A. Introduction

The Audit Commission ("Audit") conducted a review of the direct land grants made by the Government at nil or nominal premium for private hospital development, and examined one land sale transaction for private hospital development.

2. **Hon Abraham SHEK Lai-him** declared that he was currently a member of the Court and Council of the University of Hong Kong and an Independent Non-executive Director ("INED") of the Hsin Chong Construction Group Ltd. and NWS Holdings Limited. **Hon Abraham SHEK Lai-him** said that being a member of the Court of the University of Hong Kong and an INED of Hsin Chong Construction Group Ltd. and NWS Holdings Limited, he was neither informed of nor involved in the April 2012 tendering exercise for private hospital development at two government sites. **Hon Abraham SHEK Lai-him** also said that being a member of the Council of the University of Hong Kong, he was aware that the University of Hong Kong might involve in the April 2012 tendering exercise for private hospital development at two government sites.

3. **Hon Paul TSE Wai-chun** declared that he was currently a member of the Court of the University of Hong Kong. **Hon Paul TSE Wai-chun** said that he was neither informed of nor involved in the April 2012 tendering exercise for private hospital development at two government sites.

4. As a Member returned by the Real Estate and Construction functional constituency, **Hon Abraham SHEK Lai-him** decided that it was prudent for him not to chair the public hearing as well as the Committee's internal deliberations on Part 4 of the Director of Audit's Report ("Audit Report") on sale of land for private hospital development. Hon Paul TSE Wai-chun, Deputy Chairman of the Committee, presided over the public hearing as well as the Committee's internal deliberations on Part 4 of the Audit Report on sale of land for private hospital development.

5. **Hon NG Leung-sing** declared that he was a Chinese Representative of the now dissolved Sino-British Land Commission.

B. Special land grant conditions set on private hospitals

6. The Committee noted that as early as 1957 and further elaborated in 1981 (i.e. "the 1981 requirements") as set out in Appendix A to the Audit Report, it was the Government's policy to grant Government sites by private treaty at nil or nominal premium to non-profit-making private hospitals, subject to a number of conditions. These conditions included (i) the need to provide free or low-charge beds and (ii) the need to plough back profits/surplus derived from the hospitals to improve and expand the hospital facilities (i.e. the "Two Salient Requirements"), the intention of which was that with the Government revenue foregone, a wider section of the public could benefit. Audit however found that the Two Salient Requirements had not always been strictly and consistently applied to six of the eight direct land grants made to five private hospitals as shown in Table 2 in paragraph 2.10 of the Audit Report. The Committee asked which bureau/department ("B/D") was responsible for implementing the aforesaid Government's policy.

7. **Dr KO Wing-man**, the **Secretary for Food and Health**, responded that:

- the Food and Health Bureau ("FHB") was responsible for proposing the land grant conditions for inclusion in the land lease to non-profit-making private hospitals for consideration and approval by the Executive Council ("ExCo"); and

- upon approval of the land grants to private hospitals by the ExCo, the Department of Health ("DH") was responsible for enforcing the compliance with the land grant conditions by private hospitals.

8. **Ms Bernadette LINN**, the **Director of Lands**, responded that:

- it was the established practice of the Lands Department ("Lands D") to circulate the draft private treaty grant ("PTG") to the relevant B/D for comments, prior to submitting the PTG to the ExCo for approval. The relevant B/D could add or take out any land condition(s) from the draft PTG as deemed appropriate from their policy perspectives. Similar procedures would be adopted for processing subsequent changes to the private land grant arising from, say, surrendering of a land grant in exchange for another land grant and changing the use of a building on the land grant site;

- notwithstanding the Government's policy of including the Two Salient Requirements in direct land grants to non-profit-making private hospitals, the ExCo could decide on its own as to whether these Requirements should be included based on the circumstances of each case;

- the Lands D could not trace the reasons why the two Salient Requirements were not included in the land grants to some non-profit-making private hospitals, as it could not find the records which could explain such exclusion. There was also no record indicating that the Lands D had reminded the FHB and/or the DH to include the Two Salient Requirements in the land grants to non-profit-making private hospitals; and

- to ensure that future policy decisions made on land grant conditions for private hospitals were strictly and consistently applied and to avoid missing the opportunities to include any mandatory land grant condition in the land lease which was omitted from the land lease in the first place, the Lands D would take steps to facilitate better coordinated action among B/Ds in the drafting and approving of PTGs.

9. On the responsibilities between the Lands D and the B/Ds in ensuring the compliance of land grant conditions by the grantees, the **Director of Lands** explained that:

- routine inspection was conducted by the sponsoring B/Ds which had close contact with the grantees; and

- where the sponsoring B/Ds had queries on whether certain activities carried out at or arose from the land grant sites were permissible under the land grant conditions, the Lands D would follow up and/or seek legal advice, and take lease enforcement actions, such as taking back the land from the grantees as appropriate.

10. **Dr Constance CHAN Hon-yee**, the **Director of Health**, supplemented that conditions in the land lease of non-profit-making private hospitals specifying that they were subject to the satisfaction/approval of the Director of Health, such as the provision of free or low-charge beds, had been included in the DH's inspection programme of private hospitals. As regards the compliance with other conditions in the land lease which did not fall within the remit of the DH, if the DH had doubts or had received complaints about their compliance, the DH would refer the matters to the Lands D for follow-up.

11. The Committee asked the Secretary for Development whether he agreed that the Development Bureau ("DEVB") should be held accountable for not including the Two Salient Requirements in some of the land grants made to private hospitals.

12. **Mr Paul CHAN Mo-po**, the **Secretary for Development**, responded that:

- there was no question of the DEVB shirking their responsibility for the exclusion of the Two Salient Requirements from some of the direct land grants made to private hospitals. Staff of the DEVB and the Lands D had endeavoured to trace the reasons for the exclusion, but to no avail; and

- it was possible that if the FHB and the DH had not included certain conditions in the draft land lease, the Lands D might omit to include the same in the land lease submitted to the ExCo for approval.

13. The **Director of Lands** supplemented that:

- not all of the direct land grants, which did not contain the Two Salient Requirements, made to private hospitals were without any information on the exclusion;

- in the case of land grant ("LG") 2 to Hospital B, the ExCo might have considered the views of the DH made in 1962 that the PTG should not require a percentage of free beds because "it had not been recent practice to require a percentage of beds to be free, but an assurance will be required that the majority of beds should be low cost" in deciding that the PTG should only contain the "profits/surplus plough-back" requirement and not the "free or low-charge beds" requirement; and

- in the case of LG5 to Hospital D, the "profits/surplus plough-back" requirement was originally contained in the PTG approved by the ExCo in 1959, but the requirement was modified in 1983, as approved by the ExCo, to the effect that there should be no distribution of profit derived from the hospital block on the site and the hospital could apply all such profits to charitable purposes of the grantee with the exception of any evangelical or ecclesiastical purposes.

14. The **Secretary for Food and Health** supplemented that the reason why the "free or low-charge beds" requirement was not included in the land grant to Hospital B might be due to the fact that the hospital was relatively small providing only 40 to 45 beds. Hence, it was considered that merely providing just a few free or low-charge beds could not benefit a wider section of the public.

15. The Committee noted from Table 3 in paragraph 2.12 of the Audit Report that there were a few opportunities for the FHB and the DH to include the Two Salient Requirements in LG3 to Hospital C and LG7 to Hospital E when the leases of these land grants were being considered for extension for another 50 years to expire by 30 June 2047. The Committee asked the FHB and the DH why they had not done so.

16. The **Secretary for Food and Health** responded that:

- although the FHB and the DH were aware that the Two Salient Requirements should be included in the land grants for non-profit-making private hospitals, the reason for renewal of the leases of LG3 to Hospital C and LG7 to Hospital E on the existing conditions without the inclusion of these two Requirements might be due to the fact that the FHB and the DH considered it more important to align with the spirit of the Sino-British Joint Declaration 1984 and the prevailing Government's stance to ensure Hong Kong's smooth transition to the People's Republic of China's sovereignty on 1 July 1997;

- there was no record that the FHB and/or the DH had sought any legal or constitutional advice before coming to the above decision; and

- no reasons could be traced from the existing papers and documents as to why the Two Salient Requirements had not been included in LG3 to Hospital C and LG7 to Hospital E.

17. The Committee was of the view that the FHB and the DH could have taken the opportunity to include the Two Salient Requirements in LG3 to Hospital C and LG7 to Hospital E when the leases of these land grants were being considered for extension prior to 1 July 1997 on the basis of the following:

- according to the Sino-British Joint Declaration 1984, all leases of land granted by the British Hong Kong Government not containing a right of

renewal that expired before 30 June 1997, except short term tenancies and leases for special purposes, might be extended if the lessee so wished for a period expiring not later than 30 June 2047 without payment of an additional premium. As PTGs granted for non-profit-making hospitals were special purpose leases, their extension should be considered on a case-by-case basis; and

- it was mentioned in the memoranda from the Chief Estate Surveyor/Estate Management (Regrant Section) to a distribution list (including the Director of Hospital Services) on two proposed lease extensions dated 23 February 1990 and 28 January 1991 (in ***Appendices 27 and 28***) that although the leases would be extended on the existing conditions by means of the simplified extension document, "*certain basic and essential conditions will be amended/inserted where there appears to be serious defect in the existing lease*". Given that the inclusion of the Two Salient Requirements in the land grants to non-profit-making private hospitals was Government's policy, these Requirements should fall within the meaning of "basic and essential conditions" referred to in the memoranda.

