

Your Ref. : CB(3)/PAC/R49  
Our Ref. : HD(EM) SST/PSA/Gen./VFM(Conf.)  
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8 January 2008

Clerk, Public Accounts Committee  
(Attn: Ms. Serena CHU)  
Legislative Council Building  
8 Jackson Road  
Central  
Hong Kong

Dear Ms. CHU,

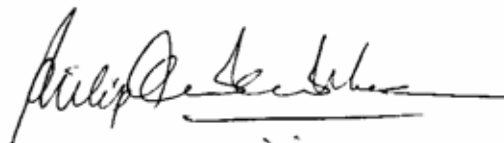
**The Director of Audit's Report on the  
results of value for money audits (Report No. 49)**

**Chapter 10 – Outsourcing of the management  
of public rental housing estates**

Thank you for your letter of 27 December 2007.

The required supplementary information, both in English and Chinese, is forwarded as attached for the consideration by the Public Accounts Committee. A soft copy of the information has been e-mailed to [cwywong@legco.gov.hk](mailto:cwywong@legco.gov.hk).

Yours sincerely,



(K. C. CHIU)  
for Director of Housing

c.c. Secretary for Financial Services and the Treasury  
Director of Audit

**Supplementary Information on the Director of Audit's Report No. 49**  
**Chapter 10 - Outsourcing of the Management of Public Rental Housing Estates**  
**Public Accounts Committee's Hearing on 10.12.2007**

(a) (i) **Time of the first case with incorrect calculation of wages for overtime work and the actions taken in the first and other similar cases**

There were about 10 cases of this nature handled by HD for the period from 1.3.06 to 28.2.07. The dates of discovery and action taken by HD on these cases are shown in **Annex A**.

(ii) **Reasons for the recurrence of similar problem**

As explained at the Public Accounts Committee hearing on 10.12.2007, most of these minor irregularities were detected in the first year of implementation of the package of measures introduced in May 2006. Reasons for the recurrence of similar problem could be due to the following factors -

- these cases were scattered in different estates involving different contractors;
- contractors had taken time to learn from these unintentional mistakes and to make improvement; and
- HD adopted a partnership approach in the past in accordance with the spirit advocated by the Efficiency Unit. Stepped-up action has been taken since November 2007.

(b) (i) **Whether breaches concerning leave and Mandatory Provident Fund (MPF) should be included under the category of issuing DN with Demerit Point**

HD follows the guidelines issued under Financial Circular No. 4/2006 which is applicable to all Government departments. It stipulates that DN carrying demerit point (DNDP) is to be issued only for any of the following four breaches on contractual obligation : (i) wages; (ii) daily maximum working hours; (iii) signing of standard employment contracts; and (iv) wage payment by means of autopay to non-skilled workers. Whether or not to include other breaches concerning leave and MPF should best be reviewed by FSTB in the context of a unified action for all Government departments. HD's view is that these breaches are breaches of Employment Ordinance (Cap. 57) and the Mandatory Provident Fund Scheme Ordinance (Cap. 485) respectively, enforcement actions of which should be taken up by the relevant enforcement agencies, i.e. the Labour Department and the MPFA respectively.

- (ii) **Whether HD could refer breaches relating to possible violation of labour ordinances to law enforcement agencies for follow-up, even without the consent of the workers concerned**

Legal advice has confirmed that HD could do so if the breaches were related to possible violation of labour ordinances. HD will, in future, refer such cases to the relevant law enforcement agency for necessary action.

