broadcasting)
Mr CHAU Tak-hay	Secretary for Commerce and Industry
Mr Philip CHAN	Principal Assistant Secretary (Commerce and Industry)
Mr NG Hon-wah	Principal Assistant Secretary (Home Affairs)
Mr LUK Ping-chuen, JP	Postmaster General
Mr Allan CHIANG	Deputy Postmaster General

Mr Gregory LEUNG Wing-lup, JP	Director of Government Supplies
Mr CHENG Yan-chee	Acting Director of Information Technology Services
Dr CHENG Hon-kwan, GBS, JP	Chairman, Hong Kong Housing Authority
Mr Marco WU, JP	Acting Director of Housing
Mr TONG Wing-shing	Business Director (Development) Housing Department
Mr Gordon SIU, JP	Secretary for Planning and Lands
Mr LEUNG Chin-man, JP	Director of Buildings
Mr CHEUNG Kwok-ming	Assistant Director (New Buildings) Buildings Department
Miss Denise YUE Chung-yee, JP	Secretary for the Treasury
Mr SHUM Man-to, JP	Director of Accounting Services
Mr Alex AU, JP	Acting Director-General of Civil Aviation
Mr CHAN Fung-ming	Acting Chief Treasury Accountant Food and Environmental Hygiene Department
Mr Paul LEUNG, JP	Director of Leisure and Cultural Services
Ms Lolly CHIU	Deputy Director (Administration) Leisure and Cultural Services Department
Mrs Maureen CHAN LEUNG Mong-lin	Executive Director, Hong Kong Sports Development Board
Mrs Katherine CHENG	Head (Operations), Hong Kong Sports Development Board
Mr Godwin FUNG	Head (Finance), Hong Kong Sports Development Board
Mr LAM Woon-kwong, GBS, JP	Secretary for Home Affairs
Mr Jonathan McKinley	Principal Assistant Secretary (Sports Policy Review), Home Affairs Bureau

Mr R H Lloyd, JP

Acting Director of Highways

Mr WONG Chee-keung

Deputy Director of Highways

Mr LEE Shing-see, JP

Secretary for Works

Mr Michael Byrne

Principal Assistant Secretary (Works)

**Introductory Remarks by
Chairman of the Public Accounts Committee,
the Hon Eric LI Ka-cheung, JP,
at the First Public Hearing of the Committee
on Monday, 7 May 2001**

Good afternoon, ladies and gentlemen. Welcome to the Public Accounts Committee's public hearing relating to the Director of Audit's Report on the results of value for money audits completed between October 2000 and February 2001, which we was tabled in the Legislative Council on 25 April 2001.

The Public Accounts Committee is a standing committee of the Legislative Council. It plays the role of a watchdog over public expenditure through consideration of the reports of the Director of Audit laid before the Council on the Government's accounts and the results of value for money audits of the Government and of organisations which receive funding from the Government. The purposes of the Committee's considering the Director's reports are to receive evidence relevant to the reports in order to ensure that the facts contained in the Director's reports are accurate, and to draw conclusions and make recommendations in a constructive spirit and forward-looking manner. I also wish to stress that the objective of the whole exercise is such that the lessons learned from past experience and our comments on the performance of the public officers concerned will enable the Government to improve its control over the expenditure of public funds, with due regard to economy, efficiency and effectiveness.

The consideration of the Director's reports follows an established process of public hearings where necessary, internal deliberations and publication of the Committee's report. The Committee has an established procedure for ensuring that the parties concerned have a reasonable opportunity to be heard. After the Committee is satisfied that it has ascertained the relevant facts, it will proceed to form its views on those facts, followed by a process of formulating its conclusions and recommendations to be included in its report. In accordance with Rule 72 of the Rules of Procedure of the Legislative Council, the Committee is required to make its report on the Director's report to the Legislative Council within three months of the date at which the Director's report is laid on the Table of the Council.

Following a preliminary study of the Director of Audit's Report No. 36, the Committee has decided, in respect of six chapters in the Report, to invite the relevant public officers and parties concerned to appear before the Committee and answer our questions. We have, apart from this afternoon's hearings, also set aside the afternoon of 14 May for the public hearings. After we have studied the issues and taken the necessary evidence, we will produce our conclusions and recommendations which will reflect the independent and impartial opinions of the

Committee. These recommendations will be made public when we report to the Legislative Council. Before then, we will not, as a committee or individually, be making any public comment on our conclusions.

I now declare the Committee to be in formal session.