18. The **Secretary for Food and Health** agreed that the FHB and the DH could have included the Two Salient Requirements in the leases of LG3 to Hospital C and LG7 to Hospital E when the leases of these land grants were being considered for extension prior to 1 July 1997.

19. The **Director of Health** supplemented that:

- the leases of LG3 to Hospital C and LG7 to Hospital E had been classified as a lease for special purpose under the New Territories Leases (Extension) Ordinance (Cap. 150);

- in the two memoranda referred to in Appendices 27 and 28, the officials on the distribution list, including the Director of Hospital Services, were invited to consider the proposed modifications to the leases contained in Annex C to the memoranda which did not include the Two Salient Requirements; and

- from the reply given by the Director of Hospital Services to the Chief Estate Surveyor/Estate Management (Regrant Section) on a proposed

lease extension dated 22 April 1991 (in ***Appendix 29***), it appeared that considerations were only given as to whether certain special conditions contained in the lease had been complied with by the grantee.

20. The Committee expressed concern about the lack of coordination between the DH and the Lands D in ensuring that the Two Salient Requirements were incorporated in the land grants to non-profit-making private hospitals. The Committee asked about the measures which would be taken by the DH and the Lands D to ensure that the Two Salient Requirements were always included in the direct land grants to non-profit-making private hospitals in future.

21. The **Secretary for Food and Health** responded that:

- the FHB and the DH would take the opportunities to include the Two Salient Requirements in those land grants which did not contain these Requirements when the grantees applied for lease renewal, lot extension or lease modification to cope with any hospital expansion or redevelopment;

- to better serve the interests of the public, the Government conducted a review of the land disposal policy and strategy for private hospital development in 2010. In January 2011, the ExCo approved the adoption of a set of minimum requirements for new private hospitals to be developed on new Government sites. These minimum requirements covered aspects such as land use, date of commencement of operation, bed capacity, service scope, packaged charge and price transparency, service target, service standard, and reporting;

- in April 2012, the Government put out two of the four Government sites reserved for new private hospital development for open tender. In the open tender, a two-envelop approach, with greater emphasis on the quality of the service provision than on land premium, was adopted. Specifically, the service provision proposal, which would be evaluated against a pre-defined marking scheme by an assessment panel comprising members from relevant B/Ds, carried a weighting of 70%; whilst the land premium carried a weighting of 30%. The tenders for these two reserved sites were closed in late July 2012. It was expected that the tender results would be announced in the first quarter of 2013; and

- having regard to the experience of these tender exercises, the responses of the market and the aspirations of the community, the FHB would consider whether the new policies for private hospital development would need to be revised/fine-tuned before reporting to the ExCo.

22. The **Secretary for Development** agreed that there was room for improvement between the coordinated actions of the Lands D and the DH to ensure that the two Salient Requirements were included in the direct land grants to non-profit-making private hospitals. The **Director of Lands** supplemented that:

- in drafting land grants and in handling lease modification in future, the Lands D would remind the DH to include essential requirements, such as the Two Salient Requirements, in the leases; and

- in the enforcement of conditions of PTGs, including those of the direct land grants for private hospitals, consideration would be given to the drawing up of a protocol setting out the respective responsibilities of the Lands D and the relevant B/Ds.

23. The Committee asked whether the FHB and the DH only became aware of the omission of the Two Salient Requirements in some of the direct land grants to non-profit-making private hospitals during the Audit review conducted in early 2012.

24. The **Secretary for Food and Health** responded that the DH had stepped up its monitoring of private hospitals' compliance with the land grant conditions prior to the Audit review. For instance, the DH had introduced in December 2010 a new arrangement of requesting private hospitals to submit, when applying for hospital re-registration, the hospital auditors' certifications of compliance with all of the financial-related requirements in the land grant conditions.

25. As the DH was empowered under the the Hospitals, Nursing Homes and Maternity Homes Registration Ordinance (Cap. 165) to regulate private hospitals, the Committee asked whether the FHB had explored the feasibility of requiring those private hospitals whose land grants did not contain the "free or low-charge beds" requirement to provide free or low-charge beds.

26. The **Secretary for Food and Health** assured members that if the land grants to non-profit-making private hospitals did not contain the "free or low-charge beds" requirement, the FHB and the DH would use administrative means to request these private hospitals to provide free or low-charge beds.

27. The Committee noted from paragraph 2.16 of the Audit Report that although Hospital F was required under the land grant conditions to provide free or low-charge beds, LG8 to Hospital F had not defined the number of such free or low-charge beds to be provided, such as "not less than 20% low-charge beds in the hospital". Instead, Hospital F was only required to provide free or low-charge beds and services as when required by the Director of Health to his satisfaction. The Committee further noted from paragraph 2.19(b) of the Audit Report that the Lands D had suggested in its first draft of the land grant conditions to Hospital F to include the "20% low-charge beds" and other 1981 requirements. In the light of this, the Committee asked the Secretary for Food and Health why the "free or low-charge beds" requirement had not been well defined in the land grant to Hospital F which could be expanded to provide 300 or more hospital beds.

28. The **Secretary for Food and Health** explained that:

- as the Government was in the process of reviewing the land policy, including the land grant conditions, for private hospital development referred to in paragraph 21 above when considering the land grant conditions for LG8 to Hospital F, the FHB had therefore decided not to define the "free or low-charge beds" in the land grant which came into effect in June 2010, so as to allow flexibility for inclusion of other additional new conditions when the aforesaid review had been finalized; and

- in view of the practical difficulties encountered in the implementation of the "20% low-charge beds" requirement and in monitoring its compliance, it was the Government's intention to abolish the "20% low-charge beds" requirement in future land grants which was to be replaced by other alternative requirements, such as packaged charge for the middle class, alongside other new conditions, such as through hospital accreditation on a continuous basis and price transparency, to ensure service quality.

29. The Committee considered that the FHB should obtain the ExCo's approval for deviating from the "20% low-charge beds" requirement stipulated in the 1981 requirements on direct land grants to non-profit-making private hospitals, as the new land policy had not yet been approved by the ExCo until January 2011. The Committee was concerned that because the FHB had not specified how the "free or low-charge beds and services", and the extent, were to be provided, the existing land grant provisions had left much leeway for Hospital F to assign and use the beds at its sole discretion, albeit subject to the DH's satisfaction.

30. The **Secretary for Food and Health** responded that with hindsight, the FHB should have sought prior approval from the ExCo for the deviation.

31. According to paragraph 2.23(a) of the Audit Report, Audit considered that the FHB and the DH needed to specify the Government's requirements clearly for provision of "free or low-charge beds and services" in LG8 to Hospital F and explore whether such provision should be replaced by the 2011 minimum requirements (such as the provision of standard beds at packaged charges) set out for new private hospitals. The Committee asked whether, and if so, what actions had been taken by the DH in this regard.

32. The **Secretary for Food and Health** said that he agreed with the Audit recommendations set out in paragraph 2.23 of the Audit Report to take action on the following:

- to specify the Government's requirements clearly for provision of "free or low-charge beds and services" in Hospital F and to explore whether the "low-charge beds and services" condition should be replaced by the 2011 minimum requirements (such as the provision of standard beds at packaged charges), taking into account the Audit's observations in Part 3 of the Audit Report on the DH's enforcement of the land grant conditions;

- to clarify the legal position on whether it was feasible for the Government to impose other additional requirements, such as the 2011 minimum requirements, on the operation of Hospital F through the use of the "Compliance with prevailing policies" condition in the land lease; and

- to put in place a proper mechanism to monitor the effective implementation of the "low-charge beds and services" or "packaged charges" requirement and any other additional requirements imposed on Hospital F as mentioned above.

33. The **Director of Health** supplemented that legal advice would be sought on whether there was legal backing in the land grant to Hospital F to require the hospital to implement the "20% low-charge beds" requirements. Pending outcome of the legal advice, the DH would discuss with Hospital F on the possibility of setting aside 20% of the total number of beds in the hospital as low-charge beds.

C. Monitoring and enforcement of land grant conditions

Provision of free or low-charge beds

34. According to paragraph 3.11(a) of the Audit Report, free beds should have been provided by Hospital D on LG5 since the 1960's. However, although the land grant had stipulated that Hospital D should furnish annually to the DH a statement indicating the total number of first, second and third class paying patients treated, and the number of in-patients treated free, Audit found that there was no reporting of these statistics. The DH did not make any enquiry until April 2012 when Audit questioned whether the 20 free beds had really been provided. In the same month, the DH also enquired the Lands D on whether the "20 free beds" requirement was still in force. The Committee asked why the DH only started to make enquiry with Hospital D and the Lands D in April 2012 on the provision of free beds in Hospital D.