(c) **Results of reviews and follow-up actions taken by HD**

- (i) **HD will review its monitoring mechanism and take appropriate regulatory actions such as serving DNs, issuing adverse performance reports (ARs) and delisting PSAs/contractors from HA approved lists. (Para. 2.27(b))**

Past Practices	New Practices Arising from the Review	Follow-up Actions
Measures on protection of non-skilled workers were audited by HD frontline staff on a monthly basis. Irregularities found in the monthly audits or detected by Central Monitoring Team (CMT) would be followed up by HD staff who would consider and decide if regulatory actions including issuance of warning letter, AR, DN, or delisting from HA's approved lists where appropriate.	In addition to the past practices, a more stringent approach will be adopted in the issuance of DNDP and DN not carrying demerit point (DNNDP). These new practices have been introduced via EMDI No. M07/2007(S) issued on 7.12.2007. For each DNDP or DNNDP, marks will be deducted in the PSA/Contractor's performance scores which will reduce their chance of success in future tendering exercises.	To follow strictly the new guidelines EMDI No. M07/2007(S) issued on 7.12.2007. Follow-up seminars with staff and contractors would be taken.

- (ii) **HD has applied stringent rules against serious breaches of labour protection requirements in relation to committed wages, daily maximum working hours, signing of standard employment contracts and wage payment through autopay as well as those PSAs/contractors failing to comply with contractual requirements. On the other hand, HD has been adopting a partnership approach in handling outsourcing work. PSAs/contractors are allowed to take rectification actions on minor irregularities if the defaults are not committed wilfully. (Para. 2.27(c))**

Past Practices	New Practices Arising from the Review	Follow-up Actions
<p>Partnership approach was adopted, DNDP on violation of the above contractual obligations was to be issued if –</p> <p>i. the employment-related irregularities were committed intentionally (in considering the severity of the act and whether it was a technical fault).</p> <p>ii. the irregularities had not been rectified by the contractor upon notification or issue of warning letters by the management.</p>	<p>Stringent rules have been adopted against all employment-related irregularities.</p>	<p>To follow strictly the new guidelines, EMDI No. M07/2007(S) issued on 7.12.2007.</p> <p>The new practices would be clearly disseminated to HD front-line staff and contractors.</p>

- (iii) **HD will review its existing regulatory system with a view to stepping up regulatory actions against defaulted PSAs/contractors, where necessary. (Para. 2.27(d))**

Past Practices	New Practices Arising from the Review	Follow-up Actions
<p>HD has been adopting a partnership approach in handling outsourcing work. PSAs/contractors were allowed to take rectification actions on minor irregularities if the defaults were not committed wilfully.</p>	<p>Stringent rules have been adopted against all employment-related irregularities.</p> <p>Work flow has been revised to enhance follow-up action to be taken against irregular cases.</p>	<p>To follow strictly the new guidelines, EMDI No. M07/2007(S) issued on 7.12.2007.</p> <p>The new practices would be clearly disseminated to HD front-line staff and contractors.</p>

- (iv) **HD will review the details of implementation for the appointment of the CMT to oversee follow-up action taken by estate staff. (Para. 2.27(e))**

Past Practices	New Practices Arising from the Review	Follow-up Actions
CMT provided support services to estate staff in monitoring the PSAs/contractors' compliance with labour protection clauses. CMT centrally monitored the Employment-related Irregularities Complaint Register to keep in view the progress and outcome of investigation and actions taken by estate staff.	In addition to the past practices, CMT is now entrusted with the responsibility of overseeing the follow-up action taken by estate staff to ensure a consistent regulatory approach is taken in compliance with the relevant instructions.	PS Contract Process Manual was revised on 23.10.2007.  To follow strictly the new guidelines, EMDI No. M07/2007(S) issued on 7.12.2007.

- (v) **HD will issue guidelines on the documentation of regulatory actions taken or not taken for compliance by estate staff. (Para. 2.27(f))**

