

Efforts of the Rating and Valuation Department in safeguarding revenue on rates and government rent

A. Introduction

The Audit Commission ("Audit") conducted a review to examine the Rating and Valuation Department ("RVD")'s efforts in safeguarding revenue on rates and government rent.

Background

Rates

2. Rates are one of Hong Kong's indirect taxes levied on properties. For 2014-2015, the revenue collected from rates under the Rating Ordinance (Cap. 116) (after deducting the amount for rates concession) was \$22.3 billion, accounting for about 4.7 % of the total government revenue. Generally, properties in all parts of Hong Kong are liable to be assessed to rates under the Rating Ordinance. Rates are charged at a percentage (currently at 5%) of the rateable value which is the estimated annual rental value of a property at a designed valuation reference date, assuming that the property was then vacant and to let. The Rating Ordinance provides two forms of rates exemptions for specific types of properties.¹ One is exemption from assessment to rates, whereby no assessment will appear in the Valuation List.² The other is exemption from payment of rates, whereby an assessment is included in the Valuation List but the property is exempted from payment of rates.

Government rent

3. Government rent is the payment made by the Government lessee (the "owner") to the Government in return for the right to hold and occupy the land for the term (i.e. duration) specified in the lease document. The revenue collected from government rent is also part of the Government's general revenue. For 2014-2015, the revenue collected from government rent under the Government Rent (Assessment and Collection) Ordinance (Cap. 515) ("the Rent Ordinance")³ was \$9.3 billion. The government rent is charged at 3% of the rateable value of the property situated on the leased land and is adjusted in step with any subsequent

¹ Please refer to Appendices A and B of the Director of Audit's Report ("Audit Report") for the types of properties exempted from assessment to rates and from payment of rates.

² RVD maintains records of all properties that have been assessed to rates in a Valuation List.

³ Please refer to paragraph 1.5 of the Audit Report for government rent payable under other ordinances.

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changes in the rateable value.⁴ The Rent Ordinance also provides for exemption of properties from liability to pay government rent. An indigenous villager or his lawful successor in the male line (or tso, or tong) who (or which) has continuously owned an old schedule lot, village lot, small house or other rural holding since 30 June 1984, or small house or resite house granted after that date is entitled to exemption from liability to pay government rent.

The Rating and Valuation Department

4. RVD is responsible for the assessment and collection of rates under the Rating Ordinance and government rent under the Rent Ordinance.

5. RVD maintains records of all properties that have been assessed to rates and those liable for assessment to government rent under the Rent Ordinance in a Valuation List and a Government Rent Roll respectively. RVD updates the Valuation List and the Government Rent Roll through General Revaluations ("GRs"),⁵ interim valuations and deletions.⁶ As at 1 April 2015, the Valuation List contained 2.43 million assessments (for 1.8 million domestic properties and 0.63 million non-domestic properties) with a total rateable value of \$608.6 billion (a year-on-year increase of 7.9%), and the Government Rent Roll contained 1.89 million assessments with a total rateable value of \$354.1 billion (a year-on-year increase of 8.3%).

6. Section 29(1) of the Rating Ordinance provides that any rates due on an interim valuation shall be payable from the date when the interim valuation became effective, or 24 months before the date of the issue of the first demand note, whichever is the later. This means that RVD cannot recover retrospectively the rates for more than 24 months. For government rent, the Rent Ordinance does not specify any time-bar for recovering government rent. Government rent due on an interim valuation is payable from the effective date of the interim valuation.

⁴ Please refer to paragraph 1.4(b) of the Audit Report for the types of properties which are generally liable for government rent under the Rent Ordinance.

⁵ RVD conducts GRs annually to bring the rateable values of all properties up to date to reflect changes in market rental values.

⁶ RVD may at any time make interim valuations of newly-built properties and properties which have undergone structural alterations and make deletions to remove properties which have ceased to be liable for assessment to rates/government rent.

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The Committee's Report

7. The Committee's Report sets out the evidence gathered from witnesses. The Report is divided into the following parts:

- Introduction (Part A) (paragraphs 1 to 10);
- General Revaluations (Part B) (paragraphs 11 to 26);
- Interim valuations (Part C) (paragraphs 27 to 40);
- Rates exemption for rural properties (Part D) (paragraphs 41 to 50);
- Collection of rates and government rent (Part E) (paragraphs 51 to 55);
and
- Conclusions and recommendations (Part F) (paragraphs 56 to 58).

Public hearing

8. The Committee held a public hearing on 7 May 2016 to receive evidence on the findings and observations of the Director of Audit's Report ("Audit Report").

Opening statement by Secretary for Financial Services and the Treasury

9. **Professor K C Chan, Secretary for Financial Services and the Treasury**, made an opening statement at the beginning of the Committee's public hearing held on 7 May 2016, the summary of which is as follows:

- the Administration had been striving to safeguard revenue from rates and government rent, which were broad-based and stable sources of government revenue. The rates arrears rate had been maintained at around 0.4% in recent years, which was far below the arrears rate in other jurisdictions charging similar taxes;

General Revaluations

- rental information provided an important basis for the GR of rateable value each and every year. RVD would issue Requisition Forms for Particulars of Tenements (Form R1A) to selected properties, and

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require ratepayers to complete and return the forms, so that it could get hold of the relevant rental information. The return rate of Form R1A had reached some 80% in recent years, which showed that the majority of ratepayers had complied with the requirement to return the forms. The verification exercise conducted on a sample basis on the rental information furnished in the forms also showed that the information provided was correct for 70% of the cases;

- RVD would closely monitor the situation and step up enforcement actions, with a view to enhancing the reliability of information collected from the Requisition Forms. RVD would also touch base with the Buildings Department ("BD") to put in place a mechanism to collect information on subdivided properties, so that RVD could assess their rateable values more accurately to safeguard government revenue;

Interim valuations

- regarding interim valuations, for unauthorized building works ("UBWs") with rates already assessed, RVD had been collecting rates until the removal of the UBWs concerned. Following the rating principles under common law that properties of transient nature would not be so assessed, RVD had all along taken it that UBWs with removal orders issued would be demolished soon and could thus be regarded as properties of transient nature. However, as the Audit Report pointed out, it might take some time for individual UBWs to be demolished. In the light of the situation, the Financial Services and the Treasury Bureau ("FSTB") had asked RVD to put in place some form of bring-up system to keep track of those existing UBWs with removal orders issued but not yet demolished, such that timely interim valuations would be made within the 24-month time-bar in recovering rates, so as to better safeguard rates revenue;

Rates exemption for rural properties

- for rural properties, the Rating Ordinance provided that properties in designated village areas ("DVAs") were exempted from assessment to rates. As pointed out in the Audit Report, a village house located within a DVA would be entitled to exemption only if it complied with certain prescribed criteria in terms of number of storeys, floor area and height. The Administration agreed that it was incumbent on RVD to inspect the status of village houses within DVAs, so as to ensure that

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only those in compliance with the prescribed statutory requirements were exempted from rates;

- since the above inspection exercise would involve inspection of some 16 000 village houses in 105 DVAs, the caseload was voluminous. It was only pragmatic for RVD to conduct inspection in a phased manner in view of competing priorities; and

Collection of rates and government rent

- as regards the long outstanding arrears cases with charging orders, RVD had been taking follow-up actions in an on-going manner. With a view to further facilitating the Lands Department ("LandsD") in taking action on bona vacantia cases,⁷ RVD had reminded its staff to notify LandsD of such cases as soon as practicable, and to request LandsD to inform RVD in a timely manner upon taking possession of the relevant properties, so that RVD could delete the rating assessments.

The full text of Secretary for Financial Services and the Treasury's opening statement is in *Appendix 4*.

10. **Secretary for Financial Services and the Treasury** also stated at the public hearing that Hong Kong received the best grades in "The Best and Worst of International Property Tax Administration: Scorecard on State and International Property Tax Administrative Practices"⁸ in September 2014. The valuation of properties for rates and government rent conducted by RVD achieved high grades in three areas, namely, transparency, simplicity and consistency, as well as procedural fairness.

⁷ Section 752 of the Companies Ordinance (Cap. 622) provides that, where a company is dissolved, the property vested in the company immediately before its dissolution is vested in the Government as bona vacantia.

⁸ The research was carried out jointly by The Council On State Taxation, the United States, and the International Property Tax Institute, Canada, to provide an international scope for tax policymakers with best practices and a comparative measure of their property tax administrative practices.