35. The **Director of Health** explained that:

- when the DH took over the regulation of private hospitals from the former Medical and Health Department ("M&HD") in December 1991, it was not a standard practice for the former M&HD to conduct inspection of private hospitals or to monitor the provision of free beds. Hence, the DH was not aware of the land grant condition for LG5 to Hospital D regarding the provision of 20 free beds until April 2012 when Audit questioned whether the 20 free beds had really been provided; and

- the DH had started to monitor the provision of 20 free beds in Hospital D on LG5 site, after the Lands D had confirmed in May 2012 that 20 free beds should be provided by Hospital D under the land grant conditions. Specifically, the DH would require Hospital D to devise a scheme for providing free beds on LG5, including ways to maximize the usage of these beds which only ranged from 17% to 24% from 2007 to 2011.

36. The **Director of Health** further said that:

- the DH had all along been monitoring the provision of low-charge beds by Hospital D on LG6 site; and

- in September 2012, the DH had incorporated the land grant conditions in its checklist for inspection of private hospitals and in the questionnaire for completion by private hospitals applying for licence renewal.

37. The Committee pointed out that it appeared that the DH had only started to step up monitoring of the provision of low-charge beds in Hospital D on LG6 site since 2008, having regard to the fact that Hospital D had only started to report the utilization of low-charge beds on LG6 site to the DH since 2008 as stated in paragraph 3.11(d) of the Audit Report.

38. The Committee further noted from paragraph 3.11(d) of the Audit Report that the low-charge beds in Hospital D on LG6 site had very low utilization rates (1% in 2008 and ranging from 23% to 45% during 2009 to 2011), as compared with 98% to 113% of other regular beds available in the whole hospital. The Committee asked why the DH had not entered into mutual agreement with the grantee of Hospital D on how to use the low-charge beds, which the DH was obliged to do so under the land grant conditions, so as to improve the usage of these beds.

39. The **Director of Health** responded that:

- the DH had all along been liaising with Hospital D to step up publicity on the provision of low-charge beds in the hospital to patients and visiting doctors;

- the reason why the usage of low-charge beds had remained low was due to the fact that patients still considered the medical fees high as compared to using public hospital beds. Apart from paying a daily rate of $100 per bed, patients using low-charge beds had to pay other hospital charges, albeit at a discounted rate; and

- although the DH had not entered into agreement with Hospital D on how to use the low-charge beds, this did not mean that the DH had not enforced the land grant condition that the Director of Health and the Chief Executive of the Hospital Authority ("HA") might utilize the low-charge beds provided that the patients using such beds should not be chronic long term cases and the Government would pay the fees for such beds. A case in point was that during the outbreak of swine flu in May 2009, Hospital D agreed to provide 60 low-charge beds for convalescence patients referred by the HA if required.

40. As stated in paragraph 3.11(f) of the Audit Report, in January 2012, Hospital D informed the DH of the criteria that patients must meet for admission to low-charge beds. The Committee queried whether this meant that the hospital could decide on its own the criteria for admission to low-charge beds or that the DH had not monitored how such criteria should be set in order to benefit the public.

41. The **Secretary for Food and Health** responded that there was no question of Hospital D deciding on its own the criteria for admission to low-charge beds or that the DH had not monitored how such criteria should be set in order to benefit the public. A case in point was that one of the three admission criteria to low-charge beds in the hospital, i.e. "those in possession of a medical insurance policy would also be entertained", was suggested by the DH for incorporation into the admission criteria.

42. On the question of how the DH had monitored the compliance with the low-charge beds by Hospital D, the **Director of Health** said that the DH examined the hospital bills for discharged cases to ensure that the following land grant conditions had been complied with:

- not less than 20% of the total number of beds provided should be low-charge beds;

- the daily maintenance charge for the low-charge beds should not exceed the maximum charges of the general ward scale in public hospitals: this was to cover beds, food and general services including nursing; and

- other hospital charges (for the 20% low-charge beds), such as charges for operating theatres, laboratory tests, X-ray tests and drugs should not exceed 50% of similar charges applied to second-class beds of the said hospital.

43. At the request of the Committee, the **Director of Health** provided an account on the monitoring of the land grant condition of LG6 by Hospital D of providing low-charge beds after the public hearing (in ***Appendix 30***).

44. On the question of whether the DH had issued any regulatory letter to Hospital D for the under-utilization of its low-charge beds, the **Secretary for Food and Health** replied in the negative. He further said that:

- due to the low utilization of free and low-charge beds, the Government would endeavour to replace the requirement of providing free or low-charge beds included in the land leases of existing non-profit-making private hospitals by the requirement of providing standard beds at packaged charges when the grantees of these land leases applied for lease renewal in future; and

- in the meantime, the FHB and the DH would assist Hospital D and Hospital F in optimizing the use of free or low-charge beds. For instance, the DH was in discussion with the HA on setting out the procedures for referring needed patients to Hospital D and Hospital F.

<u>Profits/surplus plough-back requirement</u>

45. The Committee noted from paragraph 3.13 of the Audit Report that although four private hospitals on PTG sites, i.e. Hospital B, Hospital C, Hospital D and Hospital F, had achieved surplus from their hospital operations in recent years, the DH had not timely adjusted its mode and degree of monitoring. In particular, with significant surplus being achieved by a few of these private hospitals, the DH had not effectively monitored the hospitals/grantees' financial affairs to ensure their compliance with the "profits/surplus plough-back" requirement in the land grants. The Committee further noted from paragraph 3.6 of the Audit Report that the DH

introduced a new measure in December 2010 requesting private hospitals to submit, when applying for hospital re-registration, auditors' certification confirming that the hospitals had complied with all the financial-related requirements in the land grant conditions.

46. The Committee was concerned that due to the fact that the DH had only started to require private hospitals on PTG sites to submit auditors' certification confirming that they had complied with all financial-related land grant conditions in December 2010, substantial surplus/profits derived from the four private hospitals that should have been used exclusively for hospital improvement or extension might have been significantly reduced through the following means:

- payment of licence fees of $303 million in 2009 and 2010 by Hospital D to the grantee. The licence fees represented 22.7% of the hospital's surplus for the two years;

- payment of donations of $180 million in 2009 and 2010 by Hospital D to the grantee. The donations represented 13.5% of the hospital's surplus for the two years;

- payment of donations of $22.8 million in 2009 and 2010 by Hospital F to a related organization. The donations represented 12.8% of the hospital's surplus for the two years; and

- provision of hospital-related services in the hospital premises of Hospital B and Hospital D by profit-making related companies. Profits derived by these companies were not included in the hospitals' profits/surplus (except dividends on investments).

47. The Committee considered that as Hospital B, Hospital D and Hospital F were not operated by the grantees but by related organizations with separate legal entities as stated in paragraph 3.12 of the Audit Report, the risk of reducing the hospitals' surplus available for ploughing back for the hospitals' use through licence fees/donations paid to grantees could have been avoided if the DH had monitored effectively both the hospitals' and the grantees financial affairs to ensure their compliance with the "profits/surplus plough-back" requirement.

48. The **Director of Health** responded at the public hearing and elaborated in her reply dated 17 December 2012 to the Committee (in ***Appendix 31***) that:

- prior to December 2010, private hospitals were only required to submit audited accounts when applying for re-registration and no examination had been conducted by the DH staff on the hospitals' compliance of the financial-related land grant conditions. The DH had only started to enforce the "profits/surplus plough-back" requirement on private hospitals on PTG sites in December 2010 by requesting private hospitals to provide auditors' certification of compliance with financially-related clauses in the land grant conditions for the year ended 31 December 2010;

- based on the hospitals' recent audited accounts for the year ended December 2011 submitted to the DH, the DH had been liaising with the Lands D to seek clarifications on the following:

  (a) how the profit distribution of hospitals occupying multiple land lots with various profits/surplus plough-back requirements should be handled. Although Hospital C was operating on LG3 and LG4, only the lease of LG4 contained the "profits/surplus plough-back" requirement. In the case of Hospital D, the hospital was operating on LG5, LG6 and one self-purchased land and only the lease of LG6 contained the "profits/surplus plough-back" requirement; and

  (b) whether it was permissible under the land grant conditions for private hospitals on PTG sites to make donations to the grantee and/or parent/related organizations out of surplus derived from services provided on the PTG sites;

- in cases where the grantee and the hospital were separate entities with transactions between the two, the DH would request the grantee to provide information on all its incomes and expenditures related to the operation of the hospital and to confirm whether the surplus, if any, was ploughed back to the improvement and extension of the hospital as required by the land grant conditions;

- in respect of the business arrangements which private hospitals on PTG sites had entered into with third parties for the provision of hospital services, the DH had reminded all private hospitals on PTG sites and grantees to observe their land grant conditions and to seek the approval of the Lands D as required; and

- due to the complexity of the issues involved, some of the follow-up actions, including taking legal advice, would take two to three years to complete.

49. The **Secretary for Food and Health** supplemented that to eradicate the risk of hospitals' surplus available for ploughing back for the hospitals' use being reduced through licence fees/donations paid to grantees, grantees of private hospitals on PTG sites wishing to transfer the whole or part of the operation of the hospitals to other organizations would in future need to first seek prior approval from the FHB and the DH. The FHB and the DH would incline to approve only the transfer of non-medical services, such as security and catering, from the hospitals to other organizations.

