

Legislative Council Panel on Housing

Sub-committee to Study the Letting and Rent Policies of Non-Domestic Premises of the Housing Authority and the Housing Society

Housing Authority's Letting and Rent Policies on Non-domestic Properties

1 Market Share and Shop Tenancy Categories

- 1.1 The market share of retail space in Hong Kong held by the private sector and the Housing Authority (HA), together with a broad-brush breakdown of HA's retail space by trade, is shown at **Annex A**.

2 Leasing by Tender or Negotiation

- 2.1 Tender is the most transparent and fair method of letting. However, it is not used very frequently in the private sector because it lacks the flexibility for the variation of terms even in the mutual interest of landlord and tenant, and because many popular chains are unwilling to participate in tender exercises. The HA uses a balance of negotiation and tender (about 30% negotiation and 70% tender) to achieve a reasonable mixture of tenant type (i.e. chain stores and single-outlet retailers) while continuing to give ample opportunities for small businesses to compete and develop.

- 2.2 Any proposal to let by negotiation must comply with the Guidelines set out in **Annex B**. There is no fixed rule as to which premises will be let by negotiation and which by tender; flexibility is allowed to meet the individual circumstances of the case. The Guidelines, however, allow particularly for the use of negotiation –

- (i) in the letting of a major premises such as a department stores or restaurants which will 'anchor' a shopping centre and where an emphasis on quality and continuity is particularly important; or
- (ii) where premises have failed to attract bids by tender; or
- (iii) where a centre lacks popular appeal because of a lack of recognisable brand names; or

- (iv) to facilitate expansion by tenants of medium size with a high standard of performance; or
- (v) to facilitate new retail operation by a company with demonstrated performance in non-retail fields.

2.3 As a further safeguard, all major lettings by negotiation require the endorsement of a Panel drawn from the HA's Commercial Properties Committee to oversee such lettings.

3 Restricted Tender

3.1 It is the practice of the HA to make an Ex-Gratia Allowance to tenants of the HA displaced through redevelopment of HA estates. For some years tenants have also been offered the restricted tender opportunities or a lump-sum payment in lieu. In late 1999, the HA noted that in the proceeding two years all but 16 tenants had opted for the lump sum, and decided that tenants affected by later exercises should continue to have the choice, but restricted tender would be limited to premises in existing HA markets. In the light of views expressed by the LegCo Panel on Housing, however, the HA decided in November 2001 that shops previously unsuccessfully offered twice for open tender could be opened to restricted tender by affected tenants upon request.

3.2 The question has been raised as to why a proportion of space in new shopping centres is not reserved for tenants displaced through HA redevelopment exercises. The rationale for HA policy is that tenants receive a cash allowance sufficient to secure premises and to re-establish their business if they so wish in the private sector or in HA premises offered by open tender. Tender exercises open to all potential tenants are the best way to attract the most efficient operators who will maximise the use of the premises to the benefit of residents.

3.3 A total of 15 premises were licensed by restricted tender from January 2000 to February 2002.

4. Planning of Commercial Facilities

4.1 Retail services can be regarded as supplementary to the HA core business of provision and management of public housing and are

provided where private sector facilities are not conveniently available. The HA develops and manages commercial property on commercial principles.

- 4.2 The size of retail provision for any particular estate is derived using an expenditure-based methodology, which takes into account the size of the catchment area, socio-economic characteristics of the catchment population, competing facilities in the vicinity and transport facilities.
- 4.3 Shopping facilities are planned and constructed as an integral part of an estate. The development process comprising planning, design and construction typically takes five to six years. The precise period depends upon the complexity of the project, site conditions and so on.

5 Determination of Trade Mix

- 5.1 HA shopping centres are designed to meet the daily needs of local residents for retail goods and services. It is HA's practice to exercise control over the trade mix to ensure that as far as possible the range of goods and services available corresponds to local needs. Changes in market trends and consumer tastes are monitored with a view to adjusting the trade mix as appropriate.
- 5.2 HA centres vary in size according to the local catchment. For the smallest centres, the range of trades is necessarily limited and focused on provision of daily necessities. For larger centres, the range of trades is wider, but daily necessities still form the major part.
- 5.3 A preliminary breakdown of trade mix is made at the design stage to ensure that unit sizes will be appropriate to requirements, and that suitable provision can be made for trades with special building or building service requirements such as banks or restaurants. At this stage, markets, supermarkets/superstores, restaurants, bakeries and clinics will be identified and a broad list made of other trades. This mix is monitored during construction and will be reviewed when the centre is approaching completion prior to the commencement of marketing activities.