Past Practices	New Practices Arising from the Review	Follow-up actions
<p>i. To promote partnership spirit and avoid unnecessary disputes, frontline manager had to interview the contractor and request him to give explanation prior to the issuance of DN with record of interview to be kept.</p> <p>ii. If frontline staff were in doubt on the explanation given by the contractor, directive from their senior staff would be sought.</p> <p>iii. DN would be issued if</p>	<p>Documentation of regulatory actions taken will be recorded as follows –</p> <p>i. District Senior Housing Manager (DSHM)/Senior Property Services Manager (SPSM)'s endorsement is required for each issuance of DNDP/DNNDP or non-issuance of DN.</p> <p>ii. To pass the fully completed cases, endorsed by DSHM/SPSM, to CMT for monitoring.</p> <p>iii. In case there is</p>	<p>PS Contract Process Manual was revised on 23.10.2007.</p> <p>To follow strictly the new guidelines, EMDI No. M07/2007(S) issued on 7.12.2007.</p>

the explanation given by the contractor was not acceptable.	disagreement on the outcome endorsed by DSHM/SPSM, Regional Chief Manager's decision will be sought.	
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(d) **HD to bring to the attention of Tender Committee (TC) the 5-year suspension and TC's decision**

FSTB's 5-year suspension requirement as stipulated in Financial Circular No. 4/2006 has been brought to the attention of the Tender Committee (TC) of HA again at its meeting on 13 December 2007. A copy of the draft minutes of the meeting (subject to confirmation at the next TC meeting) is attached at **Annex B**.

(e) **Seek legal advice and consider the feasibility of introducing fines to penalise PSAs with persistently poor performance.**

We have sought legal advice. The advice is that HA does not have the power under the Housing Ordinance (Cap. 283) to impose a "fine" on a PSA due to its poor performance.

The legal advice further elaborates that under the laws of contract, where one party has acted in breach of the contract, the other party is entitled to claim damages for the breach. However, damages will have to be quantified and must be genuine estimates of the loss. This is typical in a construction contract where a contractor will have to pay the employer liquidated damages of a fixed amount (for each day's delay beyond the completion date) if he fails to complete the project on time.

Even so, liquidated damages clauses have been subject to legal challenges when they are perceived as a "penalty", e.g. if they are in sums in disproportionate to the actual loss.

In view of the above, it is considered inappropriate to introduce "fines" over and above actual losses to penalise PSAs due to their poor performance.

*\*Note by Clerk, PAC: Part of Annex B (i.e. draft minutes of Tender Committee meeting) not attached.*

(f) **Number of employment-related irregularities found in PSA contracts of the lowest and higher bids**

Of the existing 41 PSA contracts, six cases of employment-related irregularities were found in contracts of the lowest bids. Another six cases were found in those with higher bids. There seems to be no correlation between employment-related irregularities and the bids offered by contractors.

Case of Incorrect Calculation of Wages for Overtime Work

	Name of Estate - Nature of Contract & Date of first discovery	for period from 1.3.2006 to 28.2.2007				Remarks
		Date of letter issued to contractor asking for explanation	Date of explanation given by the contractor	Underpayment repaid to worker (Amount involved for a worker)	Date of Advisory Letter / Default Notice issued to contractor	
1	Cheung Wah - cleansing contract 24.3.2006	-	-	✓  (Less than \$80)	Nil	
2	On Yam - security contract 8.5.2006	-	-	✓  (Less than \$40)	25.10.2007	
3	Lai King - security contract 22.5.2006	-	28.6.2006	X	N/A	Labour Department confirmed no contravention of Employment Ordinance
4	Yue Wan - cleansing contract 31.7.2006	7.2.2007	13.2.2007	✓  (Less than \$200)	Nil	
5	Shan King - security contract 31.8.2006	27.11.2006	12.12.2006	✓  (Less than \$220)	Nil	
6	Sam Shing - cleansing contract 4.10.2006	30.11.2006	5.12.2006	✓  (Less than \$30)	29.3.2007	



**Case of Incorrect Calculation of Wages for Overtime Work**

	Name of Estate - Nature of Contract & Date of first discovery	for period from 1.3.2006 to 28.2.2007				Remarks
		Date of letter issued to contractor asking for explanation	Date of explanation given by the contractor	Underpayment repaid to worker (Amount involved for a worker)	Date of Advisory Letter / Default Notice issued to contractor	
7	Lei Yue Mun - security contract 8.1.2007	16.4.2007	22.6.2007 and 25.7.2007	✓  (Less than \$100)	6.8.2007	
8	Fu Tai - security contract 18.1.2007	7.6.2007	28.6.2007	✓  (Less than \$680)	24.10.2007	
9	Shun On - security contract 29.1.2007	3.5.2007 and 5.6.2007	8.6.2007	✓  (Less than \$100)	23.7.2007	
10	Shek Yam - cleansing contract 8.2.2007	17.5.2007	13.6.2007	✓  (Less than \$200)	Nil	