50. The Committee noted from paragraph 3.8 of the Audit Report that in July 2012, the DH further sought clarification from the Lands D on the application of the "profits/surplus plough-back" requirement in the land grants to the whole hospital or to only those parts of the hospital on PTG sites. In mid-September 2012, the Lands D provided the DH with its advice on the matter. The Committee asked the Director of Lands to shed light on such advice.

51. The **Director of Lands** responded that:

- according to the legal advice, the general approach would be to look at the relevant terms in each individual case, where appropriate, taking into account also the matrix of surrounding facts of the land grant and/or advice including expert advice in relation to terminology and arrangement, for instance, in relation to accounting matters relevant to the case, and policy intention on the issues;

- subject to the considerations above, insofar as compliance with the financial-related requirements in the relevant hospital land grant conditions were concerned, each relevant lease condition should be applied to the lot or portion of the lot in question carrying the particular lease condition and be interpreted accordingly. Therefore, one possible treatment for assessing compliance with the "profits/surplus plough-back" requirement was that the profits/surplus derived from the hospital (where hospital operation straddled two or more lots with different lease conditions) should be suitably apportioned amongst the lots, or portions of the lots, in question;

- the treatment mentioned above was by no means exhaustive or intended to be binding on Government's position in relation to any cases under investigation or those which might necessitate investigation; and

- the DH and the Lands D were working closely side-by-side and would seek further legal advice as necessary in the investigation.

52. As stated in paragraph 3.7 of the Audit Report, Audit noted that the DH had not defined in its requests to the private hospitals the specific financial-related requirements which individual hospitals needed to comply with. As a result, the auditors' certifications so submitted by the private hospitals in 2011 could not provide adequate assurance that individual hospitals had properly complied with all the financial-related land grant conditions. Without specifying clearly the requirements, the auditors' certifications might fall short of the DH's expectations. The Committee asked whether, and if so, what progress had been made by the DH to rectify the situation.

53. The **Director of Health** responded that the DH had accepted Audit's recommendations as set out in paragraph 3.9 of the Audit Report. The DH had in September 2012 requested Hospital B, Hospital C, Hospital D and Hospital F to provide auditors' certification for the year ended 31 December 2011 of compliance with the "profits/surplus plough-back" requirement as stipulated in the land grant conditions.

54. Regarding the financial-related land grant conditions, the Committee suggested that the DH should (i) specify more clearly the requirements which the auditors appointed by the private hospitals should audit as soon as practicable; (ii) meet with the auditors prior to conducting annual inspections to private hospitals on PTG sites; and (iii) devise a standardized form for auditors to complete in the long run. The **Secretary for Food and Health** agreed to consider.

<u>Site development not strictly in accordance with land grant conditions</u>

Social centre for the elderly and day hospital with rehabilitation facilities required

55. As stated in paragraph 3.16 of the Audit Report, LG4 was granted to Hospital C for operating a non-profit-making medical, health and welfare centre which would provide a "social centre for the elderly" and a day hospital "with …

rehabilitation facilities" for which the "free or low-charge bed" requirement was not applicable. Paragraph 3.17 of the Audit Report further stated that as it transpired, as at September 2012, LG4 was used by Hospital C as a hospital block providing, amongst others, 112 hospital beds and including three-storey wards with first-class and second-class rooms. According to the DH and the Lands D records, and confirmed by a site visit paid by Audit on its own in mid-August 2012, Audit could not find prima facie any "social centre for the elderly" or any day hospital "with … rehabilitation facilities" in the hospital block as stipulated in the land grant. The Committee asked the Director of Health whether the DH had sought the advice of the Lands D on whether the land grant conditions had been breached if the relevant facilities were not available.

56. The **Director of Health** explained that:

- the monitoring of Hospital C's compliance with the land grant conditions of LG4 was carried out in accordance with the lease modified in June 2002 which allowed for change of the "type of building" on the PTG site at nil premium. As the relevant clause contained "other facilities may be approved by the Director of Health", the DH had therefore approved Hospital C's application for providing 109 hospital beds on LG4 site in 2008; and

- the provision of the "social centre for the elderly" was under the remit of the Social Welfare Department ("SWD").

57. In the same letter dated 17 December 2012 to the Committee, the **Director of Health** informed the Committee after the public hearings that the DH would consult the Lands D on the land lease conditions of LG4 and would request Hospital C to take remedial measures where appropriate.

58. The **Director of Lands** supplemented that:

- Hospital C, as the grantee, was liaising with the Director of Social Welfare on reprovisioning the "social centre for the elderly" (now operating at another location) in the hospital block on LG4 site. The Lands D would keep in touch with them and process any building plans expeditiously under the terms of the lease, taking advice from the relevant departments with a view to early reinstatement of the facilities to their satisfaction; and

- having regard to the recent discussions amongst the grantee and the departments concerned, the Lands D expected that the relevant building plans and the reinstatement exercise to be finalized in good time.

59. The Committee received a submission from Hospital C (in ***Appendix 32***) in which it stated in paragraphs 7 and 11 of the submission that both the social centre for the elderly and the day hospital with rehabilitative facilities would be reprovisioned in the new hospital block on LG4 site by the end of 2013, upon completion of the relevant construction works.

60. According to paragraph 3.24 of the Audit Report, the lease modification to LG4 was only executed some three years after the new hospital block on LG4 site commenced operation. The Committee asked about the reason(s) for such delay and what measure(s) would be taken by the Lands D to avoid such incident from recurring.

61. The **Director of Lands** explained that:

- the reason why the lease modification of LG4 was executed some three years after the new hospital block commenced operation was partly attributable to the technical complications of constructing a connection bridge between LG3 and LG4 and partly to the lack of a sense of timeliness within the Lands D when processing the lease modifications of the two land grants. A chronology of events for lease modifications of LG3 and LG4 and that for processing of building plan submission since 2005 are in ***Appendices 33 and 34*** respectively; and

- whilst the Lands D had been making conscious gate-keeping efforts since at least late 2009 in vetting the relevant building plans and making sure that the facilities required under lease were provided, with hindsight the Lands D could have started the serious vetting earlier and on a provisional basis, pending finalization of the related lease modifications.

Subleasing of hospital premises

62. Hospital E was established on LG7 with a site area of 1 600 m^2. In 1993, the grantee of Hospital E agreed with a third party charitable organization (Organization E) for the latter to take over the administration of Hospital E, which occupied a portion of the site (the hospital part). No rent was charged. The agreement was effective from 1 April 1993. In the same year, the grantee applied for the Government's consent to letting the hospital part of the site to Organisation E. Given that the DH had confirmed no objection to the granting of the waiver which was included in the lease of LG7, the Lands D considered and decided, after consulting its policy bureau, that submission to the ExCo was not warranted. Thus, it approved, at nil fee, a temporary waiver of the alienation restriction in February 1996 and two extensions of the waiver, with the last waiver expired in March 2005.

63. According to paragraphs 3.34 and 3.35 of the Audit Report, Audit considered the continued operation of Hospital E on LG7 by Organization E without a temporary waiver on an alienation restriction contained in the land lease and the continued subletting by Organization E of the hospital premises to medical centres were not allowed under the land lease. Up to July 2012, there had not been further progress on renewal of the temporary waiver. The Committee asked the Director of Lands about the latest situation on the matter.

64. The **Director of Lands** explained that:

- in processing the renewal of waiver for LG7, it was necessary to ascertain whether the waiver would be confined to the alienation involving Organization E or whether the operation of the seven medical centres on LG7 site would also constitute alienation which was restricted under the land lease. In this regard, up till late 2009, there were still residual doubts on whether one of the seven service agreements for the seven medical centres operating on LG7 site amounted to a sublease which was not allowed under the land lease;

- the grantee's solicitors were requested in November 2009 to provide further information, The further information clarifying the relationship between Organization E and the 7th medical centre and the use of the medical centre by the service consultants was provided to the Lands Department in September 2012. According to the legal advice

obtained, the service agreement for the 7th medical centre did not construe as a sublease;

- in October 2012, the Lands D proposed a temporary waiver of the alienation restriction for a term of six years with retrospective effect from 1 April 2005; and

- upon receipt of the grantee's acceptance of the terms of the wavier in November 2012, the Lands D was preparing the waiver letter for issuance to the grantee within December 2012.

65. According to paragraph 3.38 of the Audit Report, Audit suggests that the Lands D and the DH should clarify if similar situations as in Hospital E also exist in other private hospitals that operate on PTG sites. The Committee asked whether, and if so, what appropriate follow-up actions had been taken.

66. The **Director of Health** informed the Committee in her reply dated 17 December 2012 to the Committee that the DH had reminded all private hospitals and grantees to observe their land lease conditions, including that all incomes generated from the operation of a third-party company in the hospital premises should be regarded as incomes of the hospitals and/or the grantees, and to seek the approval of the Lands D as required.