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B. General Revaluations

Rental information collection and verification

11. The Committee noted from paragraph 2.6(a) of the Audit Report that the landlord of a domestic property was required to lodge with RVD a Notice of New Letting or Renewal Agreement (Form CR109) in respect of any new letting or renewal agreement for endorsement. The Committee asked for the reason(s) for not requiring landlord of non-domestic property to submit Form CR109 (or any other form to that effect) to RVD in respect of any new letting or renewal agreement for endorsement.

12. **Mr TANG Ping-kwong, Commissioner of Rating and Valuation**, explained at the public hearing and in his letter dated 24 May 2016 (*Appendix 5*) that:

- under section 119L in Part IV of the Landlord and Tenant (Consolidation) Ordinance (Cap. 7), owners of domestic properties were required to submit Form CR109 for endorsement by Commissioner of Rating and Valuation. The form was a source of rental data for GR and compilation of property market statistics by RVD; and
- Part IV of the Landlord and Tenant (Consolidation) Ordinance had never been applicable to non-domestic tenancies. Hence, no submission of similar form for endorsement was required for tenancies of non-domestic properties. Nonetheless, RVD had obtained rental information of non-domestic properties from other sources. As pointed out in paragraph 2.6(b)(i) of the Audit Report, an RVD staff took photocopies of some tenancy agreements at the Stamp Office, mainly the tenancy agreements of non-domestic properties (such as shops, offices and factories) to collect relevant rental data.

13. The Committee also noted from paragraph 2.7 of the Audit Report that for GRs from 2010-2011 to 2015-2016, some 240 properties for which Form R1As had been received were selected (all multi-property ratepayers) each year for issuing letters requiring the ratepayers concerned to supply supporting documents for their furnished rental information (such as copies of tenancy agreements and rent receipts). The Committee enquired about the basis for selecting only about 240 properties each year for rental verification purposes.

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14. **Commissioner of Rating and Valuation** said in his letter dated 24 May 2016 (Appendix 5) that RVD conducted a rental verification exercise each year by selecting 240 properties from Form R1As received, so as to allow it to review and enhance the templates of the Requisition Forms for making it clear to payers the information that they should furnish. Over the past three years, the in-order rate rose from 61% in 2013-2014 to 75% in 2015-2016. RVD would closely monitor the return of Form R1As and consider increasing the sample size if a growing trend in the number of cases with incorrect information was spotted. Moreover, for deterrent purpose, in the event of suspected false reporting and with sufficient evidence, RVD would take prosecution action.

15. In reply to the Committee's request, **Commissioner of Rating and Valuation** provided in his reply dated 24 May 2016 a breakdown by property type on the cases found in the rental verification exercises from the GR in 2010-2011 to the GR in 2015-2016 to have furnished incorrect information (Appendix 5).

16. According to paragraph 2.10 of the Audit Report, on average 67 (28%) of some 240 cases each year were found to have provided incorrect rental information in Form R1As during the rental verification exercises from the GR in 2010-2011 to the GR in 2015-2016. The Committee enquired about the measures taken/to be taken to improve the accuracy of rental information furnished in Form R1As, and whether consideration would be given to requiring ratepayers to submit copies of tenancy agreements and rent receipts together with their Form R1As to RVD.

17. **Commissioner of Rating and Valuation** said at the public hearing and explained in his letter dated 24 May 2016 (Appendix 5) that RVD had taken the following measures in strengthening the rental verification mechanism:

- promoting and educating the public of their responsibility to furnish rental particulars accurately and comprehensively;
- reviewing and enhancing the templates of the Requisition Forms to make it clear to payers the information that they should furnish;
- encouraging the public to use RVD templates for submission to avoid omission; and

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- reminding those who had submitted incorrect information of the importance of furnishing rental particulars accurately and comprehensively through telephone conversation, correspondence and customer liaison meetings.

18. **Commissioner of Rating and Valuation** further explained in his letter dated 24 May 2016 (Appendix 5) that under the Rating Ordinance and the Rent Ordinance, RVD might demand copies of tenancy agreements and rent receipts from rates/government rent payers for the assessment of rates and government rent. On environmentally friendly ground, RVD considered it unnecessary to request payers to return copies of relevant documents along with Requisition Forms. RVD would only request the payers of selected properties to provide copies of tenancy agreements and rent receipts for rental verification purpose.

19. In reply to the Committee's enquiry about the development of paperless solutions for capturing rental information, **Commissioner of Rating and Valuation** said in his letter dated 24 May 2016 (Appendix 5) that RVD was seeking Government Chief Information Officer's assistance in exploring the feasibility of developing paperless solutions for capturing rental information for stamped tenancy agreements for GR purposes.

20. According to paragraph 2.9 of the Audit Report, of some 307 700 Form R1As issued to obtain rental information for each annual GR from 2010-2011 to 2015-2016, about 56 400 (18%) ratepayers failed to return the Form R1As. The number of ratepayers who had failed to return Form R1As for three years consecutively increased by 22% from 6 100 in the GR in 2010-2011 to 7 417 in the GR in 2015-2016. In this regard, the Committee asked:

- measures taken/to be taken to increase the return rate of Form R1As;
- whether RVD would take more stringent enforcement actions against non-returned cases; and
- whether these non-returned cases would undermine the accuracy of rateable values generated in GRs.

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21. **Commissioner of Rating and Valuation** explained at the public hearing and in his letter dated 24 May 2016 (Appendix 5) that RVD had taken the following measures for improving the return rate of Form R1As:

- promoting via press release, radio announcements of public interest, RVD website and MyGovHK, to remind the public of their responsibility to complete and return Requisition Forms;
- encouraging electronic submission of Form R1As via RVD website; and
- sending email to remind payers who used eRVD Bill to complete and return Requisition Forms on time.

In addition, RVD would consider the need to develop a mobile website to facilitate submission of Form R1As through mobile phones; and enhance the deterrent effect by strengthening prosecution of those who had not returned the Requisition Forms. Moreover, RVD would continue to monitor the return rate of the Requisition Forms and, should the situation get worse, consider taking appropriate actions to motivate the return of the Forms and to request Department of Justice to relay to the court whether or not the sentences (a fine generally ranged between \$1,000 and \$2,000) were sufficient to achieve a deterrent effect.

22. **Commissioner of Rating and Valuation** further explained at the public hearing and in his letter dated 24 May 2016 (Appendix 5) that:

- the return rate of the Requisition Forms had reached some 80% in recent years, which was already higher than other countries;
- apart from the Requisition Forms, RVD would also collect rental information from other sources, such as Form CR109 (See paragraph 12 above) and the stamped tenancy agreements;
- RVD's annual revaluation was based on the overall rental level of properties, and the impact of non-return of individual Requisition Forms on the revaluation exercise was limited; and
- after completion of each GR, a statistical audit was conducted by RVD, based on the "Standard on Ratio Studies" issued by the International Association of Assessing Officers, at a macro level to affirm that the

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new rateable values were of reasonable, correct and consistent level as at the valuation reference date, and that the required standard of relative equity amongst individual assessments both between and within different property groups had been achieved. The statistical audits had shown that the accuracy of RVD's valuations had met the international standard.

Penalties in respect of non-compliance with Form R1A submission requirement

23. The Committee enquired about the penalties in respect of non-compliance with Form R1A submission requirement vis-a-vis those for not filing tax returns on time or providing incorrect information in tax returns, and whether consideration would be given to increasing the penalties for failure to return Form R1As or providing incorrect information in Form R1As by making reference to the penalties for failure to make tax returns or making incorrect tax returns, with a view to achieving a greater deterrent effect.