## **Protection of Non-skilled Workers Engaged in Outsourcing Contracts**

Tender Committee  
13 December 2007

### **ISSUE**

**Audit Commission** recommended that the Director of Housing should bring to the attention of the Tender Committee the FSTB's five-year suspension requirement in Financial Circular No.4/2006

(FSTB is the Financial Services and the Treasury Bureau)

## COMPARISON

### HA's Practice

(approved by TC on 23.3.2006)

- If a **service contractor** has obtained any conviction under the relevant Ordinances on or after 1.5.2006 or over a rolling period of 3 years accumulated three demerit points obtained on or after 1.5.2006, **it will be removed from the respective HA List. The period of removal will be set at a maximum of five years.**

### Government Practice

(FC No. 4/2006 promulgated on 27.4.2006)

- If a **tenderer** has obtained any conviction under the relevant Ordinances on or after 1.5.2006 or over a rolling period of 3 years accumulated three demerit points obtained on or after 1.5.2006, **its tender offer shall not be considered for a period of five years.**

## Background in formulating HA's policy

- HA's policy was approved by Members on 23.3.2006 upon discussion of **Paper No. TC 34/2006 on Tightening Measures for Service Contracts**
- **A five-year list removal was first proposed**
- Members opined that a more flexible approach should be adopted and thus approved the period should be **set at a maximum of five years** (Paper No. TC 42/2006 meeting minutes refers)

## Fundamental Difference in the Procurement Policy & Practice

### Housing Authority

- Has been maintaining permanent lists of service contractors
- Adopts a selective tendering procedure

### The Government

- Has **NO** list of services contractors
- Adopts an open tendering procedure

## HA's List Management Mechanism

### List Admission Criteria

- 5-year clean conviction record
- 5-year clean demerit point record
- Satisfactory record of fair treatment to non-skilled workers over the past 5 years

### List Retention Criteria

- Annual submission of a statement of 'all convictions' or 'no conviction' and 'all demerit point' received

### Regulatory Action

- List removal up to 5 years for any conviction received or 3 demerit points in a rolling 3-year period accumulated

### Objection or Appeal Mechanism

- Provisional Review Board considers and determines appeals against default notices attracting demerit points. (Since establishment, 2 Board Meetings were conducted in October 2005, chaired by D2 officer with the participation of one TC Member.)

## List Removal of a Service Contractor

### Paper No. TC 39/2007 (19 July 2007)

- A service contractor on HA Lists with one court conviction under the Employees' Compensation Ordinance (ECO) on 10.11.2006 was discussed. The offence was the dismissal of an injured worker in Oct 2005 before the issue of Certificate of Compensation Assessment).
- Members approved to impose a 1-year list removal, counting from the date of conviction, on the service contractor.
- The service contractor applied for List Re-admission recently. Whilst processing its application, we found that this service contractor had 2 convictions on 18.7.2003 which had contravened our list admission requirement of a 5-year clean conviction record.

## Way Forward

- The Legislative Council Public Accounts Committee (PAC) directed the Department to draw Members' attention to **consider re-examining her policy and practices** having regard to the mechanism as promulgated in the Financial Circular No. 4/2006

## **Protection of Non-skilled Workers Way Forward - Enhancement**

### **Contract Management** (Performance Monitoring)

To strengthen the system on the issuance of

- **Default Notices attracting Demerit Points, AND**
- **Default Notices not attracting Demerit Points**

### **List Management**

- **More Tightened Measures?**
- **To align with policy promulgated by FSTB?**