D. Sale of land for private hospital development

67. Hospital G is a profit-making private hospital which commenced operation in 1994 in District G. According to the first tender in 1981 for developing a hospital in District G, a site area of 1.922 hectares ("ha") was provided for erecting a hospital of "not less than 400 bed, but not more than 600 bed" together with other ancillary facilities and staff quarters. According to paragraph 4.5 of the Audit Report, as no bids were received, the then M&HD informed the then land authority in October 1981 that:

- providing 1.922 ha site for building a hospital of 200 to 400 beds was deemed appropriate; and

- it was acceptable to reduce the minimum number of beds from 400 to 200 with a possibility of phased development into 400 beds at some later date.

In late 1981, in the tender re-issued, the then land authority and the then M&HD reduced the minimum number of beds required to be provided by the hospital from 400 to 200. The Committee asked about the reason for reducing the minimum number of beds from 400 to 200 in the tender re-issued and why the site area for erecting a hospital was not correspondingly reduced.

68. The **Secretary for Food and Health** explained that the reason for reducing the minimum number of beds from 400 to 200 for erecting a hospital in District G was to allow flexibility for the tenderer to develop the site by phases.

69. The **Director of Health** supplemented that:

- as no bids were received in the first tender, the then Sha Tin District Officer, after exchanging views with the relevant stakeholders, conveyed to the then M&HD that if the minimum number of beds for erecting a hospital in District G could be reduced from 400 to 200, the chance of a successful tender would increase; and

- the provision of a site area of 1.922 ha for erecting a hospital in District G to provide a minimum of 400 beds was made in accordance with the then code of planning which provided that a standard of 50m^2 per bed should be adopted for hospitals.

70. The **Director of Lands** pointed out that the maximum number of 600 beds required to be provided by the hospital in District G remained unchanged in the tender re-issued. The reason for including a maximum number of 600 beds was that one interested party to the first tender indicated that they could provide 600 beds on the site.

71. The Committee noted from paragraph 4.10 of the Audit Report that Hospital F, a non-profit-making private hospital, was granted PTG sites (LG8 and LG9) of 0.79 ha for developing a hospital which provided not less than 300 beds. The Committee queried whether providing a site area of 1.922 ha for developing a 400-bed hospital was excessive.

72. The **Director of Lands** reiterated the views of the Director of Health that the provision of a site area of 1.922 ha for developing a 400-bed hospital was made in accordance with the then code of planning which provided that a standard of 50m^2 per bed should be adopted for hospitals.

73. The Committee noted from item (e) in Table 5 in paragraph 4.8 of the Audit Report that the operator of Hospital G ("Operator G") applied to the Lands D in August 2001 for a lease modification to allow the carving out of the "rezoned" portion and for a land exchange for the re-granting of a new residential lot. The Committee queried whether the Lands D should have approved such lease modification, as it appeared that Operator G had planned at the outset to use the whole or part of the hospital site for residential development. As stated in item (b) in Table 5 in paragraph 4.8 of the Audit Report, Operator G had applied to the Lands D for developing the whole site in 1986 and a portion of the site again in 1988 for residential development Since 1994 (up to April 2000), Operator G applied repeatedly for changing part of the hospital site to residential use. Paragraph 4.11 of the Audit Report also stated that all hospital building and related facilities of Hospital G were provided on one side of the hospital site, taking up only 54% of the total site area.

74. The **Director of Lands** responded that:

- the reason why Operator G had applied to the Lands D for developing the whole site for residential purposes in 1986 and a portion of the site again in 1988 was because Operator G could not then find an operator to run the hospital and did not have enough financial resources to develop the hospital. The ExCo rejected Operator G's request to develop the whole site for residential purposes, as the hospital had yet to be constructed then and there was a need for developing a hospital in District G. As Operator G could eventually find enough financial resources to develop the hospital, Hospital G finally commenced Phase 1 operation in 1994;

- it was not fair to say that Operator G had planned at the outset to use the whole or part of the hospital site for residential development, merely on the basis that all hospital building and related facilities of Hospital G were provided on one side of the hospital site;

- Operator G had followed the due process by submitting a rezoning request to the Town Planning Board ("TPB") and had paid the premia

for lease modification and land exchange which were $0.31 million and $609.43 million respectively; and

- to avoid providing any leeway for private hospital developers to change the use of the hospital sites for other purposes, the Government had set out stringent requirements in the two more recent tenders of the two Government sites reserved for private hospital development.

75. The **Secretary for Food and Health** pointed out that it was the usual practice of hospitals to develop on one side of the sites, so as to allow flexibility for further development in future.

76. The Committee asked about the criteria for assessing the bids received for the tender for erecting a hospital in District G.

77. The **Director of Lands** responded that the bids received for the tender for erecting a hospital in District G were decided by the Central Tender Board on the principle that the tender should be awarded to the highest bidder. In submitting the bids, the bidders were required to provide proof that they had the financial resources to erect the hospital. There was however no requirement in the tender that the bidders had to have experience in operating a hospital.

78. On the question of whether there was a provision in the land lease of Hospital G whereby the Lands D could regain possession of the site or any part thereof which had been left undeveloped for a long stretch of time, the **Director of Lands** replied that if Operator G had met the lease requirements to build a hospital providing a minimum of 200 beds and up to a maximum of 600 beds, there was no ground for the Lands D to regain possession of the undeveloped eastern portion of the hospital site which was sold to Operator G.

79. The Committee noted from Appendix D and item (b) in Table 5 in paragraph 4.8 of the Audit Report that Operator G had applied to the TPB in December 1998 and again in November 1999 for changing part of the hospital site to residential use. The applications were rejected. The Committee asked why the TPB subsequently agreed to the rezoning request from Operator G in June 2000, despite the fact that the DH had reservation on the matter as set out in Appendix D to the Audit Report.

80. **Miss Ophelia WONG**, the **Deputy Director of Planning (District)**, responded at the public hearing and elaborated in her letter dated 19 December 2012 to the Committee (in ***Appendix 35***) that:

- in considering the first application made under section 16 of the Town Planning Ordinance (Cap.131), the TPB noted that whilst the proposed residential development would assist in financing the capital costs of the future expansion of Hospital G, there was no sufficient justification to change the eastern portion of the undeveloped hospital site from "Government, Institution or Community" ("G/IC") and "Open Space" to residential development. The DH had no objection to the application. The DH was however of the view that the need of expansion would not be imminent unless there was a drastic change in policy over health financing in which patients would be forced to patronize private hospitals;

- in considering the second application (also made under section 16 of Cap. 131) in which Operator G proposed to expand the hospital by constructing three additional storeys above the existing hospital block to provide an additional 200 beds, the TPB noted that although the proposal was generally in line with the TPB Guidelines, there were neither unique circumstances nor strong reason to justify a departure from the planning intention. When commenting on the second application, the DH had reservation on Operator G's proposal to expand the hospital as there was no detailed data in the application in respect of the portion of the profit from the sale of flats that would be reserved for the operation costs and development of Hospital G;

- since there were local objections to the application to change the site from "G/IC" and "Open Space" to residential development, a majority of TPB members were of the view that should the proposed residential development be considered acceptable, it would be more appropriate to amend the Outline Zoning Plan so as to provide a statutory avenue for affected persons to lodge objections with the TPB. The TPB thus agreed, in rejecting the second application, to advise Operator G that should they consider that the undeveloped eastern portion of the hospital site was no longer required for hospital use, it would be more appropriate to request for a rezoning of the site for residential development;

- Operator G subsequently submitted a rezoning request to the TPB in May 2000 to change the "G/IC" and "Open Space" of the undeveloped

hospital site to residential development. The DH had no particular comments on the rezoning request, and reiterated its views given in April 2000 that the undeveloped land should be reserved for future development on hospital services in the long run as often seen in other hospital projects;

- in considering the rezoning request in June 2000, the TPB noted that:

  (a) Operator G would expand Hospital G through the construction of three additional storeys over the existing hospital block;

  (b) the undeveloped portion of the "G/IC" site was not required for the hospital expansion or for the provision of other types of "G/IC" facilities;

  (c) the proposed residential development would not generate significant adverse environmental and traffic impacts and impose significant pressure on the existing and planned infrastructure in the area;

  (d) the plot ratio of the proposed residential development was considered generally compatible with the adjacent residential developments;

  (e) the proposed residential development and the expansion of the hospital would require a lease modification and there was no impediment to such proceedings under the land administration policy; and

  (f) the rezoning would provide a proper avenue for the local residents to raise their objections;

- the TPB, after balancing all relevant factors in (e) above, agreed to the rezoning request on 30 June 2000. The amendment was later exhibited for public inspection under section 7 of Cap. 131 on 4 August 2000;

- during the exhibition period, a total of six objections were received against the rezoning of the site to residential development. When the objections were circulated for departmental comments, the Director of Health advised that her previous comments on the planning application were still valid;

- the objection hearing was held in January 2001. After considering the presentations made by the objectors, the Objection Hearing Committee ("OHC") decided to revert the zoning of the site from "Residential (Group B)" to "G/IC" and "Open Space". The amendments were then notified under section 6(7) of Cap. 131;

- during the notification period, one further objection, submitted by Operator G, against the amendment to revert the zoning of the eastern position of the hospital site from "Residential (Group B)" to "G/IC" and "Open Space" was received. Another hearing to consider this further objection was conducted in June 2001; and