6 Introduction of Large Chain Stores

- 6.1 HA provides commercial facilities to fulfil residents' needs for goods and services. Policies and practice are aimed at providing as far as possible the quality of services which residents prefer. The HA does not drive changes in market trends and tastes but tries to adapt to such changes as they occur. Judging by their patronage, large chain stores such as superstores are clearly welcomed by the public at large, and surveys have demonstrated that public estate residents are no different in this respect. If the HA fails to respond to changes in demand, the HA will fail in its objective of serving its tenants, lose customers to private sector shopping centres, to the detriment of both residents and commercial tenants.
- 6.2 As far as existing estates are concerned, however, the HA has considerable investment in both existing structures and in long-term relationships with tenants and has taken steps to ensure that changes are made carefully with regard to the legitimate expectations of stakeholders. In existing estates where there are traditional markets in operation, therefore, the HA has not introduced new superstores. There has been pressure for supermarkets in such estates to develop 'service-style' fresh food provision; this is permitted only for supermarkets exceeding 800m², and subject to a limitation in 20% of the total area for fresh food. Supermarkets are required to apply for this concession for HA's consideration.
- 6.3 At the same time, the HA is taking steps to enhance the environment in markets to assist stall operators. The HA in 2001 endorsed a three-year programme with a view to retrofitting air-conditioning to some 42 markets, and for action on a further 23 markets where vacancy rates are particularly high. HA rents are also adjusted in line with market movements to assist stallholders.

7 Letting of Vacant Premises for Superstores

- 7.1 There has been no such case in the past five years that vacant premises in HA estates, surrendered by market stall operators, were leased to superstores.

8 Transfer of Leases

- 8.1 HA commercial lettings are not transferable and assignment is prohibited except under special circumstances. If unauthorised assignment is detected, action is taken to recover the tenancy. This assists the HA to promote healthy competition and maintain an orderly trading environment. In small centres with a limited range of trades, there may be only one tenant for some trades. Where there is more than one operator for a designated trade, however, it is HA's policy that the second outlet should not be let to the tenant of the first, or an associate of that company, unless no other operator comes forward.

9 Basis of Rental Valuation

- 9.1 Market rents for HA premises are determined by professional estate surveyors in Housing Department (HD) taking into account all evidence available of lettings of HA's commercial properties by tender or negotiation, and of private sector lettings. Each premises has its own unique characteristics in terms of size, shape, location, permitted trade and potential or current pedestrian flow. It is the skill of surveyors to analyse the evidence available and to apply the values so derived to comparable premises for assessment, making due allowance for differences in relevant factors. Surveyors' assessments are carefully checked; in the event of any request for review the assessment will be examined at HD's directorate level and may be adjusted if appropriate.

10 Premises with Reduced Rent or Left Vacant because of High Rentals on Renewals

- 10.1 The HA keeps no record of the number of cases where the premises had to be leased at a reduced rent or left vacant after failing to reach tenancy renewal agreement with the previous tenants because of high rentals. However, records for the past three years indicate that an average of only 14 tenants quit on tenancy renewals each year. Many of these tenants are known to be leaving for reasons such as retirement, emigration or ill-health.

11 Rents of Medical/Dental Clinics and other Shops requiring Continuity of Services

- 11.1 It is HA's policy that any tenant who has complied with the terms of his tenancy be invited to apply for renewal for a new three-year term at market rent. This policy allows for continuity of services; at the same time it provides for market rent to be reviewed to current market levels. In assessing market rents HD surveyors are careful to ensure assessments are realistic : while tender evidence is useful, surveyors recognise that some tenders are at levels of rent which cannot be supported from the expected level of business, and that tenders for new estates may not be a good indication of value for the same trade in older estates. Nonetheless, if the general run of evidence indicates that some premises could be tendered for a particular trade at a rent well above the rent passing, lack of action to bring the rent up to a more realistic level would imply a subsidy to the operator, and would be out of line with HA policy.
- 11.2 In the case of estate clinics for doctors and dentists, the use of open tender is fairer than the previous ballot system as it reflects market values to individual operators more accurately. The business potential of a clinic is affected not only by its location and size, but also the business prospect or competitive advantage of a doctor's or dentist's skills and reputation. The open tender results since the replacement of the ballot system by tender system in early 2000 shows that in many cases current rents are on the low side, and that doctors and dentists are willing to pay more when premises are offered on the open market. As such, it is possible the rents are adjusted upward upon renewal of contracts, after HA has taken into account other factors such as relevant local circumstances and all evidence of any comparable private sector lettings. In any case, the present rentals for clinics should be affordable to tenants as reflected by the low vacancy rate at 3.5%.

12 Void Rate of Wet Markets

- 12.1 For HA markets operated by HD, out of a total space of 65,154.5m² internal floor area (IFA), 7,353.6m² IFA or 11.3% was vacant as at 31 December 2001. For HA Single-Operator Markets, out of a total leased area of 20,762.7m² IFA, 1,327.6m² IFA (6.4%) was vacant as at 31 October 2001.
- 12.2 It should be noted that Single-Operator Markets are the newest HA markets, built to the most modern standards and centrally air-conditioned.

Most HD-managed markets are older; some were planned over 30 years ago and possibly excessive in terms of size in relation to changed demand situation.

13 Requests for Early Termination

For markets, no Single-Operators have requested early termination. As regards shopping centres, only one Single-Operator terminated prematurely : Yiu Tung in Shau Kei Wan in 1998 but it was mainly due to over-bidding but not poor business.