24. **Secretary for Financial Services and the Treasury** said in his reply in May 2016 (*Appendix 6*) that:

- according to the Rating Ordinance and the Rent Ordinance, any person who refused to furnish particulars requested in Form R1A was liable to a fine at level 3 (i.e. \$10,000), and any person who knowingly made a false statement in Form R1A was liable to a fine at level 4 (i.e. \$25,000). In addition to the above penalties, a person convicted under the circumstances as mentioned above was also liable to a fine of treble the amount of rates and/or government rent undercharged;
- as regards the Inland Revenue Ordinance (Cap. 112), any person who without reasonable excuse failed to file a tax return was liable to a fine at level 3 (i.e. \$10,000) (i.e. same with the penalty for refusing to furnish particulars requested in Form R1A), and any person who without reasonable excuse made an incorrect return was liable to a fine at level 3 (i.e. \$10,000). Any person who wilfully with intent to evade tax made any false statement in a tax return was liable to a maximum penalty of a fine at level 5 (i.e. \$50,000) and imprisonment for 3 years. In addition to the above penalties, a person convicted under the circumstances as mentioned above was also liable to a fine of treble the amount of tax undercharged;

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- Form R1A and tax return were of different nature. Whilst the penalty provisions relating to the two were similar in certain parts, they were not entirely comparable to each other. For tax return, generally, each taxpayer had to file tax return annually, and the Inland Revenue Department would compute the tax amount to be payable by a taxpayer based on the information furnished in the tax return filed by the taxpayer and other information available to the Inland Revenue Department. In other words, the information (e.g. on income and deductions) furnished by the taxpayer in the tax return would affect the tax amount required to be paid by that taxpayer for a certain Year of Assessment;
- Form R1A served as one of the sources from which RVD collected rental information. RVD would make use of the rental information provided by ratepayers in Form R1A as well as information collected from other sources to analyze the overall market rental level, on which the assessment of the rateable value of the tenement concerned was based. In other words, the rates chargeable by RVD were based on rateable value of the tenement concerned, rather than the rental amount provided by the ratepayer in Form R1A; and
- the current penalties relating to Form R1A (i.e. \$10,000 for refusal to furnish particulars requested in the form, and \$25,000 for knowingly making a false statement in the form) were appropriate. RVD would enhance the prosecution work in accordance with the legislative provisions and the actual facts of the case, to the extent permitted by the manpower resources available. At present, the amount of fines sentenced by the court was around \$1,000 to \$2,000, which was lower than the statutory limit. RVD would closely monitor the return rate of Form R1As. In case the situation deteriorated notably, RVD would seek to reflect the situation through the Department of Justice to the court, so that the court might take the latest trend into account when sentencing.

Required property alteration information not reported in Form R1As

25. According to paragraphs 2.12 and 2.15 of the Audit Report, Audit's test check results suggested that ratepayers might not be forthcoming in disclosing information on their subdivided properties. In response to RVD's request in March 2012, BD had provided RVD with a list of 116 buildings which were found

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in 2011 to have 800 subdivided properties. BD also informed RVD that another 339 buildings would be inspected in its large-scale operations in 2012. However, in September 2012, when RVD tried to obtain a comprehensive list of subdivided properties identified in all BD's large scale operations, it was informed by BD that such a list was not available. As the subdivided property information of BD could help RVD detect the omission or under-reporting of subdivided property information in Form R1As, the Committee asked for the measures that RVD and BD would take to improve the sharing of information on subdivided properties.

26. **Commissioner of Rating and Valuation** said at the public hearing that RVD would request BD to provide the addresses of subdivided properties identified by BD, and make use of such information to identify ratepayers of subdivided properties who had under-reported subdivided property information in their Form R1As. **Mr HUI Siu-wai, Director of Buildings**, undertook at the public hearing that BD would share with RVD the information on subdivided properties required for rating assessment purposes.

C. Interim valuations

Policy decision of not collecting rates from new or re-erected illegal rooftop structures

27. According to paragraph 3.10 of the Audit Report, in November 2000, the then Secretary for the Treasury endorsed the proposal of a Task Force of the then Planning and Lands Bureau to cease collecting rates from new or re-erected illegal rooftop structures having regard to the prompt actions that would be taken by BD to clear new or re-erected illegal rooftop structures. In view of the long time taken to demolish illegal rooftop structures and other assessable UBWs and the 24-month time bar in recovering rates, the Committee asked whether the Administration would consider reviewing the 2000-2001 policy decision of not collecting rates from new or re-erected illegal rooftop structures.

28. **Secretary for Financial Services and the Treasury** stated at the public hearing that the arrangement arising from the 2000-2001 policy decision of not collecting rates from new or re-erected illegal rooftop structures would no longer be implemented. But he later on advised in his reply in May 2016 (Appendix 6) that:

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- the decision of not collecting rates from new or re-erected illegal rooftop structures was part of the package of measures drawn up by the Administration in 2000-2001 to tackle UBWs. Since the Administration expected at that time that new or re-erected illegal rooftop structures would be stopped promptly, the decision concerned was in line with the principles adopted by RVD all along, i.e. properties of transient nature would not be assessed to rates;
- having examined the matter, FSTB considered that the policy intention of the decision concerned remained appropriate, though there was room for improvement in its implementation;
- as the Audit Report pointed out, it might take some time for individual UBWs to be demolished after removal orders had been issued by BD. FSTB therefore considered that, on the premise of maintaining the above rating principles, the Administration would need to ensure that UBWs would not keep on being exempted from rating assessment due to delay in their demolition. The Administration would therefore improve the arrangements; and
- for new or re-erected illegal rooftop structures, RVD would put in place a bring-up system to keep track of those new or re-erected illegal rooftop structures with removal orders issued but not yet demolished. The bring-up system would also cover other UBWs with removal orders issued but not yet demolished, such that timely interim valuations would be made and rates be charged on that basis before the 24-month time-bar. As regards existing illegal rooftop structures (i.e. those not being new or re-erected cases) and UBWs already assessed to rates, RVD had all along been collecting rates from these structures until they were demolished.

29. Since Secretary for Financial Services and the Treasury stated at the public hearing that the arrangement arising from the 2000-2001 policy decision of not collecting rates from new or re-erected illegal rooftop structures would no longer be implemented, but his subsequent written reply after the hearing stated that the policy intention of the decision concerned remained appropriate, though there was room for improvement in its implementation, the Committee has written to the Secretary for Financial Services and the Treasury to request for clarification on whether the 2000-2001 policy decision remained valid and the reasons for advising the Committee at the public hearing that the policy decision would no longer be implemented by the Administration.

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30. **Secretary for Financial Services and the Treasury** stated in his reply dated 7 June 2016 (*Appendix 7*) that:

- at the public hearing on 7 May 2016, Secretary for Financial Services and the Treasury mentioned that the November 2000 arrangement would no longer be implemented. He also mentioned that:
 - (a) the premise on which the then Secretary for the Treasury responded to the relevant proposal was in line with the principles adopted by RVD in handling UBWs, i.e. no rates would be collected on properties if they were of transient nature; and
 - (b) FSTB had asked RVD to put in place some form of bring-up system to keep track of those UBWs with removal orders issued but not yet demolished, such that timely interim valuations would be made within the 24-month time bar in recovering rates;
- as set out in Secretary for Financial Services and the Treasury's reply in May 2016 (*Appendix 6*), he considered that the policy intention of the decision concerned remained appropriate, though there was room for improvement in its implementation;
- for new or re-erected illegal rooftop structures, RVD would no longer hold up the rating assessment on such structures across the board. Under the bring-up system as mentioned above, if any such structures with removal orders issued but not yet demolished in 24 months, RVD would make timely interim valuations such that rates would be charged on such structures (including rates to be recovered for the 24-month period concerned) in good time. This had changed the implementation arrangement made in November 2000; and
- the relevant formulation was not inconsistent with the remarks made by Secretary for Financial Services and the Treasury at the hearing, and was also in line with his understanding on the expression at the hearing that "a structure would not be exempted from rates solely because it is an UBW".

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31. The Committee noted from paragraphs 3.13 to 3.15 of the Audit Report that RVD issued a departmental instruction in 2005 covering both illegal rooftop structures and other types of assessable UBWs.⁹ It stipulated that RVD staff should not take any further action on un-assessed illegal rooftop structures/UBWs subjected to BD's removal orders, on the assumption that their existence would be transient. However, RVD's presumption that after the issue of removal orders, the illegal rooftop structures/UBWs would be demolished soon turned out to be not always valid. Of 54 637 assessable UBWs cases with removal orders issued from 2001 to 2015, 16 304 (30%) had not been complied with as at 31 December 2015, with 10 192 having remained outstanding for two years or more. In this regard, the Committee asked for an estimate on the loss of rates revenue in the past five years due to RVD's arrangement of not collecting rates from existing illegal rooftop structures and other UBWs subjected to BD's removal orders but not yet assessed to rates.

32. **Commissioner of Rating and Valuation** explained in his letter dated 24 May 2016 (Appendix 5) that:

- based on Table 7 of paragraph 3.17 of the Audit Report, and with appropriate adjustment for transient cases (i.e. those with orders issued within one year), already assessed cases and other non-assessable cases, RVD had arrived at a rough estimate in the amount of about \$4.2 million per annum of rates income if such UBWs (referring to such major types of UBWs as those on top roofs, side roofs, lane/yard, subdivided units and basement excavation) would have been assessed, representing only 0.02% of the total rates revenues in 2016-2017. However, this was a rough revenue estimate which could not be treated as a proper basis for collecting the additional rates; and
- RVD estimated that it needed to spend \$11.1 million in terms of staff cost for assessing these UBWs to rates (about 2% of the total departmental expenditure in 2016-2017).

