

Legislative Council Public Accounts Committee
Public Hearing on Report No. 62 of the Director of Audit's Report
Chapter 2 – Planning, construction and redevelopment
of public rental housing flats

Purpose

This paper provides supplementary information on some of the issues raised by Members during the first public hearing held on 5 May 2014 on Report No. 62 of the Director of Audit, Chapter 2 – Planning, construction and redevelopment of public rental housing (PRH) flats (hereinafter referred to as the “Report”).

Background

2. At the public hearing held on 5 May 2014, Members requested the Government to provide information on various issues. In the time available we have managed to prepare such information on some of the issues, which is presented in this paper. We are working on the other information which we will submit as soon as it is ready.

Supplementary Information

Fluctuation in PRH production (Paragraph 2.11 and Figure 1 of the Report refer)

3. In respect of the query as to why there were fluctuations in PRH production in the past 10 years as shown on Figure 1 of the Report, we reckon from our experience that implementation of public housing development depends on various factors such as planning, construction and resource allocation, etc. In addition, each individual project varies in scale, site specific characteristics/constraints and construction progress. Thus, PRH production for every year may vary.

4. The peak in 2004-05 with a PRH production of 24,682 units was mainly due to the transfer of some HOS projects to PRH as a result of the ceasing of sale and production of HOS in 2002, resulting in an increase of PRH production in 2004-05.

5. The low PRH production in 2006-07 was mainly because of the delay of around 12,600 PRH production from the South East Kowloon Development Area, which were originally scheduled for completion in 2006-07 and 2007-08, due to the Government's review of the reclamation proposal at the South East Kowloon Development.

Tender Price Trends (Figure 1 of the Report refers)

6. In respect of the request for information on the construction price levels for the respective years in Figure 1 of the Report, **Annex 1** presents this information by integrating the Housing Authority Tender Price Indices (TPI) with the PRH production in Figure 1 for easy reference of Members. It is noted that the TPI was relatively low when we embarked upon the works programme for completion in 2004-05. Nevertheless, this observation is for information only since we have already clarified at the public hearing on 5 May 2014 that the level of tender price is not a determining factor in planning the public housing development programme.

Financial Information for construction expenditure (Paragraph 1.5 of the Report refers)

7. In respect of the query on construction expenditure as stated in paragraph 1.5 of the Report, the operating income and expenditure for PRH in 2013-14 are estimated at \$11.9 Billion (B) and \$12.7 B respectively (i.e. an operating deficit at about \$0.8B). The construction expenditure for 2013-14 is budgeted at \$9.9 B. The HA maintains recurrent operating account and capital account separately. The annual operating expenditure under the operating account of PRH includes personal emoluments, cleansing and security, maintenance and improvements, and depreciation of completed buildings, etc. It does not include construction expenditure incurred in the year which is under the capital account. In accordance with the HA's approved accounting policy, capital expenditure incurred during the construction period is accounted for as construction in progress asset. The total construction costs of a building will be transferred and classified as fixed asset of the HA upon its completion. Depreciation is then recorded as an annual operating expenditure by allocating the total construction costs of the building over the estimated useful life of the building of 50 years on a straight-line basis.

8. The related financial information of HA for the last five years is attached at **Annex 2** for Members' information. As shown in the Annex,

the HA has annual consolidated surpluses for the last five years, after offsetting the PRH's operating deficit from the surplus of other operations and investment. With the fund generated from the annual operation and over \$60B balance carried forward in the period, the HA has been able to meet the funding requirement of its operation and the construction programmes.