- in considering the further objection, the OHC noted the Director of Health's advice that the land should be reserved for further development of hospital services in the long run as often seen in other hospital projects. After hearing the presentations of objectors/further objector and balancing all relevant factors, the OHC decided to alter its previous decision by reversing the zoning of the site from "G/IC" and "Open Space" to "Residential (Group B)" taking into account the following:

  (a) provision of hospital service in different regions was pursued by the HA in liaison with the Planning Department. According to the HA, the ratio of 5.5 beds per 1 000 persons quoted in the Hong Kong Planning Standards and Guidelines referred to a territory-wide requirement of beds that covered all types of beds both in the public and private sectors. The ratio did not reflect the requirement of hospital beds at the local district level. The HA's assessment showed that there would be a slight shortfall of about 250 general public hospital beds in the New Territories East region by 2006. The HA could not comment on the adequacy of private hospital beds as private hospitals were operated on commercial basis and their operation was totally dependent on market demand, and the HA had no plan to acquire new land in the New Territories East region to develop hospital facilities;

  (b) given its remote location and poor accessibility, the OHC considered that the site was not suitable for social welfare facilities as advised by the SWD;

  (c) Hospital G had already complied with the lease requirement for provision of hospital beds;

(d) besides, Hospital G had proposed to increase the number of hospital beds from 212 to a total of 400; and

(e) the proposed residential development was not incompatible with the adjacent residential developments and would not generate significant adverse environmental and traffic impacts.

Sections 6, 7 and 16 of the Town Planning Ordinance at the relevant time referred to in this paragraph are in ***Appendix 36***.

81. The Committee asked whether the TPB, in approving the rezoning request, was aware of the fact that Operator G would have an advantage over other land developers in that Operator G only needed to pay the premia for lease modification and land exchange at $0.31 million and $609.43 million respectively, the total costs of which might be lower if the site in question was put up for public tender for residential development.

82. The **Deputy Director of Planning (District)** responded that some members of the TPB had asked about such possible eventuality when approving the rezoning request. She however pointed out that the TPB and the Lands D operated under two separate mechanisms. Hence, whether a rezoning request complied with the land policy was not a factor which the TPB would consider in determining whether a rezoning request should be approved.

83. The **Director of Lands** supplemented that after the site had been approved by the TPB for rezoning, the applicant had to apply to the Lands D for lease modification. She further said that not all sites which had obtained the approval of the TPB and the ExCo for rezoning would automatically be allowed to change the use of the site unless the applicant agreed to the terms of the lease modification and paid the land premium.

84. The Committee asked whether the timing of approving the rezoning request from Operator G coincided with the policy of the "85 000 flats".

85. The **Deputy Director of Planning (District)** responded that past records did not show that any reference was made by the TPB to the policy of the "85 000 flats" when considering the rezoning request from Operator G. She

however said that there was a shortage of private housing flats in Hong Kong at that time.

86. At the request of the Committee, the **Deputy Director of Planning (District)** provided the number of rezoning requests handled by the TPB from 1999 to 2002 for changing the sites to residential development in her letter dated 19 December 2012 to the Committee.

87. The Committee was of the view that the Administration needed to draw lessons from this land sale transaction, which had hindered the Government from making an optimal use of the site for the original purpose of hospital development. The Committee enquired about the actions which would be taken by the Administration to prevent owners of profit-making private hospitals from applying for rezoning to change the use of the hospital site for residential development.

88. The **Secretary for Development** responded that similar incidents should not happen again in future for the following reasons. First, the Administration would be more precise in determining the size of the hospital site and in assessing the demand for service expansion. Second, strict development controls, such as total gross floor area, maximum site coverage and height, would be stipulated in the land grants of Government sites for new private hospitals.

89. The **Secretary for Food and Health** supplemented that:

- in the tenders for new private hospital development, restrictions on land use primarily for hospital services had been and would be imposed. In other words, tenderers would not be allowed to change the use of the land; and

- as land was scarce and precious in Hong Kong, the FHB and the DH would endeavour to ensure that the site sold for private hospital development would be used for its intended purposes.

E. Conclusions and recommendations

90. The Committee:

Overall comments

On direct land grants

- notes that it has been a public policy that non-profit-making private hospitals would be granted lands at nil or nominal premium in return for their agreement (i) to provide free or low-charge beds and (ii) to plough back profits or any surplus from hospital operation to improve and expand their facilities ("the Two Salient Requirements");

- expresses grave dismay and finds it inexcusable that:

  (a) the sacrifice made from the public coffers has failed to produce benefits for Hong Kong people in the ways they have been intended by the Two Salient Requirements;

  (b) such failure has been due to no other reason but the laxity and dilatoriness with which the Administration has gone about implementing the Two Salient Requirements since their pronouncement by the Executive Council ("ExCo") in 1957 and elaborated specifications in 1981; and

  (c) such laxity and dilatoriness were manifested by, inter alia, the following:

    (i) omissions to include the Two Salient Requirements in land grants made to private hospitals;

    (ii) failure to rectify such omissions when there were opportunities to do so;

    (iii) non-existence of a set of practical and practicable rules for private hospitals to follow in the implementation of the Two Salient Requirements;

    (iv) no, or no effective, effort was made to establish any, or any real, surveillance system so that compliance by private

hospitals of the Two Salient Requirements could be properly and accurately monitored and policed; and

(v) no, or no effective, co-ordination amongst relevant government departments to make sure that matters in need of follow-up would be attended to timely and with efficiency;

- acknowledges the Administration's agreement that the present situation is unsatisfactory and needs an immediate review and rectification;

- welcomes the promises and undertakings made by the Secretary for Food and Health, the Director of Health and the Director of Lands for rectification of such defects and deficiencies identified in this Report and expects to see improvements before long;

<u>On land sale</u>

- expresses grave dismay and finds it inexcusable that there had been an over-provision of land in District G for development of Hospital G. Such over-provision resulted not only in the surplus land having been left idle for years, but also gave the owner an unfair and unjustified advantage over other developers when there were subsequent negotiations with the Administration rezoning the land for residential development at a premium to be paid;

- notes the assurance given by the Secretary for Development that the Administration has learnt from the mistake. In recent and all future sale of land for development of new private hospitals, not only will there be a strict prohibition of change of use, the hospital developments will also be subject to stringent planning parameters including height restrictions, plot ratios and site coverage;

- acknowledges such assurances and urges the Administration to see to their implementation;

Specific comments

Special land grant conditions set on private hospitals

- expresses grave dismay and finds it inexcusable that:

  (a) although the Two Salient Requirements were directed as from 1957, and further elaborated in 1981, by the ExCo to be included in future direct land grants to non-profit-making private hospitals, the Audit Commission ("Audit") found that they had not always been strictly and consistently applied. As a result, the Government's intention of foregoing the land premium, so that the lower investment cost of the private hospitals could benefit a wider section of the public could not be fully realized. As shown in Table 2 in paragraph 2.10 of the Audit Report:

    (i) the "free or low-charge beds" requirement was not included in some of the direct land grants (such as LG2 for Hospital B and LG3 for Hospital C); and

    (ii) similarly, the "profits/surplus plough-back" requirement was not included in some of the direct land grants (such as LG3 for Hospital C);

  (b) the Administration could not trace the reasons why the Two Salient Requirements had been omitted in some of the direct land grants made to private hospitals; and

  (c) notwithstanding that there were a few opportunities for including the Two Salient Requirements in some of the direct land grants first made in early years, the Department of Health ("DH") and the Lands Department ("Lands D") had failed to take these opportunities to rectify the omission. Cases in point were the failure of the DH and the Lands D to incorporate the Two Salient Requirements in LG3 to Hospital C and LG7 to Hospital E when dealing with the lease extension of these two private treaty grants ("PTGs") for another 50 years to expire by June 2047;

- urges the DH and the Lands D:

  (a) to delineate clearly their responsibilities for the inclusion or continuance of the Two Salient Requirements in the terms of the PTGs made to non-profit-making private hospitals to ensure that essential requirements are always included in the lease terms in future; and

  (b) to take the opportunity to include the Two Salient Requirements in the land grants made to non-profit-making private hospitals when the grantee applies for lease renewal, lot extension or lease modification to cope with any hospital expansion or redevelopment;

- acknowledges that the DH has undertaken:

  (a) to tighten up the monitoring of private hospitals' compliance with land grant conditions pertaining to the provision of healthcare services, including the adoption of a proper checklist for compliance checking, and will work with the Lands D closely in the enforcement of land grant conditions on private hospitals; and

  (b) to explore with the grantees of those private hospitals which did not include the "free or low-charge beds" requirement in their land grants on the feasibility of providing free or low-charge beds in the hospitals;

- expresses grave dismay and finds it inexcusable that:

  (a) even with a more recent lease modification and land exchange effected in June 2010 of LG8 to Hospital F, the "free or low-charge beds" requirement was not well defined as the grantee was only required to provide free or low-charge beds and services "as when required by the Director of Health to his satisfaction". Without defining more clearly the Government's expected requirements, the condition had left much leeway for the hospital to assign and use the beds at its sole discretion and in whatever way it deems appropriate. Furthermore, the DH had not worked out with Hospital F on how the "free or low-charge beds" requirement was to be met and how the Government would monitor its effective implementation; and