At the request of the Committee, Commissioner of Rating and Valuation provided the basis of arriving at the above rough estimates of \$4.2 million per annum of rates income if the said UBWs would have been assessed and \$11.1 million in terms of staff cost for assessing these UBWs to rates (*Appendix 8*).

⁹ RVD had issued a departmental instruction covering illegal rooftop structures in 2002. The 2005 departmental instruction was an expansion of the 2002 version covering both illegal rooftop structures and other types of assessable UBWs.

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33. In reply to the Committee's further question on the measures to improve the collection of rates from existing illegal rooftop structures and other UBWs subjected to BD's removal orders but not yet assessed to rates, **Commissioner of Rating and Valuation** explained at the public hearing and in his letter dated 24 May 2016 (Appendix 5) that RVD would put in place a regular bring-up system to keep track of those UBWs with removal orders issued but not yet demolished, so that timely interim valuations would be made within the 24-month time-bar in recovering rates. The details of the bring-up system were as follows:

- BD had undertaken to regularly provide RVD with lists of specific types of UBWs, covering UBWs with removal orders issued but not yet demolished (such UBWs might be assessable to rates) and demolished UBWs as well as UBWs which were not issued with removal orders, but involved high rental values and were difficult to detect by general external inspections (e.g. subdivided properties and basements);
- RVD would set up a database to store the data collected from BD and analyze such data by reference to RVD's records. RVD would regularly update the list, and demolished UBWs would be excluded from the list; and
- RVD would deploy its staff to inspect and assess the UBWs which were issued with removal orders 15 months before and still standing, so that timely interim valuations would be made within the 24-month time-bar.

Sharing of information on unauthorized building works

34. According to paragraphs 3.10 and 3.22 of the Audit Report, starting from 2001-2002, RVD and BD had established notification arrangements for UBWs. However, based on a test check of 85 removal orders selected from BD's database in January and February 2016, Audit found that only 7 (8%) of them were copied to RVD. BD said that the notification arrangements of UBWs established since 2002 had not been fully put into practice over the years. In this regard, the Committee asked why the notification arrangements had not been fully put into practice.

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35. **Director of Buildings** said in his letter dated 24 May 2016 (*Appendix 9*) that:

- the notification arrangements were first set up in 2001 to facilitate RVD's review of the rateable values of new or re-erected illegal rooftop structures on single-staircase buildings to avoid overcharging of rates and had generally been implemented by BD;
- the purpose of extending the notification arrangements to other types of UBWs in 2004 was to facilitate RVD's review of the rateable values of properties with UBWs removed, i.e. avoiding overcharging of rates. However, the extended arrangements had resulted in a drastic increase in the number of removal orders and compliance letters required to be sent to RVD;
- in addition, BD's manpower at that time had already been in full stretch owing to the need to step up enforcement actions on UBWs erected on external walls of buildings and illegal rooftop structures on single-staircase buildings, handle the large number of reports on UBWs and tackle other building safety initiatives; and
- due to the enormous workload on ongoing initiatives since 2000s, BD could not put the extended notification arrangements fully into practice.

36. The Committee further noted from paragraph 3.22(b) of the Audit Report that in January 2016, BD informed RVD that it had decided to cease the notification arrangements of UBWs information required for rating assessment purposes. As information relating to UBWs was useful for RVD's rating assessment purpose, the Committee enquired about the reasons for making this decision and whether BD had consulted RVD before making such a decision.

37. **Director of Buildings** explained in his letter dated 24 May 2016 (*Appendix 9*) that:

- when reviewing its manpower for redeployment of resources to clear backlog orders in February 2014, BD noted that the notification arrangements for UBWs had not been fully put into practice due to the large number of orders and letters involved and the heavy workload on various building safety initiatives. Based on BD's operational

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experience, the information provided under the notification arrangements would not be sufficient in meeting RVD's needs and RVD would require further details of UBWs, such as copies of plans, photos and inspection reports by BD in some cases. Hence, BD decided to cease the notification arrangements and annul the instruction; and

- to follow up the recommendations in Chapter 1 of the Audit Report No. 64 regarding BD's actions on UBWs issued in April 2015, BD had conducted a review on its work process and internal instructions to enhance its efficiency and reprioritize its work. In January 2016, BD noted that the instruction for the notification arrangements for unauthorized signboards remained in force while such arrangements had not been fully put into practice due to the workload situation. In order to redeploy manpower to clear backlog orders and due to the heavy workload arising from the notification arrangements, BD ceased the notification arrangements for unauthorized signboards. Accordingly, BD notified RVD that the notification arrangements for UBWs information had been ceased.

38. In response to the Committee's enquiry on whether RVD had followed up with BD on sharing the information relating to UBWs, including subdivided property, illegal rooftop structure and other UBWs, **Commissioner of Rating and Valuation** explained at the public hearing and in his letter dated 24 May 2016 (Appendix 5) that upon receiving the memo from BD in January 2016 about the cessation of the notification arrangement, RVD had enquired about the background of the decision. It was the intention then that RVD would reactivate negotiation with BD of setting up afresh a notification mechanism when the Audit Report was released. RVD had a meeting with BD on 12 May 2016 and the two departments agreed to put in place a cost-effective, regular and paperless notification mechanism. In each quarter, BD would send to RVD lists retrieved from its computer systems covering UBWs with removal orders issued but not yet demolished (such UBWs might be assessable to rates) and demolished UBWs.

39. The Committee further asked whether consideration would be given to using big data technology to capture information on UBWs to facilitate the sharing of information among relevant departments for the purpose of rates and government rent assessment.

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40. **Secretary for Financial Services and the Treasury** said in his reply in May 2016 (Appendix 6) that RVD would, when enhancing its information technology system, considered the views of the Committee and considered whether there was a need to make use of big data technology. From the rating perspective, not all UBWs in BD's records were rateable items. Moreover, according to the analysis of reassessed cases completed in recent years, the average increase in rateable values which could be brought about by UBWs on the rooftop, flat roof and lane/yard was less than 5%. RVD would therefore need to consider the actual effectiveness of using the technology in enhancing the collection of property information for assessment of rates and government rent, and whether it was cost-effective to do so.

D. Rates exemption for rural properties

Exemption from assessment to rates for village houses within designated village areas

41. According to paragraph 4.7 of the Audit Report, as at January 2016, RVD had completed interim valuations of properties in 44 811 of 45 000 un-assessed rural lots in the New Territories for government rent assessment. RVD had conducted site visits and collected data on the physical attributes of the un-assessed houses. Audit examined RVD's government rent records of 228 houses in 12 selected villages within nine DVAs. According to RVD records, 18 of the 228 houses were found to be four-storey or five-storey buildings. However, RVD had not taken actions to cancel the exemption from rates of these 18 houses which did not comply with the prescribed three-storey criterion. The Committee enquired about the reasons for not taking actions on these houses which did not comply with the exemption criteria.

42. **Commissioner of Rating and Valuation** explained in his letter dated 24 May 2016 (Appendix 5) that in the early years, the assessment and collection of rates were only confined to the properties in the urban area. Starting from 1954, the rating system adopted in the urban area was extended by phases to the New Territories. The whole area of the New Territories was included in the rating area in 1988. Separately, the Rating Ordinance stipulated that the properties in DVAs were exempted from assessment to rates. Hence, RVD pooled its resources together previously to assess the houses outside DVAs where more rateable properties were found and to consider if the boundaries of DVAs should be revised. Any part of the DVAs which no longer met the relevant exemption criteria would be taken out from the DVAs, and the village houses within the part so removed would no longer be

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exempted on such basis. RVD had all along been taking forward such duties in a prudent manner in order to safeguard government revenue on rates. Since 1992 when the relevant policy was established, RVD had conducted a total of seven exercises to amend the boundaries of DVAs and had de-designated 227 DVAs.

43. **Commissioner of Rating and Valuation** further explained in the same letter (Appendix 5) that in response to the findings and recommendations of the Audit Report, for the houses within DVAs where non-compliance had been detected and where rateable values had been assessed for government rent purposes, RVD would issue rates demands in the following few months. As to other non-compliant houses within DVAs, RVD would work out a plan by the fourth quarter of 2016 to assess them to rates, with a view to issuing rates demands in phases starting from the first quarter of 2017. RVD would also seek the assistance of BD and LandsD to provide information on ineligible cases detected in the course of their enforcement action with a view to expediting the whole assessment process.