14 Conversion of Vacant Space for other purposes

- 14.1 Where commercial space becomes vacant, the initial priority will be to re-let for retail purposes. However, if repeated attempts to re-let are unsuccessful, space in less prominent locations may be offered for other purposes such as welfare. In HA markets where it is clear that part of the market is surplus to current requirements, a re-ordering exercise may be conducted to improve the layout and the space thus released converted for other compatible uses for which there is demand. The main considerations underlying the decision in any particular case would be the long-term requirement of the space for commercial purpose, the impact of any conversion on adjoining retail space and the suitability of the space for other beneficial uses.
- 14.2 The period for consideration and time to affect a conversion will vary from case to case depending upon the nature of the premises involved. The conversion of a single bay shop on the ground floor of a domestic block to a welfare use may be approved as soon as it becomes clear from market response that it is surplus to retail requirements, and conversion works may be completed in a few weeks. A major improvement scheme will however take longer to develop to allow for consideration of various alternative plans, to test for viability and to consult stakeholders. The works themselves may take several years, but every attempt is made to minimize disruption to affected tenants and to avoid adverse impact on business. Local tenants and the relevant Estate Management Advisory Committee will be consulted before any major schemes commence.

15 Co-ordination with FEHD on Provision of Markets

- 15.1 In planning for any new markets, the HA and FEHD take a similar approach in that they will take into account existing market facilities provided by both the public and private sectors and also future population growth and market facilities under planning by FEHD/HA and private sectors in the catchment area. This ensures that there is no over-provision.

In detail, HA uses an expenditure-based methodology to assess the retail floorspace requirement which takes into consideration the viability of the retail facilities, the nature and scale and existing and planned retail provisions in the vicinity and so on. As such, the supply and demand for retail facilities within a catchment area, not merely the estate alone, would be the basis of consideration in determining the level of retail provision of a housing estate.

- 15.2 Characteristically, FEHD markets tend to be located in central urban areas while HA markets are in estates in more peripheral locations, so there is limited overlap in catchments. Where such an overlap is evident, HA monitors the impact and reflect this both in rental assessments for affected HA market stalls, and in formulating proposals for periodic improvement of HA commercial facilities.

Housing Department
March 2002

Market Share and Breakdown of Retail Space in Housing Authority Estates

I. Market Share of Retail Space in Hong Kong as at 31 December 2001

	Internal Floor Area (m ²)	Percentage (%)
Private Sector ⁽¹⁾	8 883 787	89
Housing Authority	<u>1 047 148</u>	<u>11</u>
	9 930 935	100

II. Breakdown of Retail Space in Housing Authority Estates

Type of Trade	Internal Floor Area (m ²)	Percentage (%)
General Shops ⁽²⁾	683 382.80	65
Catering Services ⁽³⁾	118 519.00	11
Supermarkets & superstores	123 216.70	12
Market Stalls ⁽⁴⁾	<u>122 029.50</u>	<u>12</u>
	1 047 148.00	100

III. Market Stalls of Food and Environmental Hygiene Department

The total internal floor area for the market stalls under the purview of the Food and Environmental Hygiene Department as at December 2001 was 93 960 m².

Sources :

HA : Internal computer system as at end December 2001
 Private : Rating & Valuation Department as at 1 January 2002

⁽¹⁾ Retail space in private sector includes that under the purview of Food and Environmental Hygiene Department and the Housing Society.

⁽²⁾ This includes the trade types of general wear, durable goods, foodstuff, miscellaneous goods and government lettings and so on.

⁽³⁾ This includes the trade types of Chinese restaurant, specialty restaurant, drinks and refreshments, fast food and cooked food stalls and so on.

⁽⁴⁾ This includes market stalls managed by single-operators and conventional markets.

Annex B

Housing Authority's Guidelines for Letting by Negotiation

Letting by negotiation may be considered in the following circumstances –

- where the amount of space to be leased exceeds 250m² and where the type of trade can attract more customers to the shopping centre, or can provide a desirable facility for residents; or
- where the vacant premises concerned have failed to attract suitable bidders in at least one open tender exercise; or
- where an attraction is offered by the brand name under which the premises are to be operated, or by the tenant's ability to develop his business through substantial promotional activities, which will enhance the trading potential of the shopping centre; or
- where a sitting tenant has demonstrated his capability for expansion of his business, as indicated by –
 - (a) the tenant currently operating a minimum of three outlets under the same trade name with a total area of not less than 250m²; and
 - (b) the tenant having a clear tenancy record in the last three years e.g. without rent arrears, shop-front obstruction or encroachment, complaints from residents etc; and
 - (c) the tenant's existing operation or product providing a service which will meet the demands of estate residents; and
 - (d) the standard of fitting-out and shop display of the tenant's existing outlets being of high standard.
- where an individual or company has demonstrated adequate financial resources and management capability in non-retail sectors to demonstrate capability for successful management of a retail outlet, by having –
 - (a) a minimum of 5 years successful operation of a business;

- (b) employment of not less than 10 staff; and
- (c) financial resources adequate to sustain a retail operation of the size proposed, ie to cover :
 - payment of deposit
 - fitting out and decoration costs
 - overheads including rent for six months