(b) although the exclusion of the "20% low-charge beds" requirement from the land grant to Hospital F was a conscious decision made by the Food and Health Bureau ("FHB") in 2009, ExCo's approval had not been sought for the deviation from the requirement;

- does not accept the explanations given by the Secretary for Food and Health for excluding the "20% low-charge beds" requirement from LG8 to Hospital F: (i) in order to allow flexibility for the FHB to revise the land grant conditions once the land policy on future disposal of Government lands for new private hospital development was finalised; and (ii) because there were practical difficulties in enforcing the "low-charge beds" requirement;

- acknowledges that the Secretary for Food and Health has undertaken to seek legal advice via the Lands D on the legality of imposing new conditions on Hospital F, such as the provision of standard beds at packaged charges, through the use of the "Compliance with prevailing policies" condition available in the land lease;

- notes that:

(a) in January 2011, the Government formulated a new policy on future disposal of Government lands for new private hospital development. This included, inter alia, the decision that the Government would endeavour to replace the special condition for provision of low-charge beds included in land leases of existing non-profit-making private hospitals by the requirement of providing standard beds at packaged charges. According to the Administration, the provision of packaged charging would help enhance price transparency and provide incentive for patients to use private hospital services;

(b) with the new private hospitals to be developed on the two reserved sites under the two tender exercises in April 2012, the sponsoring department will enter into service deeds with the successful tenderers. Such service deeds will supplement the land leases and will incorporate the successful tenderers' proposals for the operation of the private hospitals, which will help the Government enforce the service-related requirements to be complied with by the tenderers; and

(c) the Secretary for Food and Health, the Director of Health and the Director of Lands have agreed with the audit recommendations in paragraph 5.10(a) to (c) of the Audit Report;

- supports the DH's suggestion that the Government should develop a protocol to facilitate coordinated action among bureaux and departments ("B/Ds") in drafting, approving and enforcing PTGs, so as to ensure that policy decisions made by ExCo will be followed through, and urges the Secretary for Development to take the lead in overseeing the development of such a protocol and disseminating the protocol among B/Ds for compliance;

Monitoring and enforcement of land grant conditions

Provision of "free or low-charge" beds

- expresses astonishment and finds its inexcusable that there were serious inadequacies in the DH's compliance programme in monitoring the private hospitals' compliance with the land grant conditions. In particular, the DH had not maintained a proper checklist for compliance checking. Such inadequacies included the following:

Provision of free beds in Hospital D on LG5

(a) the DH did not make any enquiry until April 2012 with Hospital D and the Lands D on the provision of the 20 free beds which had been imposed as a land grant condition since the 1960s. The utilization of the free beds ranged from 17% to 24% for 2007 to 2011, when the utilization of the other beds ranged from 98% to 113%. Besides, the free beds were provided at different hospital blocks and Hospital D had not designated any particular ward or bed class for such beds;

Provision of not less than 20% low-charge beds in Hospital D on LG6

(b) although Hospital D should have provided not less than 20% low-charge beds on LG6 since late 2002 after commencement of operation of the hospital block on the site, it only started to work on meeting the requirement in 2008. The low-charge beds had very low utilization rates (1% in 2008 and ranging from 23% to 45% during 2009 to 2011). Despite the low utilization rates, the DH had not taken any effective measures to optimize the use of these

beds, including consulting the Hospital Authority which is always known to be facing an acute shortage of hospital beds; and

Provision of low-charge beds in Hospital F on LG8

(c) although Hospital F was required to provide "free or low-charge beds and services" on LG8, the DH had not worked out with the hospital on how such requirement was to be met. It was only in November 2011 that Hospital F started to report that it had provided 33 low-charge beds in its Surgical Unit and Medical Unit. No information was however provided on their utilization. Besides, the DH had not verified the availability of low-charge beds in its annual and ad-hoc inspections to the hospital;

- notes that the DH has drawn up a checklist to facilitate the checking of compliance with land grant conditions, and the monitoring of compliance will be conducted alongside the processing of annual re-registration of private hospitals;

- acknowledges that the DH has undertaken:

(a) to monitor the private hospitals' compliance with land grant conditions relating to hospital services, in particular the provision of free or low-charge beds, and submission of accounts/information on bed utilization, and will make appropriate referral to the Lands D if any breach is identified;

(b) to require Hospital D to devise a scheme for providing free beds on LG5 site and to implement the scheme in the first half of 2013;

(c) to discuss with Hospital D on ways to optimize the use of low-charge beds on LG6 site;

(d) to specify the requirements for the provision of low-charge beds and services in the case of LG8 to Hospital F; and

(e) to seek legal advice on the requirements for the provision of free beds, including whether this means that patients on free beds should be waived from paying all medical fees and charges incurred in the hospital;

Profits/surplus plough-back requirement

- expresses grave dismay and finds it inexcusable that:

  (a) the "profits/surplus plough-back" requirement included in four direct land grants to four private hospitals was also not effectively enforced. Although the four private hospitals had achieved surplus from their hospital operations in recent years, the DH had not timely adjusted its mode and degree of monitoring, and had not effectively monitored the hospitals/grantees' financial affairs to ensure their compliance with the requirement. In particular, based on the hospitals' audited accounts for recent two years submitted to the DH, significant licence fees/donations had been paid by a few of the hospitals to the grantees, parent and/or related organizations as shown below:

    (i) Hospital D had paid hospital premises licence fees of $303 million in 2009 and 2010 to the grantee. The licence fees represented 22.7% of the hospital's surplus for the two years;

    (ii) in the same two years, Hospital D had also made donations of $180 million to the grantee, representing 13.5% of the hospital's surplus for the two years; and

    (iii) Hospital F had paid donations of $22.8 million to a related organization of the grantee in 2009 and 2010. The donations represented 12.8% of the hospital's surplus for the two years;

  (b) given that the above licence fees and donations paid/made to related parties, classified as related party transactions in the hospitals' accounts, will reduce the hospitals' profits/surplus available for hospital expansion or redevelopment, the DH had not made enquiry with the Lands D as to whether they were appropriate until March 2012. There were complications in that some of the hospitals might be operating on both PTG sites as well as self-purchased land and not all PTGs contained the "profits/surplus plough-back" requirement. There were further complications in that, except for LG3 and LG4 (with Hospital C as the grantee), the grantees for the other PTGs were not the hospitals themselves, but the hospitals' parent or related organizations;

(c) some hospital-related services (very often, in the form of specialist medical centres) were provided within the hospital premises on PTG sites by related companies of the grantees and/or hospitals. Given that such related companies were profit-making and maintained separate accounts from that of the grantees/hospitals, these might constitute subletting and profit-sharing arrangements by the grantees/hospitals with third parties, both of which might not be allowed under the land grant conditions;

(d) notwithstanding that most of the land grant conditions had been effective for many years, the DH had neither taken action to clarify with the FHB/Lands D on the reasonableness/propriety of the related party transactions reported in the hospitals' accounts nor requested the grantees to submit audited statements to satisfy that surplus they derived from the hospitals' operations on the PTG sites had been properly ploughed back for hospital improvement or extension in compliance with the land grant conditions. The DH had only made enquiries with the grantees/hospitals in March and August 2012 on the various related party transactions reported in the hospitals' statements of accounts;

(e) as some of the private hospitals on PTG sites are not operated by the grantees, but by related organizations with separate legal entities, the risk of reducing the hospitals' surplus available for ploughing back for the hospitals' use through licence fees/donations paid to grantees could have been avoided if the DH had monitored effectively the hospitals/grantees' financial affairs to ensure their compliance with the "profits/surplus plough-back" requirement; and

(f) although the DH introduced in December 2010 a new measure by requesting private hospitals to submit auditors' certification confirming that the hospitals had complied with all the financial-related requirements in the land grant conditions, it had not defined in its requests to the private hospitals the specific financial-related requirements which individual hospitals needed to comply with;

- acknowledges that the DH:

  (a) had in September 2012 requested Hospital B, Hospital C, Hospital D and Hospital F to provide auditors' certification for the year ended 31 December 2011 of compliance with the "profits/surplus plough-back" requirement as stipulated in the land grant conditions; and

  (b) has undertaken to:

    (i) request the grantee to provide information on all its income and expenditures related to the operation of the hospital and to confirm whether the surplus, if any, is ploughed back to the improvement and extension of the hospital as required by the land grant conditions, in cases where the grantees are not the hospitals themselves but the hospitals' parent or related organizations;

    (ii) follow up with the Lands D on rectifying the subleasing of the land lots on PTG to hospital operators who are not the grantees; and

    (iii) seek the advice of the Lands D on the handling of profits/surplus distribution of hospitals occupying more than one land lots with various profits/surplus plough-back requirements (Hospital C operates on LG3 and LG4 sites and the "profits/surplus plough-back" requirement is included only in LG4. Hospital D operates on LG5 and LG6 sites and a self-purchased land and the "profits/surplus plough-back" requirement is included only in LG6);

