



Our Ref : HD 3-2/M4-35/4/V  
Your Ref : CB(4)/PAC/R56

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Date : 31 May 2011

Clerk to Public Accounts Committee  
Legislative Council  
8 Jackson Road, Central  
Hong Kong  
(Attention : Ms Macy NG)

Dear Ms NG,

**The Director of Audit's Report on the  
Results of value for money audits (Report No. 56)**

**Hong Kong Housing Authority :  
Management of commercial properties (Chapter 7)**

I refer to your letter of 27 May 2011 on the above subject.

Members of the Commercial Properties Committee (CPC) noted the continued demand for the 8,000 small factory units in the six newer factory estates of the Housing Authority at the meeting held on 28 April 2011. In view of their high letting rate, over 99%, CPC Members supported the Housing Department's proposal to continue managing them *pro tem* and to review the situation from time to time. This modification to the policy was set out in paragraph 16 of the attached Paper No. CPC 17/2011. We will inform the Legislative Council if there is a substantial change to the long-term policy on the ownership and management of these factory estates in future.

Yours sincerely,



(LIU King-leung)

for Director of Housing

encl.

c.c. Secretary for Financial Services and The Treasury (Fax No. : 2147 5239)  
Director of Audit (Fax No. : 2583 9063)

Estate Management Sub-division (3)  
5/F, Block 2, Housing Authority Headquarters, 33 Fat Kwong Street, Ho Man Tin, Kowloon.

**Memorandum for the Commercial Properties Committee of  
the Hong Kong Housing Authority**

**Audit Report on Management of Commercial Properties**

**PURPOSE**

To inform Members of the major findings, recommendations and the management response to the Value for Money (VFM) Audit Report conducted by the Audit Commission (AC) on the Hong Kong Housing Authority (HA) : Management of Commercial Properties.

**BACKGROUND**

2. VFM study aimed at identifying areas for improvement in terms of internal control, operational efficiency, economy and effectiveness in management of HA's non-domestic properties. It comprehensively covered the management and letting of commercial properties including retail premises, carparks and factory estates, performance measurement and reporting mechanism as well as a concluding chapter for the 2005 divestment exercise. Details of VFM study are contained in Chapter 7 of Report No. 56 of the Director of Audit which is available on website at <http://www.aud.gov.hk>. A Summary of the relevant Audit Report is at the **Annex**. The Public Accounts Committee of the Legislative Council will conduct hearing on this Chapter in mid-May 2011.

**MAJOR FINDINGS AND MANAGEMENT RESPONSES**

3. AC recognised that HA and the Housing Department (HD) have taken various measures to optimise the effective use of commercial properties. However, individual cases on management irregularities such as subletting, gambling activities, unauthorised use of premises and obstructions in estate public areas were observed in the course of auditing. Recommendations were made for enhancing the effectiveness in management of HA's non-domestic properties in these respective areas.

4. We welcome and generally agree with the views and comments made by AC. Most of the recommendations have either been implemented or will be taken on board. Where policy clearance is required, we will seek the views from HA or this Committee. As to the major findings and recommendations, the management has the following responses—

**(a) Management of Retail Premises**

5. While acknowledging that HD had reduced the vacancy rate by introducing a number of initiatives in the past few years, AC recommended HD to (i) enhance actions in publicising and re-letting vacant premises; (ii) re-generate strategy for market re-ordering and shopping centre improvement works; (iii) speed up the implementation of revised leasing strategy for cooked-food-stalls; and (iv) intensify control on operating expenditure.

*Day-to-day management of retail premises*

6. The management has investigated into individual suspected cases of improper use of retail premises and storerooms and taken tenancy enforcement actions including issuance of notice to quit under Section 19 (1)(b) of the Housing Ordinance to the tenants/licensees identified in the report. HD will report promptly all suspected gambling activities to the Police for enforcement action and continue to step up measures against improper use of retail premises and gambling activities. We will also continue to combat obstructions in estate public areas under the Enhanced Marking Scheme.

7. We have issued detailed guidelines to advise HD/contractor staff to step up unit-to-unit inspections, in particular those non-trading retail premises and repeated offenders. Irregularities observed during the inspections and subsequent follow-up actions will be monitored by the senior management on a quarterly basis.

8. The management is studying the feasibility of specifying the opening hours of shop premises in the tenancy agreements according to the nature of business and customers' demand and will obtain policy blessing from this Committee as and when required.