44. In view of the additional workload from the above improvement measures and the new bring-up system on UBWs, the Committee asked whether RVD planned to seek additional resources and manpower for implementing these new measures, **Commissioner of Rating and Valuation** said at the public hearing and in his letter dated 24 May 2016 (Appendix 5) that as RVD was in the process of making an assessment on the resources involved in taking forward the various recommendations for enhancing operation as set out in the Audit Report, it could not provide at that stage an estimate of the additional resources required. By reviewing the nature and importance of various tasks from time to time, RVD would set its work priorities and pay regard to cost-effectiveness so as to strike a proper balance. If necessary, RVD would make an application for allocating additional resources for the extra work.

Exemption from payment of rates for village houses outside designated village areas

45. The Committee noted from paragraph 4.19 of the Audit Report that Audit scrutiny of the inspection results of 120 rates-exempted village houses outside DVAs revealed that 48 (40%) of them had been found having UBWs. In addition, Audit's site inspections conducted in December 2015 in three villages also found 11 rates-exempted houses with suspected UBWs. The Committee asked the Home

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Affairs Department ("HAD")¹⁰ for the measures it would take to improve the follow-up actions on ineligible rates-exempted cases outside DVAs.

46. **Miss Janice TSE Siu-wa, Director of Home Affairs**, said at the public hearing and **Secretary for Financial Services and the Treasury** stated in his consolidated reply in May 2016 (Appendix 6) and his reply dated 7 June 2016 (Appendix 7) that:

- HAD relied heavily on the assistance of other departments for detecting non-compliance of rates exemption conditions, and amongst these, UBWs. Under the existing mechanism, HAD had implemented various measures to ensure that timely actions would be taken on ineligible rates-exempted houses outside DVAs. If non-compliance of application condition was found, HAD would take follow up actions including revoking the exemption granted to the tenements, if appropriate;
- at present, HAD randomly selected exempted cases for LandsD to conduct field inspection regarding the existence of UBWs. Regarding paragraph 4.23(b) of the Audit report which recommended stepping up field inspections of rates-exempted houses outside DVAs, this would involve additional resources;
- in the light of FSTB's suggestion, HAD and LandsD had agreed to further discuss and consider how to make the best use of existing resources to enhance the effectiveness of field inspections; and
- regarding the recommendation in paragraph 4.23(c) of the Audit Report (about village houses with UBWs detected), HAD had already started exploring with BD the sharing of information on UBWs in rates-exempted houses in the New Territories through the use of information technology. It was expected that, through efficient electronic data matching and checking, it would enable early detection of non-compliance due to UBWs without generating unaffordable additional workload.

¹⁰ The Chief Executive has delegated to the Director of Home Affairs the authority to grant exemption from payment of rates for eligible village houses outside DVAs. Please refer to paragraph 4.10 of the Audit Report for details of the prescribed eligibility criteria for exemption from payment of rates for village houses outside DVAs.

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The measures taken by HAD to ensure that timely actions would be taken on ineligible rates-exempted houses outside DVAs are in *Appendix 10*.

47. The Committee further asked LandsD about the measures that it would take to ensure the completion of document checks and field inspections of rates-exempted village houses requested by HAD in a timely manner.

48. **Ms Bernadette LINN, Director of Lands, said at the public hearing and Secretary for Financial Services and the Treasury** stated in his consolidated reply in May 2016 (Appendix 6) that:

- LandsD had reminded all the New Territories District Lands Offices ("NTDLOs") in writing on 21 April 2016 of the following:
 - (a) the result of the field inspections and matching checks should be provided to HAD in a timely manner;
 - (b) all matched cases should be reported to HAD as and when UBW was detected, without waiting for the registration of the warning letter in the Land Registry; and
 - (c) when reporting to HAD, sufficient information of the matched cases should be provided, including the date of detection of the UBW and the information of the properties on which the UBW was erected/detected; and
- in order to enhance the efficiency of the matching checks, LandsD would further liaise with HAD to explore measures to improve the compatibility of data between the two departments, so that automated checking could be introduced as far as practicable.

Exemption from assessment to rates for agricultural land and buildings

49. According to paragraph 4.21 of the Audit Report, in 2015, RVD and LandsD agreed that the District Lands Offices would notify RVD of the re-entry/vesting cases, cancellation of re-entry/vesting cases and cases of unauthorized structures on

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agricultural land demolished.¹¹ However, the notification arrangement did not cover unauthorized structure cases to which LandsD had issued warning letters. As LandsD's enforcement information would help RVD identify those agricultural land and buildings which had become ineligible for rates exemption due to change of use, the Committee asked whether LandsD would consider extending the exchange of information on unauthorized structure cases to which LandsD had issued warning letters.

50. **Secretary for Financial Services and the Treasury** stated in his consolidated reply in May 2016 (Appendix 6) that LandsD had already followed up with RVD to explore extending the notification arrangement to cover unauthorized structures on agricultural land to which LandsD had issued warning letters. As agreed between the two departments, NTDLOs would copy warning letters issued by them in respect of these unauthorized structures to RVD in parallel, so that RVD could revoke the rates exemption for the agricultural land involved.

E. Collection of rates and government rent

51. The Committee noted from Table 17 of paragraph 5.5 of the Audit Report that as at 30 September 2015, the total amount of outstanding rates and government rent was \$172 million, representing 0.5% of the annual amount demanded of about \$33 billion. An ageing analysis of the outstanding rates and government rent showed that \$54 million (31%) had been outstanding for two years or more. In 2014-2015, the amount of irrecoverable rates and government rent written off totalled \$0.63 million. The Committee asked for the measures to be taken by RVD to improve the follow-up actions on the arrears cases.

52. **Secretary for Financial Services and the Treasury** said at the public hearing that RVD had taken follow-up actions on more than 20 000 outstanding arrears cases each year and recovered over \$100 million outstanding rates annually through legal actions or after issuing warning letters. **Commissioner of Rating and Valuation** supplemented at the public hearing and in his letter dated 24 May 2016 (Appendix 5) that:

¹¹ Section 36(1)(a) of the Rating Ordinance provides that agricultural land and buildings thereon used in connection with such land are exempted from assessment to rates. Such exempted land and buildings are mostly situated in the New Territories.

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- RVD would take all legal means to recover arrears in rates and government rent, including issuing warning letters and taking legal actions at Small Claims Tribunal or District Court. RVD had reviewed internal procedures and redeployed the limited resources in according priority to protecting Government's interest by speeding up legal actions on arrears cases, including application of charging orders for the judgments obtained;
- while on legal advice, in general a charging order could provide adequate protection to the interest of the Government, RVD would seek all practicable and legal means to recover arrears in respect of properties subject to charging orders;
- under the existing mechanism, when failing all legal means to recover the arrears and no other practicable action was available after seeking legal advice, RVD would refer the case to LandsD for considering re-entry/vesting actions against the property under the Government Rights (Re-entry and Vesting Remedies) Ordinance (Cap. 126) where government rent was involved; and
- having considered Audit's recommendations and reviewed RVD's internal procedures for recovery of arrears, RVD would remind the staff concerned to refer long outstanding arrears cases with charging orders earlier where warranted to LandsD for consideration of re-entry/vesting action.

53. In reply to the Committee's request, **Commissioner of Rating and Valuation** provided in his reply dated 24 May 2016 a breakdown of the outstanding rates and government rent by the number of cases and range of the outstanding amount for each case (Appendix 5), and the follow-up actions taken by RVD on these arrears cases (Appendix 5).

54. According to paragraph 5.7(b) of the Audit Report, of the 14 bona vacantia cases referred to LandsD from 2004 to 2015, LandsD only took possession of the properties in nine cases. The Committee asked for the measures to be taken by RVD and LandsD to improve the follow-up actions on bona vacantia cases.

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55. **Secretary for Financial Services and the Treasury** said at the public hearing and in his consolidated reply in May 2016 (Appendix 6) that:

- in the course of recovering arrears, RVD searched for information on the owners or occupiers through different channels. For bona vacantia properties of dissolved companies, if RVD could not recover the arrears from the occupier, RVD would request LandsD to inform RVD upon taking possession of the relevant property, so that RVD could delete the rating assessment and update the account records, so as to complete the accounting procedure;
- whilst RVD did not possess first-hand information, RVD had reminded its staff to forward such notifications to LandsD as soon as practicable, with a view to further facilitating LandsD in taking action on bona vacantia cases;
- according to LandsD, the Administration might not be in a position to take possession or dispose of the bona vacantia properties under certain circumstances. Moreover, LandsD's follow up action on bona vacantia properties might not achieve the purpose of recovering outstanding rates and/or government rent thereof; and
- for bona vacantia cases mentioned by RVD, LandsD would continue to conduct investigation and take appropriate action. LandsD had reminded its staff to keep RVD informed, in a timely manner, of the possession and disposal of the property or other relevant information, including bona vacantia cases where the dissolved companies had applied for restoration, so as to facilitate RVD's updating of the rating assessment and account records.