- urges the DH to:

  (a) review the appropriateness of allowing the grantees to transfer the administration of the hospitals to different organizations;

  (b) define what permissible activities the non-profit-making grantees/hospitals are allowed to conduct and what non-permissible activities disallowed in respect of profits derived from the hospital operations on PTG sites and similarly, what profit-sharing arrangements they can make with related and third parties;

(c) step up the monitoring of the requirement for grantees/hospitals to retain and reinvest their profits/surplus in the hospital operations, as set out in the land grants; and

(d) resolve the issues expeditiously, even though due to the complexity of the issues involved, some of the follow-up actions, for instance, with regard to the rectification of irregularities concerning profit plough-back, might take two to three years to complete;

- welcomes that it is now the stance of the FHB and the DH that grantees would in future not be allowed to transfer the administration of whole or part of the hospitals to different organizations, unless the services involved are not medically-related services, such as security and catering, and that prior approval from the DH must be obtained;

- expresses grave concern about whether the sub-licences entered by Hospital D with third parties for use of certain areas of the hospital premises on PTG sites for the provision of hospital-related services are permissible for the PTG sites under the existing land grant conditions;

- notes that the DH had reminded all private hospitals and grantees to observe their land lease conditions, including that all incomes generated from the operation of a third-party company in the hospital premises are regarded as incomes of the hospitals and/or the grantees, and to seek the approval of the Lands D as required;

Site development not strictly in accordance with land grant conditions

- expresses grave dismay and finds it inexcusable that LG4 granted to Hospital C for operating a non-profit-making medical, health and welfare centre, which would provide a "social centre for the elderly" and a day hospital "with ... rehabilitation facilities", was not developed strictly in accordance with the land grant conditions. The site was eventually used by Hospital C as a hospital block providing in-patient hospital services. Audit found that the "social centre for the elderly" and the day hospital " with ... rehabilitation facilities" were not available on the PTG site. There were various inadequacies in the way the Administration handled and monitored the land grant to Hospital C, including the following:

(a) because the site was not granted to Hospital C for operating in-patient hospital services, the land grant contained neither the

minimum number of hospitals beds that should have been provided on the site nor the requirement to provide not less than 20% low-charge beds;

(b) in 2006, Hospital C proceeded to redevelop the premises on the PTG site. The land grant condition provided that the design and disposition of any building to be erected on the lot should be subject to the Lands D's approval. However, although the hospital block on the site had commenced operation since April 2008, none of the hospital building plans (with the first plan submitted as early as November 2007) had been approved by the Lands D for compliance with the land grant conditions; and

(c) the DH and the Social Welfare Department ("SWD"), as the sponsoring departments for the PTG, should also have approved the hospital's compliance with the land grant conditions for the building plans and for the construction of the medical, health and welfare centre in accordance with the plans. However, the two departments had so far not raised any objections, notwithstanding the fact that there was neither any "social centre for the elderly" nor any day hospital " with ... rehabilitation facilities" in the hospital block on LG4. Audit has found that the SWD was not consulted on the building plans until February 2012 and the DH had so far not raised any objections on the building plans or on the usage of the site either to the Buildings Department or to the Lands D;

- notes that:

(a) the DH has undertaken to consult the Lands D on the land lease conditions of LG4 and will request Hospital C to take remedial measures where appropriate;

(b) the Director of Lands admitted that with hindsight, the Lands D could have started the serious vetting of the building plans earlier and on a provisional basis, pending finalization of the related lease modifications. Having regard to the recent discussions amongst the grantee and the departments concerned, the relevant building plans and the reinstatement exercise is expected to be finalized in good time;

(c) the SWD is prepared to collaborate with the Lands D and the DH to follow up on the provision of the "social centre for the elderly" on LG4; and

(d) according to the grantee of LG4, a social centre for the elderly and a day hospital with rehabilitative facilities will be reinstated at LG4 by the end of 2013, pending completion of the relevant construction work;

Subleasing of hospital premises

- expresses grave dismay and finds it inexcusable that in the case of Hospital E in operation on LG7, the continued operation of Hospital E on LG7 by Organization E (which is not the grantee) and its subletting of the hospital premises to medical centres operated by third parties, after the lapse of the Government waiver in March 2005, were in breach of the alienation restriction in the land lease and need to be rectified as early as possible;

- notes that the Lands D had issued a waiver to the grantee of Hospital E in December 2012, after the Lands D had clarified with Organization E that the service agreement between Organization E and one of the seven medical centres operating on the hospital premises does not construe as a sublease;

- urges the Lands D and the DH to take actions to clarify if similar situations as Hospital E also exist in other private hospitals and take appropriate follow-up include the following issues mentioned in paragraph 3.38 of the Audit Report:

  (a) whether the provision of such medical centres on PTG sites would constitute subletting which is generally disallowed under the land grant conditions;

  (b) such medical centres might have been operated by profit-making related companies. As in the case of Hospital D, such profit-sharing arrangements again might not be allowed under the land grant conditions; and

  (c) whether the hospital management is responsible for the hospital-related services provided by such medical centres, and

whether patients may misunderstand that the centre services are provided by the hospitals;

- acknowledges that:

  (a) the Lands D will follow up on the outstanding issues under the leases granted and take lease enforcement action, where necessary, to support the DH in ensuring compliance with the land lease conditions concerning services-related requirements, such as the submission of accounts requirements, the non-distribution of profits and the enforcement of the alienation restrictions; and

  (b) the Secretary for Food and Health, the Director of Health and the Director of Lands have agreed with the audit recommendations in paragraph 5.10(d) to (i) of the Audit Report;

Sale of land for private hospital development

- expresses grave dismay and finds it inexcusable that:

  (a) the hospital site of 1.922 hectares in District G for developing a hospital of not less than 200 beds, sold in 1982, might have been excessive. As it transpired, only 54% of the site area was used to operate Hospital G (with 410 beds) whereas 46% had remained undeveloped for some 20 years before it was approved to be used for private residential development. The subsequent change in use of such a sizeable portion of the hospital site for private residential development has departed from the original intended use;

  (b) setting a requirement in the land lease to provide 200 beds at the minimum and 600 beds at the maximum was too broad a range to determine the optimum size of the site area;

  (c) the provision of 1.922 hectares for building a hospital of "not less than 200 beds, but not more than 600 beds" seemed to have been worked out based on an arbitrary basis without appropriate development parameters, such as minimum gross floor area and height limits included in the land lease, to regulate the land use;

  (d) notwithstanding that the site was planned and sold for building hospital facilities that could support a hospital with 600 beds, the

land lease had not imposed a contractual obligation on the purchaser to provide more than 200 beds;

(e) during the 20 years after the hospital site was sold in 1982, the purchaser had applied repeatedly for changing the whole or part of the hospital site for residential use;

(f) given that land in Hong Kong is scarce and precious, the sale of an oversized site for private hospital development should have been avoided. The Government needs to draw lessons from this land sale transaction, particularly as the Government has reserved four sites for private hospital development, two of which had been put out for open tender in April 2012;

(g) in considering the lease modification application to carve out the rezoned portion for residential development in March 2002, the Director of Health had not revisited the need for retaining the "rezoned" portion of the site for future hospital development, but simply informed the Lands D that it had no particular comment on the application; and

(h) although due process appeared to have been followed in changing the land use of a sizable portion of the hospital site for private residential development in 2004, yet due to insufficient land space, the prevailing shortfall of hospital beds in District G and the possible expansion of Hospital G remained unaddressed;

- notes the views given by the Secretary for Food and Health and the Director of Lands that the Government should have been more precise in determining the size of the hospital site and in assessing the demand for service expansion;

- notes the view given by the Director of Health in paragraph 5.14(k) of the Audit Report that guidance notes should be provided for B/Ds to assist the latter in considering applications for change of land use and relevant lease modifications, and urge the Director of Lands to provide such protocol for B/Ds' reference;

- notes that the Secretary for Food and Health, the Director of Health and the Director of Lands have agreed with the audit recommendations in paragraph 5.11 of the Audit Report and will draw lessons from this land sale transaction and will take actions to prevent recurrence;

- acknowledges the assurance given by the Secretary for Development and the Secretary for Food and Health that this land sale transaction should not happen again for the following reasons. First, the Administration will be more precise in determining the size of the hospital site and in assessing the demand for service expansion. Second, strict development controls, such as land must be used primarily for hospital services, total gross floor area, maximum site coverage and height, will be stipulated in the land grants of Government sites for new private hospitals;

Way forward

- notes that:

  (a) in January 2011, the Government approved the adoption of a set of minimum requirements for new private hospitals to be developed on new government sites. These minimum requirements covered aspects such as land use, date of commencement of operation, bed capacity, service scope, packaged charge and price transparency, service target, service standard, and reporting; and

  (b) the Secretary for Food and Health, the Director of Health and the Director of Lands have agreed with the audit recommendations in paragraphs 5.10(j) and 5.12 of the Audit Report; and

Follow-up action

- wishes to be kept informed of the progress made in implementing the various audit recommendations, and the effectiveness of the enhanced systems and procedures for coordinating, monitoring and regulating direct land grants made to non-profit-making private hospitals.