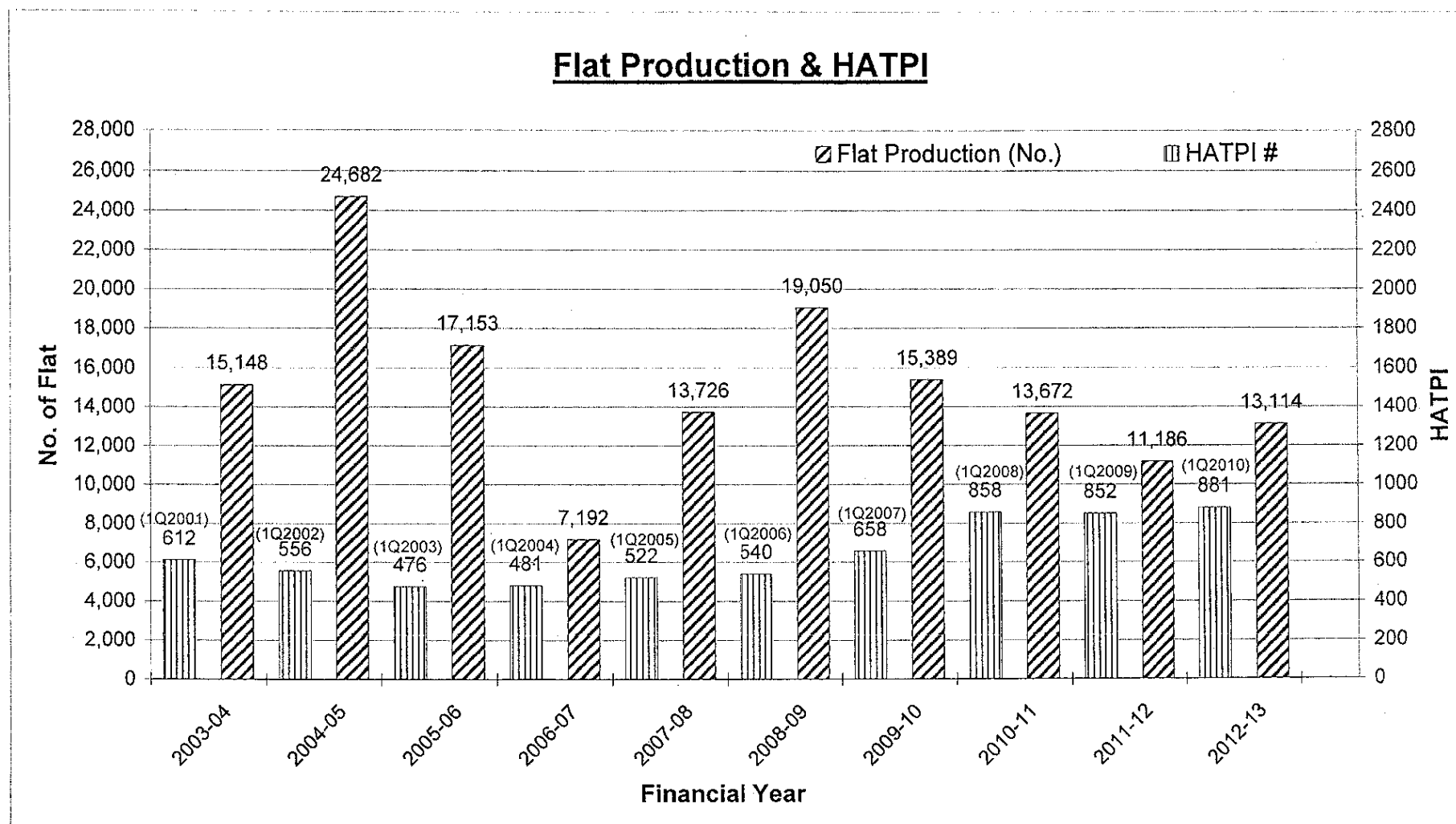
Long Term Housing Demand Projection

9. In respect of the request for information on how we plan to take forward the long term housing demand projection under the Long Term Housing Strategy review and its annual updating, we have compiled a note attached at **Annex 3** for Members' reference.

Advice Sought

10. Members are invited to note the content of this paper.

Transport and Housing Bureau
9 May 2014



As the normal building contract period is approximately 30 months (i.e. 2.5 years), the corresponding Housing Authority Tender Price Index (HATPI) for the building contract commencement date is set at 2.5 years before the middle of the Financial Year.

**Financial information of the Hong Kong Housing Authority (HA)
for the financial years from 2009-10 to 2013-14**

1. The HA's annual consolidated surplus comes from the operating accounts of Rental Housing, Commercial, and Home Ownership Assistance, as well as Funds Management Account. The Financial Statements are prepared in accordance with the Housing Ordinance and accounting policies approved by the HA.
2. As stated in paragraph 1.5 of the Report No. 62 (Chapter 2) of the Director of Audit, the operating income and expenditure for public rental housing (PRH) in 2013-14 are estimated at \$11.9 billion (B) and \$12.7B respectively (i.e. an operating deficit at about \$0.8B). The construction expenditure for 2013-14 is budgeted at \$9.9B.

The corresponding figures for the past five years are summarised as follows:

(i) Rental Housing Operating Account	2009-10 Actual	2010-11 Actual	2011-12 Actual	2012-13 Actual	2013-14 Revised Budget
	(\$B)	(\$B)	(\$B)	(\$B)	(\$B)
Total Income	9.9	9.5	10.6	10.4	11.9
Total Expenditure	(11.4)	(10.4)	(11.2)	(11.6)	(12.7)
Operating deficit	(1.5)	(0.9)	(0.6)	(1.2)	(0.8)

The operating income under Rental Housing Operating Account mainly comes from PRH rental income, while the operating expenditure includes personal emoluments, cleansing & security, maintenance & improvements, and depreciation of buildings, etc.