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F. Conclusions and recommendations

<p>Overall comments</p>

56. The Committee:

- notes that:
 - (a) rates and government rent are broad-based and stable sources of government revenue. For 2014-2015, revenue collected from rates and government rent added up to \$31.6 billion; and
 - (b) given Hong Kong's narrow tax base, it is important for the Administration to strictly adhere to the provisions stated in the Rating Ordinance (Cap. 116) and the Government Rent (Assessment and Collection) Ordinance (Cap. 515) ("the Rent Ordinance") in collecting rates and government rent respectively, and take enforcement actions against non-compliance cases as necessary, in order to safeguard these stable sources of government revenue;
- expresses grave concern that findings of the Audit Commission ("Audit") and the Committee at the public hearing revealed that the Rating and Valuation Department ("RVD") had not made its best effort in collecting rental information, making interim valuations, collecting rates and government rent, and taking follow-up actions on ineligible rates-exempted cases in rural areas under the provisions of the Rating Ordinance and the Rent Ordinance. This had resulted in a loss of government revenue;
- stresses that the Administration's continued effort in preventing the loss of government revenue will be conducive to reducing pressure on government finances in the long run, and thus may help defer the need for raising taxes to tackle possible budget deficits in the future;
- considers that unless RVD is allocated with substantial additional manpower and resources to cope with the heavy workload arising from the assessment and collection of rates and government rent, it is incumbent upon the following departments to make collective and coordinated efforts to facilitate RVD's assessment and collection of

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rates and government rent in a timely manner, in order to prevent the loss of government revenue:

- (a) the Buildings Department ("BD") to share information with RVD on unauthorized building works ("UBWs") and subdivided properties required for rates assessment purposes;
 - (b) the Lands Department ("LandsD") to:
 - share information with RVD on re-entry/vesting cases, cancellation of re-entry/vesting cases and cases of unauthorized structures on agricultural land as well as unauthorized structure cases to which LandsD has issued warning letters;
 - remind the eight District Lands Offices ("DLOs") to complete document checks and field inspections of rates-exempted village houses outside the designated village areas ("DVAs") requested by the Home Affairs Department ("HAD") in a timely manner; and
 - take timely follow-up actions on bona vacantia cases; and
 - (c) HAD to step up the field inspections of rates-exempted village houses outside DVAs and obtain information from BD on village houses with UBWs detected, with a view to taking timely actions on ineligible rates-exempted cases outside DVAs;
- expresses grave concern that RVD's decision not to collect rates from un-assessed illegal rooftop structures (since 2002) and other types of assessable UBWs (since 2005) with removal orders issued by BD may give rise to apparent unfairness between those property owners who have complied with the Buildings Ordinance (Cap. 123) and also paid rates in accordance with the requirements under the Rating Ordinance, and those property owners whose UBWs were not assessed due to the above decision (hereinafter referred to as "the apparent unfairness issue");
- appreciates that Hong Kong received the best grades in "The Best and Worst of International Property Tax Administration: Scorecard on State

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and International Property Tax Administrative Practices" ¹² in September 2014. The valuation of properties for rates and government rent conducted by RVD achieved high grades in three areas, namely, transparency, simplicity and consistency, as well as procedural fairness;

Policy decision of not collecting rates from new or re-erected illegal rooftop structures

- expresses concern that in November 2000, the then Secretary for the Treasury endorsed the proposal of a Task Force of the then Planning and Lands Bureau to cease collecting rates from new or re-erected illegal rooftop structures having regard to the prompt actions that would be taken by BD to clear new or re-erected illegal rooftop structures ("the 2000-2001 policy decision"). RVD has not taken action on un-assessed illegal rooftop structures (since 2002) and other types of assessable UBWs (since 2005) with removal orders issued by BD, on the assumption that their existence would be transient. However, RVD's presumption that after the issue of removal orders, the illegal rooftop structures/UBWs would be demolished soon turned out to be not always valid. Of 54 637 assessable UBWs cases with removal orders issued from 2001 to 2015, 16 304 (30%) had not been complied with as at 31 December 2015, with 10 192 having remained outstanding for two years or more;
- expresses concern that despite the statement made by Secretary for Financial Services and the Treasury at the public hearing that the arrangement arising from the 2000-2001 policy decision would no longer be implemented, his subsequent written reply after the hearing stated that the Administration considered that the policy intention of the decision concerned remained appropriate, though there was room for improvement in its implementation;
- considers the statement and written reply given by Secretary for Financial Services and the Treasury convoluted and that he had failed to clearly and fundamentally address the apparent unfairness issue created by the 2000-2001 policy decision. This may lead to

¹² The research was carried out jointly by The Council On State Taxation, the United States, and the International Property Tax Institute, Canada, to provide an international scope for tax policymakers with best practices and a comparative measure of their property tax administrative practices.

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unnecessary confusion and uncertainty in respect of the Administration's stance on rates assessment of UBWs and collection of rates from owners of properties with UBWs. Secretary for Financial Services and the Treasury's statement and written reply also failed to show the Administration's determination in preventing the loss of government revenue;

- notes that RVD's rough estimation¹³ indicated that about \$4.2 million per annum of rates income in the past five years was not collected as a result of the implementation of the 2000-2001 policy decision of not collecting rates from new or re-erected illegal rooftop structures. RVD also estimated that it needed to spend \$11.1 million in terms of staff cost for assessing these illegal rooftop structures and other types of assessable UBWs;
- notes Secretary for Financial Services and the Treasury's reply that:
 - (a) the Financial Services and the Treasury Bureau ("FSTB") has examined the 2000-2001 policy decision and considered that the Administration would need to ensure that UBWs would not keep on being exempted from rates assessment due to delay in their demolition; and
 - (b) the Administration would improve the implementation arrangements. For new or re-erected illegal rooftop structures, RVD would put in place a bring-up system to keep track of those new or re-erected illegal rooftop structures with removal orders issued but not yet demolished. The bring-up system would also cover other UBWs with removal orders issued but not yet demolished, such that timely interim valuations would be made and rates be charged on that basis before the 24-month

¹³ Based on Table 7 of the Audit Report, and with appropriate adjustment for transient cases (i.e. those with orders issued within one year), already assessed cases and other non-assessable cases, RVD has arrived at a rough estimate in the amount of about \$4.2 million per annum of rates income if such UBWs (referring to such major types of UBWs as those on top roofs, side roofs, lane/yard, subdivided units and basement excavation) would have been assessed.

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time-bar,¹⁴ so as to prevent the loss of government revenue due to failure to collect rates on a timely basis;

- urges Secretary for Financial Services and the Treasury to re-examine the validity of the 2000-2001 policy decision having regard to the delay in demolition of illegal rooftop structures and other assessable UBWs, and the apparent unfairness issue arising from the 2000-2001 policy decision, in order to curb the loss of government revenue and to deliver a clear message to the public that UBWs are not exempted from rates;
- urges RVD to:
 - (a) expedite the implementation of the new bring-up system to keep track of those existing UBWs with removal orders issued but not yet demolished, and make timely assessments on UBWs that are not removed within three months;
 - (b) conduct a review of un-assessed UBWs cases due to the departmental instruction of not taking action on un-assessed UBWs with removal orders issued by BD, and make interim valuations where appropriate; and
 - (c) consider the feasibility/practicality of assessing all UBWs which would be subject to rates assessment and adjust the rates assessment only upon removal of the relevant UBWs;

Rental information collection, interim valuations and rates exemption

- expresses concern that RVD has not collected rental information, made interim valuations and conducted compliance checking of rates-exempted village houses in DVAs in the most effective, efficient and timely manner with a view to preventing the loss of government revenue. This was evidenced by the following:

¹⁴ According to section 29(1) of the Rating Ordinance, any rates due on an interim valuation shall be payable from the date when the interim valuation became effective, or 24 months before the date of the issue of the first demand note, whichever is the later. However, the Rent Ordinance does not specify any time-bar for recovering government rent. Government rent due on an interim valuation is payable from the effective date of the interim valuation.