### *Letting of retail premises*

9. HD will continue to publicise vacant premises for re-letting as frequently as practicable. For premises with limited retail potential, we will consider implementing conversion plan in the longer term.

### *Monitoring of operating expenditure*

10. HD will monitor operating expenditure of the retail facilities against the benchmarks, of which periodical reviews will be conducted.

## **(b) Management of Carparks**

11. AC appreciated HD's efforts in converting surplus carparks for other uses and recommended us to regularly review the parking planning standards and expedite the conversion of excessive carparking facilities for better utilisation of resources.

### *Planning the provision of carparking facilities*

12. HD will maintain the existing co-ordination mechanism with the Transport Department to review and refine the planning standards of parking spaces and will carefully plan the provision of carparking facilities to new public housing developments on a case-by-case basis.

### *Converting surplus carparking facilities into other uses*

13. The project quoted by AC was a very special case, of which HD had exercised flexibility to speed up the establishment of a converted premises to strengthen the community cohesiveness, create job opportunities and provide training for volunteers in a new town.

14. HD will continue the practice of making rental assessment for major conversion projects with due consideration on the conversion costs and the proposed use of converted premises.

## **(c) Management of Factory Estates**

15. AC recommended HA to formulate a clearance plan for Chai Wan Factory Estate early and to develop a strategy for the long-term development of the six newer factory estates.

16. Upon approval by this Committee, we announced the clearance of Chai Wan Factory Estate on 10 March 2011 with tentative evacuation date scheduled for 30 September 2012. HD will continue to manage the six newer factory estates, viz Wang Cheong, Yip On, Hoi Tai, Sui Fai, Chun Shing and Kwai On and review the situation from time to time.

17. Regarding the day-to-day management of factory estates, HD has investigated into individual suspected subletting cases and taken necessary actions to rectify the irregularities. We have also conducted a review of the operating procedures and will strengthen enforcement actions against subletting and improper use of the factory units.

**(d) Performance Measurement and Reporting**

18. AC considered a need to revise the calculation methodology of vacancy rate for retail premises. In response, HD has excluded all new premises not yet ready for letting from the total retail stock in calculating the overall vacancy rate. HD will also revisit the approach in reporting vacancy rate of different categories of non-domestic premises and consider setting specific performance indicators and targets for different types of commercial properties where appropriate.

19. To tap the feedback from customers for continued improvement, HD will extend the scope of the annual Public Housing Recurrent Survey to cover residents' satisfaction level on the management of HA's commercial properties from 2011 onwards.

**(e) 2005 Divestment Exercise**

20. AC noted the complexity and complication of works involved in the 2005 divestment exercise. In planning a similar exercise in future, AC recommended the Administration to critically assess the potential financial implications of transferring the beneficial ownership of the divested properties without a definite timeline for the transfer of legal titles.

21. At the time of divestment in November 2005, HA had fully received the purchase price and there was no loss of revenue to HA. The original target date of mid-2008 to complete the transfer of legal titles was re-scheduled to July 2010 in view of the unforeseen statutory requirements and complexities encountered in the lease procurement process. HA met the revised timeframe for the whole procurement task in July 2010.

22. AC also recommended the Administration to conduct a post-implementation review (PIR) of the divestment exercise. Although HA has no plan to further divest its retail and carparking facilities, we will conduct a PIR of the 2005 exercise at an appropriate time.

## **IMPLEMENTATION**

23. HD has been working closely with the relevant parties to implement all the agreed recommendations. The management will conduct follow-up review to further examine the implementation progress.

## **PUBLIC REACTION**

24. The public would welcome our measures for enhancing the management of HA's non-domestic properties.

## **INFORMATION**

25. This paper is issued for Members' information. A briefing to Members will be made at the forthcoming meeting of the Commercial Properties Committee to be held on 28 April 2011.

Miss Michelle LAU  
Secretary, Commercial Properties Committee  
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File Ref. : HD 3-2/M4 – 35/4  
(Estate Management Division)  
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## Report No. 56 of the Director of Audit — Chapter 7

### HONG KONG HOUSING AUTHORITY: MANAGEMENT OF COMMERCIAL PROPERTIES

#### Summary

1. The Hong Kong Housing Authority (HA) is a statutory body established under the Housing Ordinance (Cap. 283), with the Housing Department (HD) acting as its executive arm. In November 2005, HA divested 180 retail and carpark (RC) facilities to a Real Estate Investment Trust (REIT) which was listed on the Stock Exchange of Hong Kong. Following the divestment, HA has continued to manage the non-divested commercial properties and those provided under new public housing developments.

