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**Panel on Housing**

**Meeting on 7 January 2010**

**Background brief on the new rent adjustment mechanism**

**Purpose**

This paper sets out the background to the new rent adjustment mechanism.

**Introduction**

2. Under Section 16(1) of the Housing Ordinance (HO) (Cap.283), the Housing Authority (HA) may let to any person any residential unit in its estates subject to the payment of such rent as it may determine. In determining the rents of its public housing units, HA makes reference to tenants' affordability. HA has adopted the median rent-to-income ratio (MRIR)<sup>1</sup> as a general affordability indicator. Administratively, HA used two MRIR benchmarks<sup>2</sup> in setting public housing rents based on space allocation standards, and took into account a combination of other factors, such as the comparative values of estates, their locations and transportation, flat size, management and maintenance costs, inflation, wage movement, rates, HA's financial position, etc. Prior to 1998, review of rents of public rental housing (PRH) units was conducted by HA at two-year intervals.

3. On 27 June 1997, the former Legislative Council passed a Private Member's Bill, which was subsequently enacted as Housing (Amendment) Ordinance 1997 (Amendment Ordinance 1997), to amend section 16(1) of HO to the effect that any determination of variation of rent by HA should only take effect at least three years after the preceding rent determination came into effect, and that the rent determined should be of such amount that the MRIR for all public housing estates should not exceed 10%. After the enactment of the Amendment Ordinance 1997, HA had frozen

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<sup>1</sup> Rent-to-income ratio is the expression of rent as a percentage of household income. MRIR gives the median value of the rent-to-income ratios of all public rental housing households. By definition, 50% of the relevant households' rent-to-income ratios will be below MRIR and the other 50% above it.

<sup>2</sup> The two MRIR benchmarks are 15% for the minimum space allocation standard of 5.5 m<sup>2</sup> Internal Floor Area (IFA) per person (in place since 1986), and 18.5% for the higher space allocation standard of 7 m<sup>2</sup> IFA per person (adopted in 1991).

the rents of newly completed PRH estates at the 1997 level and deferred rent reviews for existing estates since 1999. However, with the downturn of the economy since 1997, the income of the general public had been decreasing. Even without rental increase, the overall MRIR for the third quarter of 2 000 stood at 10.2%. There were strong calls from PRH tenants for the Administration to review PRH rents to comply with the 10% MRIR cap<sup>3</sup>.

4. In October and November 2002, two PRH tenants applied for judicial review in respect of HA's decisions to defer rent reviews. On 11 July 2003, the Court of the First Instance ruled in favour of the appellants. HA appealed to the Court of Appeal which ruled in favour of HA in November 2004. The case was subsequently brought to the Court of Final Appeal (CFA) which ruled in favour of HA on 21 November 2005<sup>4</sup>. The matters examined in the judicial review have raised important questions about HA's existing domestic rent policy and the long-term sustainability of its finances. In November 2006, HA endorsed a report submitted by the Ad Hoc Committee on Review of Domestic Rent Policy (the CDRP) which was set up in 2001 by HA to review its domestic rent policy with the major objective to establish a clear, objective and flexible rent adjustment mechanism to better reflect tenants' affordability and help ensure a sustainable development of the public housing programme.

5. The key recommendations of CDRP included amending HO to remove the MRIR cap to enable HA to introduce the new income-based rent adjustment mechanism to determine the extent of rent adjustments according to changes in PRH tenants' household income. To provide a fair starting point for the new adjustment mechanism to operate fairly and effectively, HA agreed to introduce an across-the-board rent reduction of 11.6% upon passage of the amendment bill, and to grant a one-off rent remission for the month of February 2007 to PRH tenants<sup>5</sup>.

6. On 31 January 2007, the Administration introduced the Housing (Amendment) Bill 2007 (the Bill) to replace the statutory 10% MRIR cap with a rent adjustment framework that provided for both upward and downward rent adjustments according to changes in PRH tenants' household income. The Bill was passed at the Council meeting on 13 June 2007 and came into operation on 1 January 2008. The report of the Bills Committee on Housing (Amendment) Bill 2007 is hyperlinked below for easy reference.

### **New rent adjustment mechanism**

7. Under the new rent adjustment mechanism, a review of PRH rent will be conducted once every two years. The PRH rent will be either adjusted upward or downward according to changes in the income index, which reflect changes in PRH

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<sup>3</sup> The MRIR reached 14.3% in the third quarter of 2006 as compared to 9.1 % when the statutory 10% cap was passed by the former Legislative Council under the Housing (Amendment) (No. 3) Bill 1996 in June 1997.

<sup>4</sup> HO Choi-wan v Hong Kong Housing Authority (2005) 8 HKCFAR 628.

<sup>5</sup> The rent remission has been granted to PRH tenants and Interim Housing licensees with the exception of those paying additional rent or licence fees.

tenants' household income and will be computed by the Commissioner for Census and Statistics. For downward rent adjustment, the PRH rent shall be reduced according to the rate of reduction of the income index. In case of upward rent adjustment, the PRH rent shall be increased by the rate of increase of the index or 10%, whichever is less. To provide a new starting point for the income-based rent adjustment mechanism to operate effectively, HA reduced the PRH rent by 11.6% starting from August 2007.

### **Latest development**

8. The Administration proposes to brief members on the approved methodology and the progress of the first rent review under the new rent adjustment mechanism at the Panel meeting on 7 January 2010.

### **Relevant paper**

Report of the Bills Committee on Housing (Amendment) Bill 2007 to the Council meeting on 13 June 2007

<http://www.legco.gov.hk/yr06-07/english/bc/bc01/reports/bc01cb1-1871-e.pdf>

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