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- (a) Form R1As are statutory returns essential for obtaining rental information for General Revaluation ("GR") purposes.¹⁵ Of some 307 700 Form R1As issued for each annual GR from 2010-2011 to 2015-2016, about 56 400 (18%) ratepayers failed to complete and return the Form R1As. However, RVD had only taken prosecution actions on an average of 43 non-returned cases each year in the same period;
- (b) for the rental verification exercises conducted by RVD from the 2010-2011 GR to the 2015-2016 GR:
- RVD only selected about 240 properties (selected ratepayers were all multi-property ratepayers) each year for which Form R1As had been received (on average of 251 343 Form R1As received each year) for issuing letters requiring the ratepayers concerned to supply supporting documents for their furnished rental information (such as copies of tenancy agreements and rental receipts);
 - on average 67 (28%) of some 240 cases selected for verification each year were found to have provided incorrect rental information in Form R1As. However, no prosecution action had been taken against the relevant persons in these cases; and
 - the accuracy of rateable values generated in GRs might be undermined by inaccurate rental information furnished in Form R1As, which could affect the overall revenue from rates and government rent;
- (c) subsequent to the 2000-2001 policy decision, RVD has not taken action on un-assessed illegal rooftop structures (since 2002) and other types of assessable UBWs (since 2005) with removal orders issued by BD. However, RVD staff were not reminded by the departmental instructions to check whether the un-assessed UBWs were new or re-erected cases before deciding

¹⁵ For the assessment and collection of rates and government rent under the Rating Ordinance and the Rent Ordinance, RVD maintains records of all properties that have been assessed to rates and those liable for assessment to government rent under the Rent Ordinance in a Valuation List and a Government Rent Roll respectively, which are updated through GRs, interim valuations and deletions.

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not to take actions on these cases. As a result, rates were not collected from some existing illegal rooftop structures and other UBWs which were subjected to BD's removal orders but not yet assessed to rates;

(d) RVD has not put in place a system for compliance checking of village houses in DVAs to ensure that they meet the prescribed eligibility criteria for rates exemption.¹⁶ In Audit's inspections of two DVAs, 58 village houses were found with four or five storeys, apparently not complying with the prescribed statutory three-storey criterion; and

(e) RVD has not taken timely follow-up actions on village houses which were identified in rent assessments as not meeting the eligibility criteria. As at January 2016, RVD has completed interim valuations of properties in 44 811 (99.6%) of 45 000 un-assessed rural lots in the New Territories for government rent assessment. Audit's sample check of RVD's government rent records of 228 houses in 12 selected villages within nine DVAs found that 18 houses did not comply with the prescribed three-storey criterion, but RVD had not taken actions to cancel their exemption from assessment to rates. Given the 24-month-time-bar, rates for some 4 to 16 years had become irrecoverable for these 18 houses;

- notes that RVD will inspect the status of village houses within DVAs in a phased manner, so as to ensure that only those in compliance with the prescribed statutory requirements are exempted from rates. For those houses within DVAs which have been found to be unable to meet the prescribed criteria for rates exemption and where rates assessments have been made, RVD will issue rates demands as soon as practicable. As regards other houses within DVAs, RVD will work out its work plan by the fourth quarter of 2016, with a view to issuing rates

¹⁶ A village house within a DVA has to comply with the following prescribed size, height and type criteria in order to be qualified for exemption from assessment to rates:

- (a) it will be a building of not more than three storeys and:
 - (i) has a roofed-over area not exceeding 65.03 square metres and does not exceed 8.23 metres in height; or
 - (ii) has a roofed-over area not exceeding 92.90 square metres, does not exceed 7.62 metres in height and complies with certain standard plans; or
- (b) it is a pre-war dwelling house (i.e. built before 16 August 1945), irrespective of size and height, which is of the type normally built for New Territories residents.

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demands to non-compliant houses by phases beginning from the first quarter of 2017;

- urges FSTB to consider reviewing the manpower and financial resources of RVD so that RVD could have the required resources in collecting rental information, making interim valuations and conducting compliance checking of rates-exempted village houses in DVAs in the most efficient, effective and timely manner, given that rates and government rent are stable sources of government revenue;
- urges RVD to:
 - (a) give consideration to requiring ratepayers to submit supporting documents such as copies of tenancy agreements and rent receipts together with their Form R1As with a view to improving the accuracy of the rental information in Form R1As and streamlining the rental verification process;
 - (b) encourage ratepayers to submit their Form R1As and supporting documents through electronic means;
 - (c) educate the public of the need for compliance with Form R1A submission requirement through Government-led promotion effort;
 - (d) for rental verification exercises in the future, use stratified sampling and include ratepayers of single-property so as to improve the accuracy of reported rental information;
 - (e) take more stringent enforcement actions against cases of repeated non-compliance with Form R1A submission requirement;
 - (f) review the departmental instructions of not taking actions on un-assessed UBWs with removal orders issued by BD to ensure that rates are collected from existing UBWs subjected to BD's removal orders but not yet assessed to rates;
 - (g) put in place a control mechanism to ensure that follow-up actions on ineligible rates-exempted cases found in the course of government rent assessments are promptly taken; and

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- (h) review the government rent records of the village houses within DVAs and take prompt actions to revoke the rates exemption of ineligible cases;

Coordination among relevant government departments

- expresses grave concern that RVD has not made sufficient efforts to coordinate and solicit support from BD, LandsD and HAD to provide useful information to facilitate the assessment of rates and government rent in a timely manner. This is evidenced by the following:
 - (a) despite there were agreed notification arrangements of assessable UBWs between BD and RVD, BD only instructed its staff to provide to RVD hardcopy of the removal orders for illegal rooftop structures and advertising signs but not for other types of assessable UBWs. Based on Audit's test check of 85 removal orders selected from BD's database, only 7 (8%) were copied to RVD;
 - (b) despite that BD's information on UBWs, including subdivided properties, illegal rooftop structures and other UBWs, was essential for RVD to assess UBWs in a timely manner, BD decided in January 2016 to cease the notification arrangements of UBWs information required for rates assessment purposes;
 - (c) under the agreed notification arrangements, BD was not required to provide RVD with information on assessable types of actionable UBWs without removal orders issued, and the number of such cases totalled 59 032 from 2001 to 2015. Audit's examination of 1 000 cases with assessable UBWs found that 549 cases might not have been reviewed by RVD;
 - (d) while DLOs of LandsD have been assisting HAD¹⁷ to carry out compliance checking of rates-exempted houses outside DVAs,

¹⁷ Applications for exemption from payment of rates for village houses outside DVAs have to be made to HAD for authentication. After authentication, HAD will forward the application forms to RVD for recommendation on whether exemption should be granted. RVD verifies the details of the village houses in the application forms and, if necessary, conducts site inspections. The application forms together with RVD's recommendation are then returned to HAD for approval. Once the rates exemption is granted, RVD will stop issuing rates demand notes to the applicants.

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some document checks and field inspections requested by HAD were not completed by DLOs in a timely manner. For example, of the 270 field inspections requested by HAD from June 2014 to June 2015, 22 (8%) were still outstanding as at December 2015;

- (e) there was no established arrangement for LandsD to provide RVD with the information on cases of unauthorized structures on agricultural land to which LandsD has issued warning letters. This information could facilitate RVD in identifying ineligible rates-exempted cases; and
- (f) given the 24-month time-bar in recovering rates, there is a risk of loss of revenue if the rateable values of properties with assessable UBWs are not reassessed in a timely manner;

- notes that:

- (a) RVD and BD have agreed to put in place a regular notification mechanism on UBWs. BD will retrieve the relevant information from its computer system, on a quarterly basis, and will forward the information to RVD in a paperless manner;
- (b) RVD will request BD and LandsD to provide information on ineligible cases detected in the course of their enforcement work, with a view to expediting RVD's inspection exercise of village houses in DVAs;
- (c) HAD has implemented various measures to ensure that timely actions would be taken on ineligible rates-exempted houses outside DVAs. Such measures include:
 - the provision of information by RVD and the Land Registry to HAD on rental records, change of ownership/rates payers of rates exempted tenements;
 - HAD randomly selects 10 exempted cases per district (i.e. 90 cases in total) every six months for LandsD to conduct field inspection regarding the existence of UBWs; and