2. As at December 2010, the commercial and non-domestic properties under HA's management comprised 168 600 square metres of retail areas and 27 000 carparking spaces, as well as factory, welfare and other miscellaneous premises. In 2009-10, HA commercial operations generated an operating surplus of \$461 million. HA's Commercial Properties Committee (CPC) advises HA on policies concerning its commercial, industrial and other non-domestic facilities, and optimising the financial return on its investment. The Audit Commission (Audit) has recently conducted a review of the management of HA commercial properties.

#### Management of retail premises

3. *Day-to-day management of retail premises.* Audit visited 12 HA major retail facilities between October 2010 and January 2011 and found that: (a) some storerooms had been altered by tenants for other uses without HD's approval; (b) suspected gambling activities appeared prevalent in some retail facilities; (c) some let-out retail premises were not open for business (i.e. non-trading) during normal business hours; and (d) there were areas where improvements could be made in the implementation of the HA marking scheme. *Audit has recommended that the Director of Housing should: (a) request HD staff and contractors to step up their daily patrol work and unit-to-unit inspections to prevent unauthorised use and alteration of retail premises (including storerooms); (b) step up measures to combat suspected gambling activities in HA retail facilities; (c) ascertain the reasons for the prevalence of non-trading in some retail facilities and take actions to address them; and (d) remind HD staff and contractors to strictly follow the established procedures in enforcing HA marking scheme.*

4. ***Letting of retail premises.*** Although many HA retail premises have remained vacant for a long time, HD did not take adequate measures to ensure that these premises were widely publicised and put up for open tender as frequently as practicable. For a vacant premises which did not attract any bidder in an open tender, HD would normally take about two calendar months to re-tender the same premises. Also, HD staff may not have full market information when re-designating the trade appropriate for the premises in the re-tendering exercise. *Audit has recommended that the Director of Housing should: (a) ensure that all vacant retail premises available for letting are widely publicised; and (b) in re-letting vacant retail premises, further encourage prospective tenants to make trade suggestions.*

5. ***Implementation of improvement measures.*** In recent years, HA has implemented a number of improvement measures for its retail premises, such as earmarking four retail facilities for early consideration of major improvement works and conducting “re-ordering” exercises in a number of markets. In setting the priority for major improvement works, HD mainly took into account the commercial potential of the retail facilities concerned. Audit also noted that although HD had taken improvement measures in some markets, their vacancy rates remained high. *Audit has recommended that the Director of Housing should: (a) duly take into account the vacancy rates of retail facilities when selecting them for major improvement works to enhance their commercial potential; and (b) take early actions to address the long-standing vacancy problem in some HA markets.*

6. ***Monitoring of operating expenditure.*** To ensure that retail facilities are operated cost-effectively, HD has set major operating expenditure benchmarks for compliance by its estate housing managers. In 2009-10, many retail facilities had their operating expenditure exceeding HD benchmarks. Some estate housing managers had not fully reported the non-compliance to the senior management, nor had they proposed adequate follow-up action for improving the situation. *Audit has recommended that the Director of Housing should improve the current monitoring mechanism to ensure that effective follow-up actions are taken on all cases of non-compliance.*

## **Management of car parks**

7. ***Planning the provision of parking facilities.*** Prior to 2009, parking facilities for public housing developments were built according to old planning standards stipulated in the Hong Kong Planning Standards and Guidelines (HKPSG). According to HD records, for many aged estates, the provision of public housing carpark facilities had turned out to be greater than the actual demand, leading to high vacancy rates in many HA car parks. Since 2009, substantial revisions to the parking standards have been made to HKPSG.

*Audit has recommended that the Director of Housing should, in consultation with the Transport Department, continue to regularly review the parking planning standards, having regard to the changing supply and demand conditions.*

8. ***Measures to improve the utilisation of parking spaces.*** In recent years, HD has taken various measures to improve the utilisation of parking spaces, including conversion of surplus carpark facilities into other beneficial uses and letting of parking spaces to non-residents. In 2010, HD conducted strength-weakness-opportunity-threat (SWOT) analysis of 38 car parks (with occupancy rate below 70% and with more than 20 parking spaces) and categorised them into different groups for follow-up actions. *Given that many of the 38 car parks had a consistently low occupancy rate for many years, Audit has recommended that the Director of Housing should expedite efforts to implement the recommendations arising from the SWOT analysis.*