(ii) Construction Expenditure	2009-10 Actual	2010-11 Actual	2011-12 Actual	2012-13 Actual	2013-14 Revised Budget
	(\$B)	(\$B)	(\$B)	(\$B)	(\$B)
Total Construction Expenditure	5.8	6.4	7.6	8.9	9.9

In accordance with the HA's approved accounting policy, capital expenditure incurred during the construction period is accounted for as construction in progress asset. The total construction costs of a building would be transferred and classified as fixed asset of the HA upon its completion. Then depreciation is recorded as an annual operating expenditure by allocating the total construction costs of the building over the estimated useful life of the building of 50 years on a straight-line basis.

3. The HA's annual surplus incorporating the above operating deficit from Rental Housing Operating Account and surplus from other accounts for the past five years are summarised below:

	2009-10 Actual	2010-11 Actual	2011-12 Actual	2012-13 Actual	2013-14 Revised Budget
	(\$B)	(\$B)	(\$B)	(\$B)	(\$B)
Surplus for the year	7.7	8.2	4.4	5.8	5.6

4. With the fund generated from the annual operation and over \$60B balance carried forward in the period, the HA has been able to meet the funding requirement of its operation and the construction programmes, as summarised in the following cash flow movement:

	2009-10 Actual	2010-11 Actual	2011-12 Actual	2012-13 Actual	2013-14 Revised Budget
	(\$B)	(\$B)	(\$B)	(\$B)	(\$B)
Cash & Investment Balance at beginning of year	56.5	62.4	69.7	69.4	69.2
Surplus for the year	7.7	8.2	4.4	5.8	5.6
Add: Adjustments on non-cash items (mainly Depreciation) and others	4.5	6.1	3.8	3.8	4.2
Less: Payment of capital expenditure					
(a) Construction works	5.8	6.4	7.6	8.9	9.9
(b) Other improvement works and computer assets	0.5	0.6	0.9	0.9	1.0
Cash & Investment Balance at end of year	62.4	69.7	69.4	69.2	68.1

Long Term Housing Demand Projection

The Government set up the Long Term Housing Strategy (LTHS) Steering Committee in September 2012 to make recommendations on Hong Kong's LTHS for the next ten years. An important task of the LTHS review was to project the long term housing demand. To support the work of the LTHS Steering Committee, the Housing Department (HD), in collaboration with relevant Government bureaux/departments, developed a proposal for a new methodology for the projection of long term housing demand and submitted the proposal for consideration by the LTHS Steering Committee. Since a new methodology was being developed after the setting up of the LTHS Steering Committee, the HD has not used its old long-term housing demand assessment method since 2012. Based on the proposal submitted by HD, the LTHS Steering Committee adopted a new method. We briefed the Subcommittee on the Long Term Housing Strategy under the Panel of Housing of the Legislative Council (LegCo) on this new methodology vide LegCo Paper No. CB(1)194-13-14(02) on 11 November 2013.

2. Under the new method, the LTHS Steering Committee considers that every household in Hong Kong should be adequately housed, irrespective of whether they live in public or private housing; or in owned or rented accommodation. For the purpose of projecting long term housing demand, housing demand is defined as the total number of new housing units required to be built if each and every household is to be accommodated in adequate housing over the long term. When projecting the number of new housing units required, the LTHS Steering Committee considered the following major components -

- (a) net increase in the number of households;
- (b) those who would be displaced by redevelopment; and
- (c) those who were inadequately housed.

In addition, the new method adds a “miscellaneous” factor, which included private permanent living quarters occupied by “mobile residents only” households, non-local students who might take up accommodation in Hong Kong, and the demand of non-local buyers who may take up flats but without channelling them back to the

market. This is one of the major areas where the LTHS method is different from HD's old method. Another major difference under the new method is the use of an econometric modeling exercise to produce a range of projections to take into account the impact of different economic and property situations, thereby obtaining a more comprehensive gauge of the estimated housing demand under different economic and property market situations.

3. Using the new method, the LTHS Steering Committee projected that the total housing supply in the next ten years should range between 440 000 and 500 000 units, with a proposed supply target of 470 000 units (mid-point). The Government will use this new methodology to project long term housing demand in future and will review it on an annual basis as recommended by the LTHS Steering Committee.

4. As for the way forward, we have been working on operational details of the annual updating of the demand forecast. Such details include establishing processes for the preparation of the various data inputs, internal process for validating data and projections, and timing and method for the promulgation of the updated forecasts, etc. While not all such details need to be featured in the text of the Government's Long Term Housing Strategy, we aim to have them sorted out before we present our Long Term Housing Strategy before the end of this year.