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- HAD provides a list of all rates exempted houses to LandsD every four months for matching check against the records maintained by the eight New Territories District Lands Offices ("NTDLOs") for houses which have been detected to have UBWs during their routine work;
- (d) LandsD has followed up with RVD to explore extending the notification arrangement to cover unauthorized structures on agricultural land to which LandsD has issued warning letters. As agreed between the two departments, NTDLOs would copy warning letters issued by them in respect of these unauthorized structures to RVD in parallel, so that RVD can revoke the rates exemption for the agricultural land involved; and
- (e) LandsD has reminded all NTDLOs in writing on 21 April 2016 of the following:
- the result of the field inspections and matching checks should be provided to HAD in a timely manner;
 - all matched cases should be reported to HAD as and when UBW was detected, without waiting for the registration of the warning letter in the Land Registry; and
 - when reporting to HAD, sufficient information of the matched cases should be provided, including the date of detection of UBW and the information of the properties on which UBW was erected/detected;
- urges FSTB to:
- (a) strengthen the coordinating efforts among RVD, BD, HAD and LandsD for sharing of information for the purposes of rates and government rent assessment; and
- (b) give consideration to using big data technology by the Administration to capture information on UBWs to facilitate the sharing of information among relevant departments for the purposes of rates and government rent assessment;

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- urges BD to:
 - (a) take measures to improve the sharing of information with RVD on UBWs and subdivided properties required for rates assessment purposes, including details of those UBWs without removal orders issued, so that RVD could take timely actions to reassess the rateable values of properties; and
 - (b) take measures to improve the sharing of information with HAD on village houses with UBWs detected outside DVAs, so that HAD could take timely actions on ineligible rates-exempted cases;
- urges HAD to take measures to step up the field inspections of rates-exempted village houses outside DVAs and obtain information from BD on village houses with UBWs detected outside DVAs, with a view to taking timely actions on ineligible rates-exempted cases; and
- urges LandsD to take measures to ensure the completion of document checks and field inspections of rates-exempted village houses outside DVAs requested by HAD in a timely manner.

Specific comments

57. The Committee:

General Revaluations

- expresses concern that:
 - (a) of some 307 700 Form R1As issued to collect rental information for each annual GR from 2010-2011 to 2015-2016, about 56 400 (18%) ratepayers failed to return Form R1As, and the number of ratepayers who had failed to return Form R1As for three years within this period consecutively increased by 22% from 6 100 to 7 417;
 - (b) for the rental verification exercises conducted by RVD for each annual GR from 2010-2011 to 2015-2016, on average 67 (28%)

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of some 240 cases selected for verification each year were found to have provided incorrect rental information in Form R1As, suggesting that the accuracy of rateable values generated in GRs could be undermined by inaccurate rental information furnished in Form R1As;

- (c) RVD only selected ratepayers of multiple properties for conducting the rental verification exercises, which might not provide a complete picture of the accuracy of rental information obtained in Form R1As;
 - (d) for the GR of 2013-2014, RVD issued 3 189 Form R1As to all ratepayers in the 116 buildings which were found by BD to have 800 subdivided properties. However, of 2 244 Form R1As received, only 44 reported rental and subdivided unit information, suggesting that ratepayers might not be forthcoming in disclosing information on their subdivided properties; and
 - (e) RVD also obtains rental information from stamped tenancy agreements, and for each GR from 2010-2011 to 2015-2016, the number of stamped tenancy agreements copied by RVD increased from 18 099 to 26 187 (45% increase). This arrangement was not conducive to effective green management;
- notes that Commissioner of Rating and Valuation has generally agreed with Audit's recommendations in paragraph 2.16 of the Director of Audit's Report ("Audit Report");

Interim valuations

- expresses grave concern that the notification arrangements of UBWs established by RVD and BD since 2001-2002 have not been properly implemented to ensure the timely reassessment of properties with assessable UBWs to prevent loss of revenue as evidenced by the following:
 - (a) subsequent to the 2000-2001 policy decision, RVD has not taken actions on un-assessed illegal rooftop structures (since 2002) and other types of assessable UBWs (since 2005) with removal orders issued by BD, on the assumption that their existence would be transient. The 2002 departmental instruction of RVD

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had not reminded RVD staff to check whether the un-assessed illegal rooftop structures were new or re-erected before deciding not to take actions on these cases. Furthermore, there was no documentary evidence to indicate that before issuing the 2005 departmental instruction,¹⁸ RVD had ascertained from BD whether UBWs with removal orders issued could be removed shortly. RVD's presumption that after the issue of removal orders, the illegal rooftop structures/UBWs would be demolished soon turned out to be not always valid. Of 54 637 assessable UBWs cases with removal orders issued from 2001 to 2015, 16 304 (30%) had not been complied with as at 31 December 2015, with 10 192 having remained outstanding for two years or more;

- (b) there was no established arrangement for BD to notify RVD of assessable UBWs cases without removal orders issued, and the number of such cases totalled 59 032 from 2001 to 2015. Given the 24-month time-bar in recovering rates, there is a risk of loss of rates revenue if the rateable values of properties with assessable UBWs are not reassessed in a timely manner. Based on RVD's rating assessment records of 312 subdivided properties, the rateable values of properties with assessable subdivided units could increase by 5% to 217% (averaging 58%) upon reassessments; and
- (c) BD only instructed its staff to provide to RVD hardcopy of the removal orders for illegal rooftop structures and advertising signs but not for other types of assessable UBWs. Audit's test check of 85 selected removal orders revealed that only 7 (8%) were copied to RVD;

- expresses concern that:

- (a) RVD has not conducted any survey to identify un-assessed advertising signs since the last one in 2011. Of 100 selected advertising signs surveyed by Audit, 41 (41%) had not been assessed to rates; and

¹⁸ Similar to the 2002 version, the 2005 departmental instruction covering both illegal rooftop structures and other types of assessable UBWs also stipulated that RVD staff should not take any further action on un-assessed illegal rooftop structures/UBWs subjected to BD's removal orders.

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- (b) of 30 693 new interim valuations completed by RVD from April 2014 to September 2015, the assessment of 46 of them was not completed within the 24-month time-bar, resulting in a loss of revenue (estimated to be \$1 million before taking into account rates concessions given to ratepayers over the years). For 32 of the 46 interim valuations, the relevant documents required for initiating interim valuations were received by RVD, on average, 104 months after their effective dates of interim valuations;
- notes that:
 - (a) Commissioner of Rating and Valuation has generally agreed with Audit's recommendations in paragraph 3.40 of the Audit Report; and
 - (b) Director of Buildings has agreed to consider the feasibility of taking forward Audit's recommendations involving the sharing of information on UBWs with RVD;

Rates exemption for rural properties

- expresses grave concern that:
 - (a) RVD has not put in place compliance checking of rates-exempted village houses in DVAs to ensure that they meet the prescribed eligibility criteria;
 - (b) Audit's sample check of RVD records revealed that for government rent purposes, RVD had assessed 18 village houses within DVAs as four-storey or five-storey buildings from 1997 to 2009 but it had not taken actions to cancel their rates exemption for not complying with the prescribed three-storey criterion. Given the 24-month time-bar for recovering rates, rates for some 4 to 16 years had become irrecoverable for these 18 houses;
 - (c) HAD has set the effective date of revocation of rates exemption of village houses outside DVAs based on the date of notification by DLOs instead of the date of detection of UBWs by DLOs.

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Audit's sample check revealed that in two rates exemption revocation cases, the delay in notifying HAD had resulted in rates revenue loss of three-and-a-half and eight years respectively;

- (d) while the number of exemption cases outside DVAs had increased from 1 000 in 1998 to 19 000 in 2015, the number of cases selected for site inspections had remained at 180 a year. Audit's scrutiny of the field inspection results of 120 rates-exempted village houses outside DVAs revealed that 48 (40%) of them had UBWs, indicating a high incidence of ineligible cases; and
- (e) while RVD needs to identify those agricultural land and buildings which have become ineligible for rates exemption due to change of use, it has not established with LandsD notification arrangements for this purpose. Audit's test check of three cases of unauthorized structures on agricultural land to which LandsD had issued warning letters revealed that RVD had made interim valuation in one case while the other two cases were still exempted from assessment to rates;

- notes that:

- (a) Commissioner of Rating and Valuation has generally agreed with Audit's recommendations in paragraph 4.22 of the Audit Report;
- (b) Director of Home Affairs has agreed with Audit's recommendations in paragraph 4.23 of the Audit Report; and
- (c) Director of Lands will take appropriate actions to follow up on Audit's recommendations in paragraph 4.24 of the Audit Report;

Collection of rates and government rent

- expresses concern that for 10 of the 14 bona vacantia cases as at 30 September 2015, RVD took 7.5 years or more to refer them to LandsD for taking possession of the defaulting companies' properties; and

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and government rent*

- notes that Commissioner of Rating and Valuation has generally agreed with Audit's recommendations in paragraph 5.8 of the Audit Report.

<p>Follow-up action</p>

58. The Committee wishes to be kept informed of the progress made in implementing the various recommendations made by the Committee and Audit.