9. ***Conversion of surplus carpark facilities into other uses.*** Since 2006, HD has converted some underutilised parking facilities into other uses. As at January 2011, four projects were completed and successfully leased out. One of these projects related to leasing part of a car park to an organisation. Although this project was a commercial letting according to HD records, the rent charged to the organisation was on a par with the concessionary rent normally applicable for welfare lettings. This was contrary to HD's established practice of charging market rate for commercial lettings. *Audit has recommended that, in exploring major conversion of commercial premises in future, the Director of Housing should ensure that the rent for the converted premises is assessed, duly taking into account the conversion costs and the proposed use of the premises.*

### **Management of factory estates**

10. Having regard to its core mission of providing subsidised rental housing, HA decided in 1989 to progressively absolve itself from the ownership and management of factory estates in the long term. Since then, a number of factory estates had been cleared. As at January 2011, the HA still managed seven factory estates. Of these, the Chai Wan Factory Estate (CWFE) was built in 1959 using old design standards without lift service. The remaining six, completed in or after 1979, were built to comparatively modern standards.

11. ***Clearance of old factory estates.*** In November 2000, HA reviewed the position of the old factory estates (those built in the late 1950s to mid-1970s). Given the obsolete design and increasing maintenance costs, HA noted that the estates were approaching the point where clearance needed to be considered. Up to January 2011, HA had cleared all old factory estates, except

CWFE. CWFE had been running at a deficit of about \$2 million each year and was in poor building conditions. Audit raised concern about a lack of a definite clearance plan for CWFE. In the event, CPC approved in March 2011 a clearance plan for CWFE.

12. ***Long-term development of newer factory estates.*** Since 1989, it has been HA's policy to absolve itself from the ownership and management of factory estates (see para. 10). However, up to January 2011 (after more than 21 years), HD had not formulated a long-term strategy to implement the policy. *Audit has recommended that the Director of Housing should review the position of the six newer factory estates and develop a strategy for their long-term development.*

13. ***Subletting of factory premises.*** Under the provisions of factory tenancy agreement, a tenant should not sublet factory premises without HD written permission. To help detect subletting or unauthorised use of factory premises, HD has laid down procedures to be followed by its staff. These procedures include conducting thorough inspection of each factory unit on a 18-month cycle covering the checking of any change of factory name and trade, and whether the factory is operated by the tenant or by an unauthorised person. Audit visited two factory estates and examined their inspection records. Audit found that HD procedures had not been properly followed.

14. Audit also found that many factory units bore names or carried out trades which were different from those shown in HD records. Audit selected some factory units for conducting business registration search. The results indicated that, for some of these units, the tenants were not the business owners. Instead, businesses were operated by third parties. *Audit has recommended that the Director of Housing should follow up on the suspected subletting cases identified by Audit and step up efforts to combat the problem of subletting.*

### **Performance measurement and reporting**

15. HA has set various key performance indicators (KPIs) and targets for the management of commercial properties. KPIs include vacancy rate for retail premises, rent arrears, and operating expenditure as a percentage of income. Audit found that: (a) HD had not properly calculated the vacancy rates of retail premises for reporting to CPC; (b) HD did not systematically collect feedback on the residents' satisfaction level on various aspects of performance in the management of commercial properties; and (c) apart from retail premises, there were no KPIs/targets to measure the vacancy position of other types of properties. *Audit has recommended that the Director of Housing should: (a) review and revise the basis for calculating the vacancy rate of retail premises; (b) devise a mechanism to gauge, and report to CPC, the residents' satisfaction*

*level concerning management of commercial properties; and (c) consider setting specific KPIs and targets for different types of commercial properties.*

### **The way forward**

16. The divestment of 180 RC facilities in 2005 (see para. 1) was the first exercise of its kind implemented by HA. In 2006, the Administration reported that HA would look for opportunities to further divest the remaining RC facilities and those to be built in the future. In December 2009, the Secretary for Transport and Housing said that HA still had no plan to further divest its properties. There have been various issues arising from the 2005 divestment exercise, including the transfer of legal titles of divested properties from HA to REIT. *Audit has recommended that the Director of Housing, in consultation with the Secretary for Transport and Housing and the Secretary for Financial Services and the Treasury, should: (a) conduct a post-implementation review of the 2005 divestment exercise to evaluate its effectiveness and to identify if there are lessons to be learnt; and (b) based on the outcome of the review, map out the way forward for the management of HA commercial properties.*

### **Response from the Administration**

17. The Director of Housing agrees with the audit recommendations.

April 2011